OFFERING CIRCULAR

Centrica plc

(incorporated with limited liability in England and Wales with registered number 03033654)

$750,000,000 4.000 per cent. Senior Notes Due 2023

$600,000,000 5.375 per cent. Senior Notes Due 2043

Issue Price: 99.292 per cent. of the principal amount of the 2023 Notes and 99.234 per cent. of the principal amount of the 2043 Notes

Centrica plc (the "Company") is issuing $750,000,000 4.000 per cent. senior notes due 2023 (the "2023 Notes") and $600,000,000 5.375 per cent. senior notes due 2043 (the "2043 Notes" and, together with the "2023 Notes", the "Notes") (the "Offering").

Interest on the Notes is payable semi-annually in arrears on 16 April and 16 October of each year, commencing on 16 April 2014. The 2023 Notes and the 2043 Notes will mature on 16 October 2023 and 16 October 2043, respectively (each, a "Maturity Date"). The Notes will be the Company's unsecured and unsubordinated obligations and will rank *pari passu* in right of payment among themselves and with all other unsecured and unsubordinated indebtedness of the Company (save for certain obligations required to be preferred by law). The Company may redeem the Notes in whole or in part at any time at the redemption prices specified herein. See "Description of the Notes—Optional Redemption". Upon the occurrence of certain change of control events, each holder of Notes shall have the option to require the Company to redeem or, at the Company's option, purchase all of such Notes at an amount equal to 101 per cent. of its principal amount together with accrued and unpaid interest to but excluding the date of redemption or purchase. See "Description of the Notes—Change of Control Investor Put". For a more detailed description of the Notes, see "Description of the Notes".

Investing in the Notes involves risks. For a discussion of these risks, see "Risk Factors" beginning on page 11.

The Notes have not been and will not be registered under the US Securities Act of 1933, as amended (the "Securities Act"), or any state or other securities laws, and the Notes are being offered only to "qualified institutional buyers" (as defined in Rule 144A under the Securities Act ("Rule 144A")) ("QIBs") under Rule 144A and outside the United States under Regulation S of the Securities Act ("Regulation S"). Prospective purchasers that are QIBs are hereby notified that the seller of the Notes may be relying on the exemption from the provisions of Section 5 of the Securities Act provided by Rule 144A. For a description of certain restrictions on transfer of the Notes, see "Transfer Restrictions".

The Initial Purchasers expect to deliver the Notes to purchasers in book-entry form through the facilities of The Depository Trust Company ("DTC"), and its participants, including Clearstream Banking, *société anonyme* ("Clearstream, Luxembourg") and Euroclear Bank S.A./N.V. ("Euroclear"), against payment in immediately available funds on or about 16 October 2013.

The Company has a solicited long-term debt rating of A3 stable outlook by Moody's Investors Service Ltd. ("Moody's") and A- stable outlook by Standard & Poor's Credit Market Services Europe Limited ("S&P"). It is expected that the Notes will be rated A3 stable outlook by Moody's and A- stable outlook by S&P only. Moody's and S&P are established in the European Union and are registered under Regulation (EC) No. 1060/2009 (as amended) (the "CRA Regulation"). A security rating is not a recommendation to buy, sell or hold securities and may be subject to suspension, change or withdrawal at any time by the assigning rating agency.

Application has been made to the UK Financial Conduct Authority under Part VI of the Financial Services and Markets Act 2000 (the "FSMA") (the "UK Listing Authority") for the Notes described in this offering circular (the "Offering Circular") to be admitted to the official list (the "Official List") of the UK Listing Authority and to the London Stock Exchange plc (the "London Stock Exchange") for the Notes to be admitted to trading on the London Stock Exchange's Regulated Market. References in this Offering Circular to Notes being "listed" (and all related references) shall mean that the Notes have been admitted to trading on the London Stock Exchange's Regulated Market and have been admitted to the Official List. The London Stock Exchange's Regulated Market is a regulated market for the purposes of Directive 2004/39/EC (the "Markets in Financial Instruments Directive").

Joint Book-Running Managers

Barclays	**BNP PARIBAS**	**Citigroup**	**Deutsche Bank Securities**
HSBC	**J.P. Morgan**	**RBS**	**Société Générale Corporate & Investment Banking**

11 October 2013

IMPORTANT: You must read the following before continuing. The following applies to this Offering Circular. You are therefore advised to read this carefully before reading, accessing or making any other use of this Offering Circular. In accessing this Offering Circular, you agree to be bound by the following terms and conditions, including any modifications to them any time you receive any information. This Offering Circular does not constitute an offer of any securities other than those to which it relates or an offer to sell, or solicitation of an offer to buy, to any person in any jurisdiction where such an offer or solicitation would be unlawful.

This Offering Circular comprises a prospectus for the purposes of Directive 2003/71/EC, as amended, to the extent that such amendments have been implemented in the relevant Member State of the European Economic Area (the "Prospectus Directive") and for the purpose of giving information with regard to the Company, the Company and its subsidiaries and affiliates taken as a whole and the Notes which, according to the particular nature of the Company and the Notes, is necessary to enable investors to make an informed assessment of the assets and liabilities, financial position, profit and losses and prospects of the Company. The Company (the "Responsible Person") accepts responsibility for the information contained in this Prospectus. To the best of the knowledge and belief of the Company (which has taken all reasonable care to ensure that such is the case), the information contained in this Offering Circular is in accordance with the facts and does not omit anything likely to affect the import of such information.

The Notes have not been registered with, or recommended or approved by, the US Securities and Exchange Commission (the "Commission") or any other federal or state securities commission or regulatory authority, nor has the Commission or any such other commission or regulatory authority passed upon the accuracy or adequacy of this Offering Circular. Any representation to the contrary is a criminal offence.

NOTICE TO NEW HAMPSHIRE INVESTORS

NEITHER THE FACT THAT A REGISTRATION STATEMENT OR AN APPLICATION FOR A LICENCE HAS BEEN FILED UNDER CHAPTER 421-B OF THE NEW HAMPSHIRE REVISED STATUTES ANNOTATED, 1955, AS AMENDED ("RSA 421-B") WITH THE STATE OF NEW HAMPSHIRE NOR THE FACT THAT A SECURITY IS EFFECTIVELY REGISTERED OR A PERSON IS LICENCED IN THE STATE OF NEW HAMPSHIRE CONSTITUTES A FINDING BY THE SECRETARY OF STATE THAT ANY DOCUMENT FILED UNDER RSA 421-B IS TRUE, COMPLETE AND NOT MISLEADING. NEITHER ANY SUCH FACT NOR THE FACT THAT AN EXEMPTION OR EXCEPTION IS AVAILABLE FOR A SECURITY OR A TRANSACTION MEANS THAT THE SECRETARY OF STATE HAS PASSED IN ANY WAY UPON THE MERITS OR QUALIFICATIONS OF, OR RECOMMENDED OR GIVEN APPROVAL TO, ANY PERSON, SECURITY OR TRANSACTION. IT IS UNLAWFUL TO MAKE, OR CAUSE TO BE MADE, TO ANY PROSPECTIVE PURCHASER, CUSTOMER OR CLIENT ANY REPRESENTATION INCONSISTENT WITH THE PROVISIONS OF THIS PARAGRAPH.

NOTICE TO INVESTORS IN JAPAN

The Notes have not been and will not be registered under the Securities and Exchange Law of Japan and are not being offered or sold and may not be offered or sold, directly or indirectly, in Japan or to or for the account of any resident of Japan, except (i) pursuant to an exemption from the registration requirements of the Securities and Exchange Law of Japan and (ii) in compliance with any other applicable requirements of Japanese law.

STABILISATION

In connection with the issue of the Notes, Barclays Capital Inc. (the "Stabilising Manager") (or any person acting on behalf of the Stabilising Manager) may over-allot Notes or effect transactions with a view to supporting the market price of the Notes at a level higher than that which might otherwise prevail. However, there is no assurance that the Stabilising Manager (or any person acting on behalf of the Stabilising Manager) will undertake stabilisation action. Any stabilisation action may begin on or after the date on which adequate public disclosure of the terms of the offer of the Notes is made and, if begun, may be ended at any time, but it must end no later than the earlier of 30 days after the issue date of the Notes and 60 days after the date of the allotment of the Notes. Any stabilisation action or over-allotment must be conducted by the relevant Stabilising Manager (or any person acting on behalf of the Stabilising Manager) in accordance with all applicable laws and rules.

IMPORTANT NOTICE

THIS OFFERING IS AVAILABLE ONLY TO INVESTORS WHO ARE EITHER (1) QIBs UNDER RULE 144A OR (2) NON-US PERSONS LOCATED OUTSIDE OF THE UNITED STATES IN ACCORDANCE WITH REGULATION S.

This Offering Circular is being provided on a confidential basis to QIBs in the United States and to non-US persons outside the United States for use solely in connection with the offering of the Notes. Its use for any other purpose is not authorised. This Offering Circular may not be copied or reproduced in whole or in part, nor may it be distributed nor any of its contents be disclosed to any person other than the prospective investors to whom it is being provided.

Prospective investors should note that there are further restrictions on the offering and sale of the Notes and the distribution of this Offering Circular. See "Plan of Distribution" and "Transfer Restrictions".

You should rely only on the information contained in this Offering Circular. The Company has not authorised anyone to provide you with different information. You should not assume that the information contained in this Offering Circular is accurate as at any date other than the date on the front of this Offering Circular. By receiving this Offering Circular, investors acknowledge that they have had an opportunity to request for review, and have received, all additional information they deem necessary to verify the accuracy and completeness of the information contained in this Offering Circular. See "Available Information".

Investors also acknowledge that they have not relied on the Initial Purchasers in connection with their investigation of the accuracy of this information or their decision on whether to invest in the Notes. The contents of this Offering Circular are not to be considered as legal, business or tax advice. Prospective investors should consult their own counsel, accountants and other advisers as to legal, tax, business, financial and related aspects of a purchase of the Notes.

In making an investment decision, investors must rely on their own examination of the Company and its respective affiliates, the terms of the offering of the Notes and the merits and risks involved. This offering is being made in reliance upon exemptions from registration under the Securities Act for an offer and sale of securities that does not involve a public offering. By purchasing the Notes, investors are deemed to have made the acknowledgements, representations, warranties and agreements set forth under "Transfer Restrictions".

Each potential investor in the Notes must determine the suitability of that investment in light of their own circumstances. In particular, each potential investor should:

- have sufficient knowledge and experience to make a meaningful evaluation of the merits and risks of investing in the Notes;
- have access to, and knowledge of, appropriate analytical tools to evaluate, in the context of their particular financial situation, an investment in the Notes and the impact such investment will have on their overall investment portfolio;
- have sufficient financial resources and liquidity to bear all of the risks of an investment in the Notes, including where principal or interest is payable in one or more currencies, or where the currency for principal or interest payments is different from the potential investor's currency;
- understand thoroughly the terms of the Notes and be familiar with the behaviour of any relevant indices and financial markets; and
- be able to evaluate (either alone or with the help of a financial adviser) possible scenarios for economic, interest rate and other factors that may affect their investment and their ability to bear the applicable risks.

Potential investors should not invest in the Notes unless they have the expertise (either alone or with the help of a financial adviser) to evaluate how the Notes will perform under changing conditions, the resulting effects on the value of such Notes and the impact this investment will have on the potential investor's overall investment portfolio. The investment activities of certain investors are subject to investment laws and regulations, or review or regulation by certain authorities and each potential investor should consult their legal advisers or the appropriate regulators.

The Initial Purchasers reserve the right to withdraw this Offering at any time and to reject any commitment to subscribe for the Notes, in whole or in part. The Initial Purchasers also reserve the right to allot less than the full amount of Notes sought by investors. The Initial Purchasers and certain related entities may acquire a portion of the Notes for their own account.

No action has been taken by the Initial Purchasers, the Company or any other person that would permit an offering of the Notes or the circulation or distribution of this Offering Circular or any offering material in relation to the Company or its affiliates or the Notes in any country or jurisdiction where action for that purpose is required.

The laws of certain jurisdictions may restrict the distribution of this Offering Circular and the offer and sale of the Notes. Persons into whose possession this Offering Circular or any of the Notes come must inform themselves about, and observe any such restrictions. None of the Company, the Initial Purchasers or their respective representatives is making any representation to any offeree or any purchaser of the Notes regarding the legality of any investment in the Notes by such offeree or any purchaser under applicable legal investment or similar laws or regulations. Accordingly, no Notes may be offered or sold, directly or indirectly, and neither this Offering Circular nor any advertisement or other offering material may be distributed or published in any jurisdiction, except under circumstances that will result in compliance with any applicable laws and regulations. Persons into whose possession this Offering Circular or any Notes may come must inform themselves about, and observe any such restrictions on the distribution of this Offering Circular and the offering and sale of the Notes. In particular, there are restrictions on the distribution of this Offering Circular and the offer or sale of the Notes in the United States, the EEA (including the United Kingdom) and Japan. For a further description of certain restrictions on the offering and sale of the Notes and the distribution of the Offering Circular, see "Plan of Distribution" and "Transfer Restrictions".

To purchase the Notes, investors must comply with all applicable laws and regulations in force in any jurisdiction in which investors purchase, offer or sell the Notes or possess or distribute this Offering Circular. Investors must also obtain any consent, approval or permission required by such jurisdiction for investors to purchase, offer or sell any of the Notes under the laws and regulations in force in any jurisdiction in which investors are subject or in which investors make such purchase, offer or sale. None of the Company, its affiliates or the Initial Purchasers will have responsibility therefor.

SERVICE OF PROCESS AND ENFORCEMENT OF CIVIL LIABILITIES

The Company is a public limited company incorporated under the laws of England and Wales. The majority of the directors and executive officers of the Company are resident outside of the United States and a substantial portion of their assets are located outside of the United States. Although the Company has agreed, in accordance with the terms of the fiscal and paying agency agreements governing each series of Notes (together, the "Fiscal and Paying Agency Agreements"), to accept service of process in the United States by agents designated for such purpose, it may not be possible for holders of the Notes (a) to effect service of process upon the Company or its directors or officers or (b) to enforce judgments of courts of the United States predicated upon the civil liability of such entity or persons under the US securities laws against any such entity or persons in the courts of a foreign jurisdiction.

AVAILABLE INFORMATION

The Company has agreed that, for so long as any Notes are "restricted securities" within the meaning of Rule 144(a)(3) under the Securities Act, the Company will, during any period in which the Company is neither subject to Section 13 or 15(d) of the US Securities Exchange Act of 1934, as amended (the "Exchange Act"), nor exempt from reporting pursuant to Rule 12g3-2(b) thereunder, provide to any holder or beneficial owner of such restricted securities or to any prospective purchaser of such restricted securities designated by such holder or beneficial owner upon the request of such holder, beneficial owner or prospective purchaser, the information required to be provided by Rule 144A(d)(4) under the Securities Act.

CERTAIN DEFINITIONS

Unless the context requires otherwise, references to the "Company" or the "Issuer" are to Centrica plc and references to the "Group" or "Centrica" are to the Company together with its consolidated subsidiaries. For definitions of other terms used in this Offering Circular, see "Glossary".

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OVERVIEW

The following overview is qualified in its entirety by, and should be read in conjunction with, the more detailed information appearing elsewhere in this Offering Circular. Capitalised terms used but not defined in this overview are defined in the text of this Offering Circular. Investors should thoroughly consider this Offering Circular in its entirety, including the information set forth under "Risk Factors", prior to an investment in the Notes.

Overview of the Group

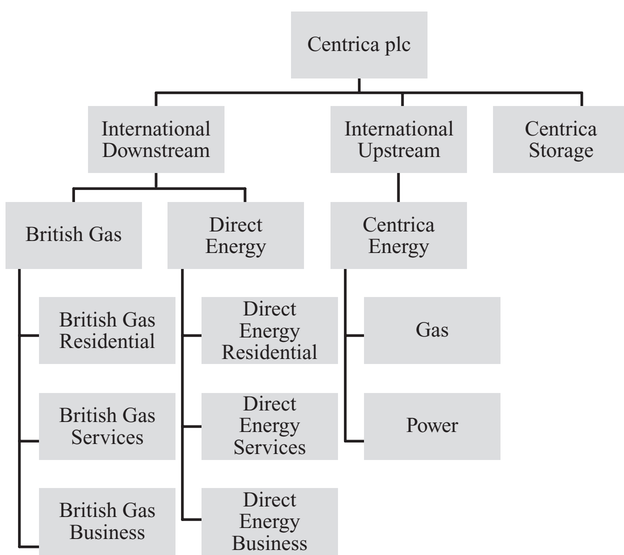
The Group is an integrated energy company that produces, sources and supplies gas and electricity for millions of residential and business customers in the United Kingdom and North America. The Group also provides a range of energy services solutions to its residential and business customers, including installation, maintenance, service and repair contracts, low-carbon and energy efficient products. Centrica was listed in 1997 on the London Stock Exchange following the demerger of the gas supply, service and retail businesses of British Gas plc together with its Morecambe gas field production activities. Since 1997, the Group has evolved significantly, shifting its primary focus from downstream activity in the initial years after listing towards becoming a leading integrated energy company in its chosen markets. The Group seeks to operate across the energy value chain from upstream production to downstream supply, although it focuses its operations on price-deregulated markets.

The Group's operations are broadly divided into three categories: International Downstream (British Gas in the United Kingdom and Direct Energy in North America), International Upstream (Centrica Energy) and Centrica Storage.

International Downstream operations involve the supply of energy to residences and businesses in the United Kingdom (excluding Northern Ireland) and North America and the provision of energy-related services to customers, including installation, maintenance, service and repair contracts, insurance and low carbon and energy efficient products. The Group's downstream operations principally operate under the British Gas and Direct Energy brands in the United Kingdom (excluding Northern Ireland) and North America, respectively.

International Upstream operations comprise exploration, development, production and processing of natural gas and oil assets and power generation. They also include the transaction of major procurement contracts to source gas from around the world for the UK and North American markets, and energy trading activities. The Group's upstream assets located in the UK, Canada, Norway, the Netherlands and Trinidad and Tobago, and procurement contracts provide a stable supply of gas and power to its downstream operations, which in turn, provide a market for the Group's upstream production.

Centrica Storage sells capacity in its Rough gas storage facility, along with ancillary services to customers who typically inject gas in the summer and withdraw during the winter for the UK market. The following chart summarises the Group's business structure:



Strengths and Strategy

Strengths

The Group believes that it has the following key strengths:

Downstream scale and energy services

The Group benefits from the scale and strength of its downstream operations in the United Kingdom. Its principal brand, British Gas, was originally the market incumbent in gas supply and as of 30 June 2013 had approximately 16.6 million residential and business gas and electricity accounts. The Group also had approximately four million energy services customers with 8.3 million product holdings. British Gas is the leading residential energy and services provider in Britain by number of accounts.

The Group believes that the combination of its high profile brand, large scale, good customer service levels and unique energy services offering is a key differentiating factor from many of its large competitors in the UK market. In North America, the Group is a large supplier of energy to residential customers in price-deregulated markets.

Integrated business model

The Group is an integrated energy company with both upstream and downstream operations in multiple geographies. High-quality upstream assets and procurement contracts provide a stable supply of gas and power to its downstream operations, which in turn provide a market for the Group's upstream production. The Upstream business provides a natural economic hedge against exposure to energy price movements.

Upstream optionality

The Group maintains a low level of committed capital expenditure. Although it requires a certain level of capital expenditure to maintain upstream gas production, this can be adjusted in response to a variety of factors, including commodity prices and changes in risk profile.

Financial strength

The Group benefits from a strong balance sheet, stable cash flow and an investment grade credit rating. This financial strength has been beneficial to the Group in different areas. It has reduced funding costs, limited the amount of collateral required to access key commodity markets and contributed to the Group's ability to enter into agreements with key partners, including multi-year supply agreements with Statoil and Qatargas and, together with Qatar Petroleum International, the acquisition of natural gas and crude oil assets in Canada.

Strategy

The Group's vision is to be the leading integrated energy company in its chosen markets, with customers at its core. In February 2013, the Group announced refreshed strategic priorities to position it for future growth, and moved to an international functional organisation with a new management structure aligned to its core competencies of upstream and downstream operations.

Innovate to drive service excellence and growth

The Group's downstream operations are at the core of its business. In order to maintain a market-leading position in its key markets, the Group aims to innovate and lead with high quality service and efficient operations. These goals are supported by the Group's technological capabilities, with the aim of enabling its customers to control their energy use in a simpler, more efficient way. The Group intends to build on its leading capabilities, facilitating growth in its selected markets, in the UK and particularly in North America, through a combination of organic growth and acquisitions.

Integrate its natural gas business, linked to its core markets

The Group's upstream business owns interests in gas and oil assets, and power assets. The Group intends to grow and diversify its gas and oil exploration and production portfolio and intends to maintain a low-carbon power hedge, investing where it sees value. The upstream business also plays an important role in managing the energy requirements of downstream customers, and the Group intends to develop its midstream business to integrate along the gas value chain.

Increase its returns through efficiency and continued capital discipline

The Group intends to continue developing organisational capability to optimise its resources to focus continually on safety, with the aim of delivering value to shareholders through efficient deployment of capital.

Overview of the Offering

The overview below describes the principal terms of the Notes. Certain of the terms and conditions described below are subject to important limitations and exceptions. The "Description of the Notes" section of this Offering Circular contains a more detailed description of the terms and conditions of the Notes. Terms used in this overview and not otherwise defined herein have the meanings given to them in "Description of the Notes".

Company	Centrica plc, a public limited company incorporated under the laws of England and Wales. Its registered office and the business address of each of its directors is Maidenhead Road, Windsor, Berkshire, SL4 5GD, United Kingdom, and its telephone number is +44 1753 494 000.
The Notes	$750,000,000 4.000 per cent. senior Notes due 2023 and $600,000,000 5.375 per cent. senior Notes due 2043.
	The Notes will be issued under the Fiscal and Paying Agency Agreements between the Company and Citibank, N.A., London Branch (collectively in its capacities as fiscal agent, paying agent, transfer agent and registrar, the "Fiscal and Paying Agent").
Issue Price	99.292 per cent. of the principal amount of the 2023 Notes and 99.234 per cent. of the principal amount of the 2043 Notes.
The Offering	The Notes are being offered and sold by the Initial Purchasers (i) within the United States only to QIBs in reliance on Rule 144A and (ii) outside the United States to persons other than US persons in reliance on Regulation S.
Issue Date	16 October 2013.
Maturity Date	The 2023 Notes will mature on 16 October 2023 and the 2043 Notes will mature on 16 October 2043. The Notes are redeemable prior to maturity as described under "Description of the Notes—Optional Redemption", "Description of the Notes—Change of Control Investor Put" and "Description of the Notes—Redemption for Tax Reasons".
Interest Rate	The 2023 Notes will bear interest from the Issue Date at the rate of 4.000 per cent. per annum, payable semi-annually in arrears.
	The 2043 Notes will bear interest from the Issue Date at the rate of 5.375 per cent. per annum, payable semi-annually in arrears.
Interest Payment Dates	Interest on the Notes will be paid semi-annually in arrears on 16 April and 16 October of each year, beginning on 16 April 2014 (each, an "Interest Payment Date").
Interest Periods	The first interest period for the Notes will be the period from and including the Issue Date to, but excluding, the first Interest Payment Date. Thereafter, the interest periods for the Notes will be the periods from and including each Interest Payment Date to but excluding the immediately succeeding Interest Payment Date. The final interest period will be the period from and including the Interest Payment Date immediately preceding the Maturity Date to and including the Maturity Date.
Regular Record Dates	The close of business on 1 April or 1 October (whether or not a Business Day) immediately preceding each Interest Payment Date.

Business Day	Any day which is not, in London, England or New York, or any other Place of Payment, a Saturday, Sunday, legal holiday or a day on which banking institutions are authorised or obliged by law or regulation to close (a "Business Day").
Optional Redemption	The Company may redeem any series of Notes in whole or in part, at the Company's option, at any time and from time to time at a redemption price equal to (i) if such redemption occurs prior to 16 July 2023 in the case of the 2023 Notes or 16 April 2043 in the case of the 2043 Notes, the greater of (a) 100 per cent. of the principal amount of the Notes to be redeemed and (b) as determined by the Independent Investment Banker, the sum of the present values of the applicable Remaining Scheduled Payments discounted to the date of redemption (the "Redemption Date") on a semi-annual basis (assuming a 360 day year consisting of twelve 30 day months or, in the case of an incomplete month, the number of days elapsed) at the Treasury Rate plus 25 basis points in the case of the 2023 Notes and 25 basis points in the case of the 2043 Notes, or (ii) if such redemption occurs on or after 16 July 2023 in the case of the 2023 Notes or 16 April 2043 in the case of the 2043 Notes, 100 per cent. of the principal amount of the Notes to be redeemed, together, in each case, with accrued and unpaid interest on the principal amount of the Notes to be redeemed to but excluding the Redemption Date.
Change of Control Investor Put	If a Put Event (as described under "Description of the Notes—Change of Control Investor Put") occurs, unless the Company has redeemed the Notes in full, the Holder of each applicable Note will have the option (the "Put Option") to require the Company to redeem or, at the Company's option, purchase all of that Holder's Notes at an amount equal to 101 per cent. of the aggregate principal amount of such Notes, plus accrued and unpaid interest, if any, on such Notes, to but excluding the date of redemption or purchase.
Redemption for Tax Reasons	In the event of a Change in Tax Law that would require the Company to pay Additional Amounts on the Notes, the Company may, under certain conditions, redeem in whole, but not in part, the Notes prior to maturity at a redemption price equal to 100 per cent. of the principal amount of the Notes to be redeemed plus accrued and unpaid interest to the date of redemption.
Payment of Additional Amounts	If the Company is required by a Tax Jurisdiction to deduct or withhold taxes in respect of any payment on the Notes, the Company will, subject to certain exceptions, pay additional amounts to Noteholders.
Covenants	The Company has agreed to certain covenants with respect to the Notes, including a negative pledge and limitation on mergers, consolidations, amalgamations and combinations. See "Description of the Notes—Covenants".
Ranking of the Notes	The Notes will be unsecured and unsubordinated obligations of the Company (except for the provisions of "Description of the Notes—Covenants—Negative Pledge") and will rank *pari passu* in right of payment among themselves and with all other unsecured and unsubordinated indebtedness of the Company (save for certain obligations required to be preferred by law).

Denominations, Form and Registration of the Notes	The Notes will be issued in fully registered form and only in denominations of $200,000 and integral multiples of $1,000 in excess thereof. The Notes will be initially issued as global notes. DTC will act as depositary for the Notes. Except as set forth herein, global notes will not be exchangeable for certificated Notes. The global notes will be deposited with Citibank N.A., London Branch as custodian (the "Custodian") for DTC and registered in the name of Cede & Co., as nominee of DTC. The Notes sold to QIBs in the United States in reliance on Rule 144A will be represented by the Rule 144A Global Note. The Notes sold outside the United States to persons other than US persons in reliance on Regulation S will be represented by the Regulation S Global Note.
Governing Law of the Notes and the Fiscal and Paying Agency Agreements	The State of New York.
Listing	Application has been made to obtain the listing of the Notes on the Official List of the United Kingdom Listing Authority and for the admission of the Notes to trading on the Regulated Market of the London Stock Exchange.
Defeasance	The Notes will be subject to defeasance and covenant defeasance provisions in the Fiscal and Paying Agency Agreements.
Further Issuances	The Company may, subject to certain conditions, from time to time, without notice to or the consent of the Noteholders, "reopen" any series of Notes and create and issue additional notes having identical terms and conditions as to the applicable series of Notes (or in all respects except for the issue date, issue price, payment of interest accruing prior to the issue date of such additional notes and/or the first payment of interest following the issue date of such additional notes), so that the additional notes are consolidated and form a single series of notes with the applicable series of Notes, as the case may be.
Use of Proceeds	The total net proceeds of the Offering, after underwriting commissions, are expected to be approximately $1,331,469,000. The Group will use the net proceeds of the Offering for general corporate purposes, which may include (i) financing announced acquisitions; (ii) refinancing indebtedness originally incurred to finance acquisitions made by the Group or (iii) refinancing other outstanding indebtedness. For more information, see "Use of Proceeds" and "Capitalisation and Indebtedness".
Fiscal and Paying Agent	Citibank, N.A., London Branch
Transfer Restrictions	The Notes have not been and will not be registered under the Securities Act and may not be offered or sold, except pursuant to an exemption from, or in a transaction not subject to, the registration requirements of the Securities Act and in compliance with all applicable laws. The Notes are subject to certain restrictions on resale and transfer. See "Transfer Restrictions".

Timing and Delivery	The Company expects delivery of the Notes to occur on 16 October 2013.
Ratings	It is expected that the Notes will be rated A3 stable outlook by Moody's Investors Service Ltd. and A− stable outlook by Standard & Poor's Credit Market Services Europe Limited. A security rating is not a recommendation to buy, sell or hold the Notes. There is no assurance that a rating will remain for any given period of time or that a rating will not be lowered or withdrawn by the relevant rating agency if, in its judgment, circumstances in the future so warrant. In the event that a rating initially assigned to the Notes is subsequently lowered for any reason, no person or entity is obliged to provide any additional support or credit enhancement with respect to the Notes and the market value of the Notes is likely to be adversely affected.

Summary Historical Financial Information of the Group

The following summary historical financial data of the Group is derived from, and should be read in conjunction with, the unaudited consolidated financial statements for the six months ended 30 June 2013 and the consolidated financial statements as of and for the years ended 31 December 2012, 2011 and 2010 and the accompanying notes thereto, all of which are included elsewhere in this Offering Circular.

This Offering Circular contains some measures which are not accounting measures within the scope of IFRS and which the Group uses to assess the financial performance of its businesses. These measures include adjusted operating profit, adjusted earnings, adjusted operating profit margin, EBITDA, net debt, working capital movements, margin calls, net capital expenditure, payments to shareholders, and foreign exchange and other. These non-IFRS measures have been included because the Directors believe that they are helpful to investors in assessing the historical financial performance of the Group. These are not measures of operating performance derived in accordance with IFRS, and should not be considered a substitute for gross profit, operating profit, profit/(loss) before tax, cash flow from operating activities or other income or cash flow statement data as determined in accordance with IFRS, or as a measure of profitability or liquidity. The Group's calculation of adjusted operating profit, adjusted earnings, adjusted operating profit margin, EBITDA, net debt, working capital movements, margin calls, net capital expenditure, payments to shareholders, and foreign exchange and other may be different from the calculation used by other companies and therefore comparability may be limited.

The summary financial and operating data set forth below should be read in conjunction with "Presentation of Financial and Other Information", "Selected Historical Financial Information", "Operating and Financial Review", and the Consolidated Financial Statements and the accompanying notes thereto, each of which is included elsewhere in this Offering Circular. See "Presentation of Financial and Other Information" for the Group's definition of "Business performance", "Exceptional items", "Certain re-measurements", "Adjusted earnings", "EBITDA" and other non-IFRS financial measures.

Income Statement Data

The following table sets out the Group's financial performance for the six months ended 30 June 2013 and 2012 and the years ended 31 December 2012, 2011 and 2010:

	Six months ended 30 June						Year ended 31 December								
	2013			2012			2012			2011			2010		
	Business performance	Exceptional items and certain re-measure-ments	Statutory result	Business performance	Exceptional items and certain re-measure-ments	Statutory result	Business performance	Exceptional items and certain re-measure-ments	Statutory result	Business performance	Exceptional items and certain re-measure-ments	Statutory result	Business performance	Exceptional items and certain re-measure-ments	Statutory result
	(£m) (unaudited)						(£m)								
Group revenue	**13,651**	**—**	**13,651**	**11,977**	**—**	**11,977**	**23,942**	**—**	**23,942**	**22,824**	**—**	**22,824**	**22,423**	**—**	**22,423**
Cost of sales	(10,886)	104	(10,782)	(9,445)	513	(8,932)	(18,676)	514	(18,162)	(17,959)	(658)	(18,617)	(17,595)	1,075	(16,520)
Gross profit	**2,765**	**104**	**2,869**	**2,532**	**513**	**3,045**	**5,266**	**514**	**5,780**	**4,865**	**(658)**	**4,207**	**4,828**	**1,075**	**5,903**
Operating costs	(1,332)	—	(1,332)	(1,244)	(90)	(1,334)	(2,844)	(445)	(3,289)	(2,750)	(110)	(2,860)	(2,641)	(181)	(2,822)
Share of profits/(losses) in joint ventures and associates, net of interest and taxation	52	1	53	58	(2)	56	140	(6)	134	93	(26)	67	7	(14)	(7)
Group operating profit	**1,485**	**105**	**1,590**	**1,346**	**421**	**1,767**	**2,562**	**63**	**2,625**	**2,208**	**(794)**	**1,414**	**2,194**	**880**	**3,074**
Net finance cost	(103)	—	(103)	(102)	—	(102)	(183)	—	(183)	(146)	—	(146)	(265)	—	(265)
Taxation	(649)	(19)	(668)	(521)	(168)	(689)	(1,029)	(140)	(1,169)	(810)	(16)	(826)	(708)	(221)	(929)
Profit from continuing operations after taxation	**733**	**86**	**819**	**723**	**253**	**976**	**1,350**	**(77)**	**1,273**	**1,252**	**(810)**	**442**	**1,221**	**659**	**1,880**
Discontinued operations	—	—	—	—	—	—	—	—	—	13	(34)	(21)	(5)	67	62
Profit for the period	**733**	**86**	**819**	**723**	**253**	**976**	**1,350**	**(77)**	**1,273**	**1,265**	**(844)**	**421**	**1,216**	**726**	**1,942**
Earnings attributable to non-controlling interests	—	—	—	—	—	—	—	—	—	—	—	—	(7)	—	—
Depreciation of fair value uplifts from Strategic Investments, after taxation	34			30			56			68			88		
Adjusted earnings	**767**			**753**			**1,406**			**1,333**			**1,297**		

Balance Sheet Data

The following table summarises the Group's financial position as of 30 June 2013 and as of 31 December 2012, 2011 and 2010:

	As of 30 June	As of 31 December		
	2013	2012	2011	2010
	(£m) (unaudited)		(£m)	
Total non-current assets	15,822	15,812	13,973	13,269
Total current assets	6,022	6,140	5,596	5,551
Total assets	**21,844**	**21,952**	**19,569**	**19,275**[1]
Total non-current liabilities	9,737	9,439	7,699	7,820
Total current liabilities	6,243	6,586	6,270	5,268
Total liabilities	**15,980**	**16,025**	**13,969**	**13,088**
Total equity	**5,864**	**5,927**	**5,600**	**5,819**

Note:

(1) Total assets for the year ended 31 December 2010 include £455 million of assets held for sale at that date.

Cash Flow Statement Data

The following table summarises the Group's cash flows for the six months ended 30 June 2013 and 2012 and for the years ended 31 December 2012, 2011 and 2010:

	Six months ended 30 June		Year ended 31 December		
	2013	2012	2012	2011	2010
	(£m)	(unaudited)		(£m)	
Net cash inflow from operating activities	1,411	1,032	2,820	2,337	2,428
Net cash outflow from investing activities	(647)	(1,443)	(2,558)	(1,400)	(1,584)
Net cash (out)/inflow from financing activities	(897)	888	190	(907)	(1,677)
Net (decrease)/increase in cash and cash equivalents	(133)	477	452	30	(833)
Cash and cash equivalents	800	954	931	479	451

Other key metrics

The following table sets out certain other key financial metrics of the Group for the six months ended 30 June 2013 and 2012 and the years ended 31 December 2012, 2011 and 2010:

	Six months ended 30 June		Year ended 31 December		
	2013	2012	2012	2011	2010
		(£m)	(unaudited)		
EBITDA[1]	2,112	1,773	3,650	3,128	3,181
Net debt[2]	(4,251)	(4,341)	(4,047)	(3,292)	(3,195)
Net debt to EBITDA ratio[3]	2.01	2.45	1.11	1.05	1.00
Interest cover ratio[4]	18.2	24.0	17.4	16.2	10.9

Notes:

(1) EBITDA is defined as operating profit before exceptional items and certain re-measurements, and before amortisation, depreciation and impairments, and share of profits/(losses) in joint ventures and associates, net of taxation. See "Presentation of Financial and Other Information—Non-IFRS Financial Measures" above for further detail on the use of EBITDA as a non-IFRS financial measure and a reconciliation thereof.

(2) The Group defines net debt as current and non-current borrowings, less cash and cash equivalents, less current and non-current securities, less mark-to-market values on derivatives used to hedge offsetting movements in borrowings. See "Selected Historical Financial Information" for a reconciliation of net debt.

(3) Net debt to EBITDA ratio is calculated as Net debt divided by EBITDA.

(4) Interest cover ratio is calculated as EBITDA divided by Net financing interest paid.

RISK FACTORS

An investment in the Notes entails risks. There are a number of factors, including those specified below, that may adversely affect the Group's ability to make payments under the Notes. You could therefore lose a substantial portion or all of your investment in the Notes. Consequently, an investment in the Notes should be considered only by persons who can assume such risk. The risks described below are all risks the Group considers to be material. However, there may be additional risks that the Group currently considers immaterial or of which the Group is currently unaware, and the Group's business, financial condition and results of operations could be materially adversely affected by any of these risks. Prospective investors should also read the detailed information set out elsewhere in this Offering Circular and reach their own views prior to making any investment decision.

Risks related to Centrica's business

The Group is exposed to movement in commodity prices

A significant proportion of the Group's financial performance is dependent upon its ability to manage exposure to wholesale commodity prices for gas, oil, coal, carbon and power, all of which have been volatile in recent years. The Group's operations and profitability depend on commodity prices across all parts of its business.

In the downstream businesses, longer-term commodity price increases or decreases may require the Group to change the price at which it sells energy to its customers on variable tariffs. The Group may not be able to pass through all increases in commodity prices to its customers. When commodity prices fall, the Group may experience pressure to reduce prices and margins for downstream customers. Where the Group does pass increased commodity prices through to its customers or fails to pass on decreased commodity prices, those customers may seek to switch to competitors. In the United States, the low cost of natural gas may present new risks to the Group as barriers to entry are lowered and margins tightened requiring cost cutting and development of innovative products to maintain market share.

In the upstream production businesses, commodity price decreases may reduce gas and oil production profits, and over the longer term may make certain exploration and development projects uneconomic. In upstream power, higher gas prices will put pressure on profits from gas-fired power plants, and lower power prices will reduce profits from gas-fired, nuclear and wind generation assets. In UK electricity generation, as is common in other European markets, the combination of power, gas and European Union (EU) emissions prices means that the opportunities to run the Group's fleet of gas-fired power stations are currently limited.

In the midstream business, an uncertain price environment creates a risk that surplus commodity positions cannot profitably be sold to the wholesale markets and that any commodity short position cannot be covered at a cost that can be passed on to customers. The Group also has a number of contractual capacity contracts, the economic value of which depends on certain price relationships.

In Centrica Storage, profits depend on the difference between summer and winter gas prices in the UK (summer/winter "spreads"). A narrowing of these spreads over recent years has reduced levels of profitability for Centrica Storage, and further narrowing of these spreads would have an adverse impact on the profitability of the Storage business.

In addition, both investment decisions and the valuation of existing assets are based upon evaluations underpinned by forecasts of longer-term commodity prices. Assets, including goodwill, may be impaired if discounted future cash flows from such assets are insufficient to cover their cost on the balance sheet.

Commodity prices fluctuate based on a large number of factors, most notably forecasts for supply and demand in local and global markets as well as political and economic factors. Seasonal variations and, in the short-to-medium term, economic conditions, make it difficult to forecast future energy demand. Political factors include unrest in the Middle East which may trigger an expectation of disruptions in supplies from the region. In recent years, there has also been significant investment in shale gas in North America resulting in lower wholesale gas prices and a weakening of the traditional links between gas and oil prices. This emerging energy source could further influence global energy markets over time and, in particular, the surplus of gas could affect the current liquefied natural gas ("LNG") sector, which is becoming an increasingly important source of natural gas in the United Kingdom. If the Group is unable to successfully manage its exposure to fluctuating commodity prices, its competitive position could be negatively impacted and its business, financial condition and results of operations could be adversely affected.

The Group's business is subject to political intervention and regulatory oversight

The Group is subject to various political and regulatory interventions implemented by the governments and regulatory bodies in both the UK and North America. Objectives of these regulatory interventions vary, but include carbon emission reduction, security of energy supplies, and protection of consumers and business customers.

The Group is subject to oversight from a wide range of regulatory bodies including the Office of Gas and Electricity Markets ("Ofgem"), the Competition Commission, the Financial Conduct Authority ("FCA") and the Prudential Regulatory Authority ("PRA") in the United Kingdom, the Federal Energy Regulatory Commission ("FERC") in the United States and a number of regulators at state and federal level in the United States and Canada. Regulatory bodies have the power to amend licences, conduct investigations into companies' operations, and issue fines and enforcement notices. In certain cases, regulators have the power to impose very substantial fines, in some cases up to 10 per cent. of Group revenue. While fines imposed to date by regulators on the Group and close competitors have not come close to these levels, future fines may be greater.

In the downstream business, the Group is facing heightened levels of scrutiny from regulators, and other key stakeholders, including governments and consumer groups following rising energy bills and levels of public distrust in energy companies. For example, in the United Kingdom final proposals published by Ofgem in June 2013 following their Retail Market Review ("RMR") underlined a growing pressure to increase regulation of energy suppliers. The requirements in the RMR could affect the way the Group structures its retail tariffs. Ofgem's Standards of Conduct ("SOC") were published in August 2013, and have been introduced into licences with guidance required as to how these will be enforced. In addition, the leader of the principal opposition party has indicated that it would pursue a policy of further regulation of the energy industry if such party were to form a UK government following the next general election, which must occur by May 2015. The policy proposals include the imposition of a price freeze from May 2015 to early 2017 and the separation, in some way, of ownership of power generation and supply. Although there is uncertainty regarding how or if these proposals would be implemented, the heightened level of political discussion in periods preceding the election may lead to increased pressure for increased regulation of energy suppliers.

The UK upstream and downstream businesses have also seen regulators impose significant obligations to implement carbon reduction measures. The Energy Companies Obligation ("ECO") came into effect as of January 2013. The Group expects its obligations under ECO to cost approximately £1.4 billion through to the end of the programme in March 2015. There is a risk that the assumptions underlying the Group's estimates may change or may prove to be incorrect. In addition, there may be changes to the UK government's policy regarding carbon emissions or a lack of industry capacity or customer uptake. Any of the aforementioned may result in a substantial increase in the estimated cost to fulfil the Group's obligations, which, to the extent that such costs cannot be adequately passed through to customers, could have an adverse impact on the Group's results of operations and financial condition. There is also no assurance that the speed at which the Group implements its ECO obligations will be sufficient to meet the ECO targets, which could also harm the Group's reputation and have an adverse effect on its results of operations and financial condition. The Group was unable to meet its obligations under the Community Energy Saving Programme ("CESP") scheme, and to a lesser extent, under the Carbon Emissions Reduction Target ("CERT") scheme, which were predecessors of ECO, by the appointed deadlines. As a result, Ofgem could choose to levy a fine against the Group.

The UK downstream business is also affected by changes to the retail supply and wholesale industry procedures, which could have an impact on the Group's operating costs. Ofgem published a decision in May 2012 confirming its support for a gradual change to electricity network access rates and requesting that the network manager, National Grid Electricity Transmission Company, submit various options for such change. Any material increases in the regulated charges which the Group pays for use of transmission, distribution, network price controls and other infrastructure may also impact the Group's margins, to the extent that any such increases cannot be passed on to its customers.

In North America, regulatory approaches vary by jurisdiction and regulator. Although the Group operates primarily in price-deregulated markets in North America, it is subject to certain regulations and oversight by regulatory agencies in Direct Energy's principal residential energy markets, primarily Texas, the northeastern United States, and the Canadian provinces of Ontario and Alberta, as well as federal regulators, such as FERC. These regulators have proposed, and may propose in the future, measures to reduce greenhouse gas and other carbon emissions at the state, provincial and federal levels.

In the UK power generation business, key elements of the UK government's initiative to increase investment in low carbon infrastructure are set out in the Electricity Market Reform ("EMR") draft energy bill 2012 (due for Royal Assent by the end of 2013). There is uncertainty regarding how EMR will affect the market in general and the Group's business in particular, but the effects may change the generation mix in the UK and adversely affect the profitability of the Group's existing generation assets.

In the Group's upstream and midstream businesses, energy markets in the United Kingdom, North America and mainland Europe are closely regulated and significant changes to the legal or regulatory framework of these markets could have an impact on the Group's ability to achieve its operational or financial goals. In the United States there is the risk that LNG exports to non-Free Trade Agreement countries, such as the United Kingdom, will not be approved or that limitations may be imposed on such exports.

Following the acquisition by the Group of the Rough facility and a subsequent Competition Commission inquiry, undertakings were given by the Group and Centrica Storage to the Secretary of State for Trade and Industry in 2003 which place certain obligations on Centrica Storage and the Group in respect of the storage business. The undertakings require Centrica Storage to be legally, financially and physically separate from all other Centrica businesses. In addition, there are restrictions prohibiting the disclosure by Centrica Storage of commercially sensitive information to other parts of the Group and prohibiting the solicitation or making use of such information by other parts of the Group. In March 2012, the Company and Centrica Storage signed amended undertakings with certain variations. Any failure to comply with these undertakings could result in substantial fines for the Group.

Consequently, political and regulatory developments affecting the energy markets within which the Group operates are uncertain and may have a material adverse effect on the Group's business, results of operations and financial condition. Government intervention in energy markets, or changes in government policy, may also affect the Group's ability to invest in new assets in the markets concerned. Additionally, any failure or perceived failure by the Group to comply with such developments or related requirements could result in substantial fines or have a negative impact on its brands, operations and reputation.

Damage to corporate reputation or brand perception could affect the Group's competitive position

The Group must actively manage its reputation with a number of different stakeholders including customers, investors, opinion-formers, employees, the media, governments and government agencies, other political parties and regulatory and trade union bodies. A failure to follow the Group's global business principles of operating professionally, fairly and with integrity, or public perception that there has been such a failure, could undermine public trust in the Group, lead to increased regulatory intervention, harm the Group's reputation, damage its consumer brands and adversely affect its business, results of operations and financial condition.

Rising prices, increased political pressures and recessionary impacts have all increased the level of media coverage of the energy industry, particularly in the UK. The increased use of social media also allows customers and consumer groups to engage in direct action and other campaigns more readily than before. In addition, British Gas, as the United Kingdom's leading residential energy and services provider by number of customer accounts, may be subject to heightened scrutiny by the media, in particular regarding compliance with its regulatory obligations and its retail energy pricing policies. The increased level of media coverage may result in additional or heightened government and regulatory scrutiny. In North America, the Group operates under numerous brands, each of which faces the risk of heightened media scrutiny and/or adverse media coverage, which could have a negative impact on the reputation of one or more of the individual brands and, ultimately, the Group.

In June 2013, the Group acquired a 25 per cent. interest in a shale exploration licence with Cuadrilla Resources Ltd and AJ Lucas. This move into hydraulic fracturing or "fracking", together with the award of an exploration licence in Norwegian Arctic waters, has the potential to cause significant adverse publicity affecting the brand and reputation of the Group. The Group intends to continue to explore opportunities for unconventional energy supply and generation as part of its business strategy. Any investment in unconventional energy or related technology may expose the Group to adverse publicity and adversely affect its business, results of operation and financial condition.

The loss of rights to use trademarks and logos could affect the Group's competitive position

As part of the demerger of British Gas in 1997, BG Group plc. (which is a separately listed company and not a part or affiliate of the Group) assigned ownership of the British Gas trademarks and related logos for use in Great Britain to the Group. BG Group plc. has the right to call for a reassignment of this intellectual property if a third party acquires control of the Group. If, as a result of a change of control, the Group is unable to continue to use the British Gas trademarks and logos, this could materially adversely affect its competitive position. In addition to the British Gas trademarks and logos, the Group trades under various other well-known brands, such as Dyno in the United Kingdom and Direct Energy in North America. Any damage to the Group's ability to use its key brands or maintain brand perception could have a material adverse effect on the Group's reputation, business, results of operations and financial condition.

The Group may be significantly impacted by changing tax laws and tax rates

The Group is subject to tax rates and tax legislation applicable in the markets and jurisdictions in which it operates. In particular, the Group pays significantly higher rates of tax in its upstream production businesses, most notably in the UK, where tax rates currently vary from 62 per cent. to 81 per cent. and in Norway where the aggregate tax rate is 78 per cent. The Group's upstream production businesses are typically subject to different tax rates and regimes than those that apply to its downstream businesses. Consequently, the Group is exposed to the risk of changes both to the general corporate tax regime and to specific tax regimes in relation to upstream production or other business segments. Tax laws, tax rates and interpretation of legislation change regularly. Action by governments to increase tax rates, impose additional taxes, revise tax legislation or its interpretation could have a material adverse effect on the Group's business, results of operations and financial condition.

The Group may fail to provide good quality customer service levels

The delivery of good quality customer service is central to the Group's business strategy and there is a risk that customers will leave the Group if they experience unacceptable customer service levels or if it is perceived that the Group is failing to maintain service quality. In an environment where price differentials may narrow, trust and services become increasingly important factors for retention and growth of the customer base. It is not certain what effect a renewed focus on trust and service quality will have on the Group's business or results of operations. Any failure to maintain good quality customer service levels could have a material adverse effect on the Group's reputation, business, results of operations and financial condition, as well as subject the Group to the risk of increased regulatory scrutiny that could, in turn, result in sanctions from the appropriate body.

The Group is exposed to the risk of interruptions to information systems or failure to protect customers' confidential information

Effective and secure information systems are essential for the Group's operations including the efficient management and accurate billing of the Group's customers, effective upstream operations, and successful energy trading and hedging activities. The confidentiality, integrity and availability the Group's information systems could be affected by:

(i) accidental or deliberate disclosure of share-price sensitive information, customer or employee and contractor personal data;

(ii) viral effect of employees, crusader consumers or "hacktivist" groups using social media channels that expose the Group to legal liabilities, damage the Group's reputation or disclose confidential information;

(iii) accidental or deliberate changes to financial and other data the Group relies on;

(iv) lack of availability of systems due to inadequate infrastructure and data-recovery processes; and

(v) an external online attack that renders the Group unable to conduct normal business activities and/or results in the loss or disclosure of personal data, intellectual property or other confidential information or the disruption of control systems.

There can be no certainty that recovery plans and contingency plans will be effective in all possible scenarios. In addition, the Group relies on third-party hardware and software, which are not fully under its control. Outages and interruptions could affect the Group's ability to conduct day-to-day operations.

The Group must comply with regulations on the secure storage and use of customer data, and provide for secure transmission of confidential information to ensure the security of financial and personal data passing over public networks. There can be no assurance that the Group's controls to ensure the confidentiality, integrity and availability of customer and company data will eliminate such risk effectively, and the Group may breach restrictions or may be subject to attack from computer programs that attempt to penetrate the network security and misappropriate confidential information. Due to continual advancement of these programs, computing capabilities and other developments, there is no guarantee that the Group's security measures will be sufficient to prevent all possible breaches. The US and EU data privacy proposals increase the impact if such risks were to materialise, due to the requirement to make public notification of any data breach and the scale of associated fines for non-compliance.

Significant disruption to systems, including that caused by a cyber-attack, and any compromise of the confidentiality of information could have a material adverse effect on the Group's reputation, business, results of operations and financial condition, and may result in regulatory sanctions.

The Group depends on the performance of third parties for certain contracts, which have been outsourced

The Group has entered into a number of outsourcing contracts, some of which are for offshore operations, in respect of certain support functions for its businesses in the United Kingdom and North America, including business-critical information technology services, financial accounting matters and customer billing transactions. In addition, third-party infrastructure will continue to be relied upon by a number of the Group's assets. Upstream production, including new upstream projects, are increasingly being operated or developed by third parties. This brings risks that may lead to HSSE issues and decisions that adversely affect upstream production. In addition, the Group may face increased reputational and legal risks as a result of acts or omissions by operators of joint ventures or other upstream projects, as well as liabilities in proportion to the Group's equity interest, which could have a material adverse effect on the Group's business, results of operations and financial condition. As with any contractual relationship, there are inherent risks to be considered. There can be no guarantee that the chosen suppliers will be able to provide the support functions for which they have contracted, and therefore that the anticipated benefits will be delivered. Any failure of the counterparties to deliver the contracted goods or services could have a material adverse effect on the Group's business, results of operations and financial condition.

The Group operates in competitive markets

In the Group's principal markets, there is strong competition for the supply of energy and services to business and residential energy customers.

The Group operates in retail energy supply markets in the UK and North America that are highly competitive. Suppliers may price aggressively in order to build market share, and customers may switch suppliers based on price, product and service levels, as well as competitor activity. In many North American markets, the Group is competing against an incumbent utility supplier which may have a lower cost base and be able to offer lower prices to the Group's existing and target customers. The retail energy environment is highly competitive across residential and business segments as well as energy services, including new business areas, such as smart enabled applications. In addition, small suppliers continue to enter the supply market, further increasing competition. The Group also operates in the competitive home services market in both the UK and North America. Competition in these markets is increasing as existing energy and other service providers, such as insurance companies, telecom companies, supermarkets, and other large retail companies have entered the services market and seek to strengthen their positions. Failure to sustain competitive cost and service levels could affect market share, and challenge the Group's ability to deliver sustainable operating margins.

In the exploration and production business, the Group faces competition from both international and state run energy companies for obtaining exploration and development rights, particularly outside the UK, and in developing and applying new technology to maximise hydrocarbon recovery. If the Group fails to obtain new exploration and development acreage or to apply and develop new technology, its results of operations and cash flows may be adversely affected. The current trend of the industry towards a reduction in the number of operators through takeovers or mergers may lead to stronger competition from operators with greater financial resources and a wider portfolio of development projects.

There can be no certainty that the Group will retain or develop a competitive position within the markets in which it operates, which could have a material adverse effect on its business, results of operations and financial condition.

The Group's business may be affected by changes in weather conditions

Gas sales volumes and, to a lesser extent, electricity sales volumes, are affected by temperature and other weather factors, which may have an adverse impact on the Group's business, results of operations and financial condition.

The demand for power and gas is seasonal and weather dependent. In the UK, higher demand is typically experienced during the cold weather months of October to March and lower demand during the warm weather months of April to September. In North America, hot weather results in an increased demand for electricity to operate air conditioning units. The Group's profitability is dependent upon its ability to manage its exposure to unseasonably warm or cold weather and to stabilise the impact of such fluctuations through adjustments to its tariffs. The Group's revenues and results of operations could be negatively affected if the Group were unable to adjust for fluctuations in pricing and demand due to changing weather patterns.

The Group is affected by global economic conditions

The Group continues to pursue a range of investment options in different geographies and across the energy chain to deepen the Group's customer relationships and secure the Group's future energy requirements.

Therefore, the Group's operating and financial performance is influenced by the economic conditions of the countries and markets in which it operates, most notably the UK and the United States. Pressure from economic deterioration, higher wholesale prices, increased levels of competition, reduced demand and recessionary impacts all contribute to making market conditions challenging. Recent economic conditions have meant that disposable income has decreased or remained flat and consumer confidence has declined, which could result in discretionary spend being reduced and also lead to increased customer turnover in services, or lead to customers delaying or forgoing the purchase of products and services. The Group's services businesses have been some of the most impacted by the economic downturn, with customers choosing to decrease their cover or exit the cover markets altogether in favour of on-demand or do-it-yourself options, or delaying purchases or upgrades. The prospects for economic recovery remain uncertain, and economic conditions could have a negative impact on the Group's principal businesses.

Strategic issues, including capital investment in mergers, acquisitions, disposals, market position, climate change, sustainable development and new technologies, are also affected by global economic conditions and the Group's ability to grow its business successfully in these respects may be subject to circumstances beyond its control. New or continued weakness in the economic conditions in the Group's principal markets could have an adverse effect on the Group's business, results of operations or financial condition.

The Group's business relies on the security of energy supply

As UK gas reserves have declined, the UK energy market has become increasingly reliant on supplies from Norway and other parts of mainland Europe, together with LNG supplies from other parts of the world. Key elements of security of supply are access to these reserves and the reliability of the storage, pipeline and gas-processing infrastructure operated by the Group and third parties both in the UK and abroad. Any break in this supply chain, for example as a result of unplanned outages, could impact the Group's earnings. The Group's entire business is exposed to the risk of its own or third party facilities being damaged by natural disasters, including but not limited to severe weather conditions. The Group owns a variety of gas and power assets in the United Kingdom and overseas and its results of operations and financial condition could be materially adversely impacted if there were to be long-term outages associated with those assets.

The Group depends on third-party supply arrangements and cannot guarantee the security of the supply chains. In respect of gas provided by the Group, the Group's reserves and resources figures are estimates reflecting applicable reporting regulations as they may evolve. These estimates are consistent with the relevant internationally accepted guidelines and definitions. However, the Group's gas and oil reserves and resources figures are only estimates, and subsequent downward adjustments are possible.

In addition, there is a risk of terrorist activity, including acts and threats to the energy sector, which may include sabotage or cyber-attack, of power stations or pipelines, which could in turn affect security of supply or cause a break in supply of energy. Any such failure could have a material adverse impact on the Group's business, results of operations and financial condition.

The Group is exposed to falling residential energy consumption

Improved energy efficiency, building insulation, new boiler installations and changing customer behaviour as a result of greater environmental awareness, reaction to past price increases, long-term weather patterns, and the general economic downturn have led to a reduction in energy demand in recent years. The UK government sees both residential and business energy efficiency as a key part of meeting its carbon reduction targets. As the United Kingdom government and households in the United Kingdom continue to focus on and emphasise low-carbon solutions, the Group may be subject to additional regulatory obligations, which may lead to higher operational costs, increased capital investment, and operational constraints for certain of the Group's activities and assets.

The Group expects gas demand in the United Kingdom to continue to decline over the next decade with improvements in insulation of houses and buildings in the UK and widespread installations of more energy efficient boilers. The Group also expects that the emergence of smart technology and more energy efficient appliances will offset underlying growth in electricity demand such that the Group expects overall electricity demand to decline by a small amount or remain flat. The long-term demand for gas will be significantly affected by government decisions about market structures, climate change initiatives, and industry decisions around the generation mix. These changes may significantly reduce the volume of energy that the Group is able to sell to its customers, which could have an adverse impact on the Group's results of operations and financial condition. While these trends are currently most pronounced in the United Kingdom, changes in consumption patterns in the Group's other principal markets due to regulation, technology or other reasons could have an adverse impact on the Group's financial condition and results of operations.

The Group's business activities and sales may be affected by changing customer behaviour and the emergence of new technologies

With the increasing recognition of the economic and environmental impact of global climate change, the Group's future operations will potentially be shaped by changes in customer demands and expectations, and regulatory requirements necessitating a move towards a low-carbon economy, which may present significant additional risks and lead to higher operational costs, reduced energy demand, increased capital requirements and operational constraints for certain of the Group's activities and assets. In addition, the ineffective or incomplete implementation of new legislation may have adverse consequences on the viability of investment in new technologies and the development of new assets.

As digital media, the Internet and mobile devices play a greater role in the retail energy business sector, the Group has faced, and will continue to face, heightened competitive pressures resulting from falling barriers to market entry and swiftly changing customer loyalties. The value of customer data has increased, and there is a widening range of virtual interaction with customers through the emergence of new technologies, such as smart metering and smart grids. These factors could affect gas and electricity demand, and therefore the Group's earnings, and place greater emphasis on energy related services, such as energy efficiency, microgeneration and energy management/automation. New technology allows non-energy, web-based firms to access customer energy consumption data, with or without the agreement of energy suppliers. This new data may not simply be used for billing, but also to provide the customer with improved reporting, advice, new products and new services. The Group cannot be certain that its future operations and strategy will successfully mitigate against the risks presented, or enable the Group to offer innovative product and service offerings or to otherwise take advantage of opportunities that may present themselves.

The Group is also currently subject to certain government enforced obligations to promote greater energy efficiency by its customers, including smart meter installation. Failure by the Group to comply with these obligations or adapt to further regulation and changing customer demands and behaviour as a result of global climate change and increased awareness of the environmental impact of energy use may have a material adverse effect on the Group's reputation, business, results of operations and financial condition.

The Group may not sufficiently fund investment in or develop operational assets

Continual investment is required to maintain and improve the condition of, and to address operational issues that arise in relation to, the Group's Upstream assets. Such investment affects the operational life and the output achievable from these assets. The Group reviews the value of its assets periodically to inform valuation and investment decisions and, if appropriate, may write down the value of certain assets.

Upstream capital projects are exposed to the risk of potential build quality issues, as well as cost and timetable overruns, unsuccessful development of partnership opportunities and Health, Safety, Security and Environment ("HSSE") failures. The complexity and inherent risk of the current project pipeline suggests an increasing risk profile caused by a number of potential issues including the complexity of project interfaces, the pioneering nature of technology and construction techniques, hostile operating environments, dependency on joint venture partners and key contractors, inability to realise reserves and capability shortfalls.

Timing delays, cost overruns, changes in the regulatory environment and other factors could reduce a project's net present value and damage relationships with partners, investors and regulators, or otherwise render a project uneconomic. Assets may not perform as expected, including as a result of shutdowns or an inability to realise expected productions volumes, among other things. In addition, the Group may decide not to continue with certain investments or developments if the Group believes the anticipated risks are too severe or the anticipated returns are or become insufficient to justify the investment.

The level of investment is dependent on sufficient cash resources being available. A lack of investment, or failure to direct investment as required, may reduce the output from, and resale value of, the Group's assets. A reduction in the output or resale value would adversely affect the Group's business, results of operations and financial condition.

Failure to identify, execute and finance suitable acquisitions may result in the Group failing to deliver on its strategy

The Group's success in achieving its strategy through the acquisition of suitable assets may be limited by its ability to execute and finance such acquisitions. In order to deliver on its strategy, the Group must identify suitable acquisitions and negotiate acceptable terms and conditions relating thereto. The Group may face significant competition in identifying and acquiring suitable targets from competitors who may have greater resources or greater familiarity with the market. In North America, in particular, the Group will continue to evaluate and pursue acquisitions and investments as part of its overall strategy and it may have difficulty doing so in a highly competitive market. The Group may not be successful in identifying, executing and financing suitable acquisitions in the future or economic stakes taken in businesses may not prove to be good investments. The Group also faces the risk that an acquired business may not be integrated successfully into the Group. In particular, the Group may face difficulty retaining and/or replacing the acquired business' existing management and employees or may expend significant time and resources integrating or adapting the acquired business' information systems. Failure by the Group to identify, execute, finance or integrate acquisitions of available assets could also mean the Group fails to secure long-term energy supplies for its customers as it produces less gas and power than it requires to fulfil downstream demand. Furthermore, the Group may be required to refinance indebtedness incurred to fund such acquisitions, in the capital markets or otherwise, and there is no guarantee that the Group will be able to do so on favourable terms or at all. Any of these factors could have a material adverse effect on the Group's business, results of operations and financial condition.

The Group uses derivatives and hedging arrangements in the conduct of its business, which exposes it to further regulatory risk

The Group uses derivatives and hedging arrangements in the conduct of its business, which exposes it to further regulatory risk. The Group uses a number of derivatives arrangements and other financial instruments in the ordinary course of its business as part of its risk management programme. As a result, the Group is subject to additional regulatory regimes. Regulation of derivatives and other similar financial instruments in the United States and the EU is changing rapidly. Some regulations are in the process of implementation but others are being revised and/or require the publication of subordinate legislation and it is uncertain when or how these will be fully implemented and therefore what the consequences for the Group will be.

In the United States, these regulations are being implemented through the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act"), which is being implemented through published rulemaking. This process has been on-going since 2011 and is forecast to conclude by the end of 2014. In Europe, regulation is being implemented through the European Market Infrastructure Regulation ("EMIR"). Certain subordinate legislation and/or regulatory processes remain outstanding, including in key areas such as the mandatory clearing obligation and the mandatory collateral requirements that apply to non-cleared OTC products. Full implementation is likely not to be complete until 2019. An additional complexity in analysing the impact of EMIR on the Group is that the Markets in Financial Instruments

Directive ("MiFID") is under review by European legislators. This review may alter the nature and scope of the OTC derivatives which are covered by MiFID, and therefore by EMIR, and may include products used by the Group which are not currently covered. Any amendment to MiFID is not expected to take effect before 2015.

Both United States and European regulations require certain market participants to clear certain financial derivatives through central clearing parties. Derivatives, which are not so cleared, may become covered by rules obliging the exchange of margin between OTC counterparties as well as a number of other operational and risk management requirements. The full and final effect of all of these regulations on the Group is uncertain. The Group could be subject to increased cash margin and collateral requirements, restrictions as to which platforms can be used for certain types of trade, increased transaction costs and the risk of reduced liquidity in some of its markets. Any of these outcomes could adversely affect the Group's ability to manage risk and the cost of its risk management programme, and therefore may have a material adverse effect on its business, results of operations and financial condition.

The Group is subject to extensive HSSE risks and regulations

The Group manages significant HSSE hazards associated with its operations, including the operation of onshore and offshore gas production, exploration, transportation, gas storage and supply, and power generation assets. The five principal categories of HSSE risks associated with the Group's operations are:

(i) an incident resulting in one or more fatalities or multiple injuries at an owned, operated or other facility where the Group has an interest;

(ii) an incident which results in significant environmental damage or compliance breach;

(iii) an incident which results in a fatality or major injury to a member of the public;

(iv) a security event, requiring activation of the Group's crisis management plan and/or business continuity plan; and

(v) failure of due diligence activity or to identify liabilities during merger and acquisition or project activity, which may significantly and adversely change the HSSE risk profile of the business.

Any of these risks may result in widespread distress and harm, as well as significant disruption to operations and damage to the Group's reputation. In turn, resultant legal action could have an adverse financial impact on the Group. Certain events, including those arising because of third-party acts, such as acts of terrorism or war, are not within the Group's control. There is a growing expectation that companies accept responsibility for the actions of the third parties with whom they contract.

Although ultimate responsibility for the safe operation of nuclear plants remains with Electricité de France Energy, Nuclear Generation Group Limited ("ENGGL"), the Group, through its joint venture with Electricité de France S.A. ("EDF"), is also indirectly exposed to the scope of the hazards associated with the nuclear power generation industry.

The Group and the management of its operational assets is subject to various environmental, health and safety laws and regulations governing, among other things: (a) the development and operation of high hazard facilities and associated process safety requirements; (b) the generation, storage, handling, release, remediation, use, disposal and transportation of hazardous materials and wastes, including nuclear waste; (c) decommissioning and decontamination of its facilities and assets; (d) air emissions, including of greenhouse gas emissions and other hazardous air pollutants; (e) the health and safety of the public and its employees; and (f) the generation of electricity. Complying with these regulations or changes to these regulations could significantly impact the cost of managing the Group's operational assets, and may make it uneconomic to continue managing certain of its operational assets. Environmental, health and safety laws and regulations are complex, vary between jurisdictions and may become more stringent over time. The Group has incurred and will continue to incur costs to comply with them. The Group is currently remediating contamination at certain of its well sites in Canada and there can be no assurance that significant costs will not be incurred in connection with this or future contamination.

Environmental and safety permits are required to be obtained from various governmental and regulatory authorities in order to manage the Group's operational assets. Certain permits require periodic renewal or review of their conditions, and it cannot be guaranteed that it will be possible to renew such permits or whether material changes in permit conditions will be imposed or can be satisfied on an economically viable basis. While the nature of developments in environmental regulation cannot be predicted, it is anticipated that the direction of future changes will be towards stricter controls. In addition, the Group's customers may require that the Group maintains certain quality and safety certifications, or meets certain quality and safety targets, during the term of a contract. Failure on the Group's part to obtain and maintain these certifications or meet these targets may result in the early termination of the respective contract or in the Group's failure to be considered for future contracts, any of which could have a material adverse effect on the Group's results of operations and financial condition.

In addition, the Group's service engineers in the UK and North America complete more than 10 million home visits each year to carry out essential work on gas and electrical installations, appliance maintenance, and plumbing and drain services. Home visits present potential health and safety risks to the Group's staff and customers, as well as reputation risks, due to the work taking place in customer homes, which are outside of the Group's direct control.

Significant HSSE events, precautionary closures, suspension of activities, or breach of applicable HSSE regulations could affect the safety of individuals or gas and/or power production (including the premature closure of operational assets), result in liabilities, fines or other sanctions, be the subject of litigation, or lead to a loss of production and/or service which, in turn, could have a material adverse effect on the Group's reputation, business, results of operations, and financial condition. Insurance proceeds, where available, may not be adequate to cover any or all liabilities incurred, lost revenue or increased expenses resulting from the Group's operations.

The Group is exposed to risks associated with the existing ENGGL nuclear fleet

The Group holds a 20 per cent. interest in Lake Acquisitions Limited, a nuclear power generation business which owns eight nuclear power facilities in conjunction with EDF which are operated by ENGGL. The Group's investment in the existing fleet of eight nuclear power stations exposes it to the risks associated with the nuclear industry (including the fleet's operational life, planned and unplanned outages, and operational costs) and the impact of nuclear regulation (including regulation by the Office for Nuclear Regulation relating to the operation of nuclear power stations). The existing nuclear fleet is ageing, with all reactors except one having already been granted life extensions. The Group is exposed to potential losses in production due to the fleet's stage in life, and this could be further exacerbated by unforeseen plant closures.

Although the Group enjoys certain veto rights over certain decisions to be taken by Lake Acquisitions Limited (or their respective affiliates), EDF has majority management control of such entities. If the Group disagrees with EDF's management, it has limited rights to dispute and seek compensation in relation to such decisions.

The Group is subject to numerous permit requirements and licencing regimes

The operation of the various businesses conducted by the Group requires authorisations from various national, state, provincial and local government agencies. Obtaining necessary permits, licences, authorisations and certifications can be a complex, time-consuming process, and the Group cannot guarantee that it will be able to obtain all such authorisations required for the operation of its various businesses in a timely manner or at all. Failure to obtain or renew such required authorisations or any disputes in connection with previously obtained authorisations could result in the suspension or termination of the Group's operations or the imposition of material fines, penalties or other liabilities that could have a material adverse effect on the Group's financial condition, results of operations and cash flows. In addition, the Group's customers may require that the Group maintains certain quality and safety certifications, or meets certain quality and safety targets, during the term of a contract. Failure on the Group's part to obtain and maintain these certifications or meet these targets may result in the early termination of the respective contract or in the Group's failure to be considered for future contracts, any of which could have a material adverse effect on the Group's financial condition, results of operations and cash flows.

The Group may fail to attract and retain senior management and skilled personnel

The attraction, retention and succession of senior management and individuals with key skills is a critical factor in the successful execution of the Group's strategy. This is especially relevant in highly competitive markets, such as the Group's upstream business, where technical and project management skills are required to both maintain existing and build new assets, as well as new business ventures such as shale gas. Failure to recruit or retain senior management and individuals, or to make appropriate succession plans, could compromise achievement of the Group's strategy and could have a material adverse effect on the Group's business, results of operations and financial condition.

The Group is exposed to uncertain decommissioning costs

In addition to the risks associated with the Group's upstream operations during the life of oil, gas and storage fields, the Group incurs liabilities and costs associated with the decommissioning of such fields at the end of their lives. The Group's estimates of the cost of decommissioning are reviewed periodically and for producing fields are based on proven and probable reserves, price levels and decommissioning technology at the relevant balance sheet date. For storage assets, the estimated cost of decommissioning is based on the general economic performance of each asset, including price levels, and decommissioning technology at the relevant balance sheet date. As of 31 December 2012, the Group's decommissioning provision was £2,171 million. The payment dates of expected future decommissioning costs are uncertain and dependent on the lives of the facilities, which are also uncertain.

The decommissioning of such fields is also regulated by law and may require the owners of offshore installations and pipelines to provide security or enter into a decommissioning security agreement. Changes in law imposed by the Energy Act 2008 may result in increased decommissioning liabilities since the Secretary of State is now entitled to make all relevant parties (which may include former owners of such assets) liable for the decommissioning of an installation or pipeline, and may require financial information and decommissioning security at any time during the life of an oil or gas field. This could result in increased costs for present and future owners of offshore installations and pipelines.

The existing ENGGL nuclear fleet will, following closure of the power stations, give rise to decommissioning costs. Certain of ENGGL's nuclear liabilities will be paid for out of the Nuclear Liabilities Fund, which is underwritten by the UK government. There is a risk that a breach of minimum performance standards may result in the creation of disqualified liabilities, which would not be funded by the Nuclear Liabilities Fund and would fall to ENGGL to discharge.

Decommissioning costs could exceed the Group's estimated costs and provisions, and the Group may be required to provide greater security for decommissioning costs than expected, which could have a material adverse effect on the Group's business, results of operations and financial condition.

The Group may fail to execute change programmes and business restructuring

The successful delivery of business change is fundamental to the Group's future success, and includes both cultural and technical transformation. As the Group grows, structures are regularly reviewed to ensure that activities are organised in an effective and efficient way to keep the Group's cost base as low as possible in order to offer the customer base competitive prices and products. With changes to the Group's structure and priorities, there is a risk that industrial relations could worsen. This primarily affects areas of the operational workforce in upstream activities, the engineers in British Gas and the staff in Direct Energy Services, and could also be triggered by changes to terms and conditions, changes to pensions or as a response to a wider climate of trade union unrest.

Furthermore, through acquisition activity there is a risk that the Group will not be able effectively to integrate purchased assets to achieve expected synergies. Additionally, the delivery of certain technical change programmes may be large and complex. There are a number of risks arising, including failure to complete the change, overstretching the Group's resources, undermining system integrity, threatening business continuity, cost and/or timing overruns and failure to realise planned benefits. Unexpected or additional costs in relation to restructuring or integration could have a material adverse effect on the Group's business, results of operations and financial condition.

Labour disputes could have an adverse impact on the Group's business

The Group cannot provide any assurance that labour disputes or unrest, such as strikes, walkouts, claims or other labour disturbances, will not disrupt its business. A significant strike or other labour dispute could impact the Group's ability to provide upstream operations or downstream residential and business services in one or more of its key markets and could impact the customer service offered to residential and business supply customers. Any such disruption to the Group's business could negatively impact its reputation and may result in the loss of customers to competitors. The Group has not taken out any insurance to cover losses due to business disruptions caused by labour issues. Consequently, its financial position and operating results may be adversely affected by labour unrest.

Liquidity risk, and in particular risk relating to margin obligations as a result of existing contracts, is inherent in the Group's operations

Liquidity risk is the risk that the Group is unable to meet its obligations as they fall due. Managing liquidity risk is particularly important in the current economic and market environment where the financial markets are volatile and the availability of capital is uncertain.

The liquidity risk within the Group is increased by the margin cash arrangements contained in certain wholesale commodity contracts. As the Group is a net purchaser of commodities, this means that it is generally required to deposit cash as collateral with margin counterparties when wholesale prices fall. Cash forecasts identifying the liquidity requirements are produced at least monthly and these are assessed for different scenarios, including the impact of significant changes in commodity prices or a credit rating downgrade; however, the Group's ability to access liquidity during periods of liquidity stress may be constrained as a result of current and future economic and market conditions. A reduction of the Group's liquidity could have a material adverse effect on its business, results of operations, and financial condition.

A downgrade in the Group's credit ratings may increase its costs of funding and limit its ability to trade in commodity markets

The Group benefits from its credit rating (long-term debt: A3 stable outlook (Moody's), A- stable outlook (Standard & Poor's); short-term debt: P-2 stable outlook (Moody's), A-2 stable outlook (Standard & Poor's)). Any deterioration in the Group's credit ratings may increase its costs of funding or otherwise affect its ability to obtain credit. The Group would also need to increase its levels of credit support for certain arrangements, most notably margin or other security in its wholesale commodity contracts or face limits on its ability to trade in commodity markets and to implement its hedging strategy. The Group would also need to increase its security for decommissioning of assets. Any of these factors could have a material adverse effect on the Group's business, results of operations and financial condition.

The Group has funding risks relating to its defined benefit pension schemes

The Group maintains a variety of pension schemes including defined benefit schemes. The pension fund liabilities are partially matched with a portfolio of assets, which leaves potential risk around the mortality rate, inflation, interest rates and returns on assets. Accounting changes, effective as of 2013, will reduce the income statement credit from the return on pension scheme assets. The schemes contain a high proportion of equity assets that are expected to provide a better return in the long-term than alternative investments such as bonds; however, in the short-term, the difference between the value of liabilities and assets may vary significantly, potentially resulting in a large deficit having to be recognised on the Group's balance sheet, alongside an increase in the income statement expense and the funding requirements (cash and possibly contingent assets). In the current business environment, with volatile bond and unstable equity markets, this could lead to significant changes in long-term interest rates and inflation, long-term gilt yields, corporate bond yields, equity values and credit spreads, or a material weakening of the Group's credit rating. Furthermore, a quicker than expected increase in life expectancy, or employee pensionable salaries increasing above the assumed rates, or a further change in accounting standards could all lead to an increased risk that large deficits may arise in connection with the Group's pension schemes. The pension schemes are also subject to triennial actuarial evaluation (next due in March 2015) and if this exercise was to identify higher deficits, this could result in additional deficit payments being made into the schemes, a further cap on increases in pensionable pay, or reducing cash contributions through the offering of asset backed security/contributions. Any requirement to put cash into these schemes to cover any such deficits, if sufficiently large, could have a material adverse effect on the Group's business, results of operations and financial condition.

The pension regulator in the UK continues to guide trustees to clear deficits as quickly as companies can afford. In addition, actions by the pension regulators or the trustees of the Group's pension schemes and/or any material revisions to existing pension legislation could require accelerated and increased contributions to the Group's pension funds before or concurrent with any increased return to shareholders beyond the normal dividend, which may restrict the Group's ability to carry out a share repurchase. The trustees could also seek accelerated and increased contributions in the event of the Group planning to take on more leverage through acquisitions or investment, which may restrict the Group's ability to carry out such transactions or investments. This could therefore have a material adverse effect on the Group's business, results of operations, and financial condition.

The Group's business may be affected by the default of counterparties in respect of monies owed to the Group

As a consequence of its normal operations, the Group often has significant amounts owed to it by its energy counterparties. In addition, the Group often holds large cash balances on deposit with financial institutions. In the current unstable business environment, there is an increased risk of a counterparty default, which may, among other things, reduce the Group's cash flows. The Group's policy to limit counterparty exposures by setting credit limits for each counterparty, where possible by reference to published credit ratings, cannot eliminate such exposure or adequately mitigate such risk, and such a counterparty default may have a material adverse effect on the Group's business, results of operations and financial condition. The Group is also, in the ordinary course of its business, owed amounts by its retail and wholesale customers. A significant number of customer defaults could adversely affect the Group's results of operations and financial condition.

The Group is exposed to currency fluctuations

The Group has operational exposure in US and Canadian dollars, Norwegian krone, euros and Trinidadian dollars. Operational and capital expenditure cash flows may also be in currencies other than pounds sterling, the Group's reporting currency. The Group's profitability may be adversely affected if the results and cash flows associated with these international operations fall or cash outflows rise because of currency fluctuations against the pound.

It is the Group's policy to use hedging instruments, within certain parameters, to manage the impact of currency fluctuations. To the extent that any of the Group's potential exposure remains unhedged, or such hedging is ineffective, the value of its investments may be affected by fluctuations in currency. Adverse movements in currency rates may have a material adverse effect on the Group's business, results of operations and financial condition.

The Group is exposed to interest rate fluctuations

The Group is exposed to movements in interest rates, which affect the amount of interest paid on borrowings and the return on its cash investments. If interest rates were to increase, the amount of interest paid on floating rate borrowings would increase, as would the cost of funding investments. The Group uses derivative financial instruments, such as interest rate swaps, to manage interest rate risk on long-term borrowings. Adverse movements in interest rates could have a material adverse effect on the Group's business, results of operations and financial condition.

Risks Related to the Notes

An active trading market for the Notes may not develop, and the transfer of the Notes will be subject to restrictions

Each of the Notes are a class of securities that has never been traded. There can be no assurance regarding future development of a market for the Notes. An application has been made for the admission of the Notes to listing on the Official List and to trading on the Regulated Market. However, there can be no assurance that the Notes will be listed on any exchange at the time the Notes are delivered to the Initial Purchasers or at any time. The Initial Purchasers have informed us that they intend to make a market in the Notes. However, they are not obliged to do so and may discontinue such market making at any time without notice. There can be no assurance that an active trading market for the Notes will develop or, if one does develop, that it will be sustained.

The Notes have not been registered under the Securities Act or any US state securities law, and the Company has not agreed to, and does not intend to register the Notes under the Securities Act or any US state securities law. Therefore, you may not offer or sell the Notes, except pursuant to an exemption from, or in a transaction not subject to, the registration requirements of the Securities Act and applicable state securities laws. You should read the discussion under the heading "Transfer Restrictions" for further information about the transfer restrictions that apply to the Notes. It is your obligation to ensure that your offers and sales of Notes within the United States and other countries comply with all applicable securities laws.

The Notes will initially be held in book-entry form and therefore you must rely on the procedures of the relevant clearing systems to exercise any rights and remedies

Unless and until the Notes in definitive registered form, or definitive registered Notes, are issued in exchange for book-entry interests, owners of book-entry interests will not be considered owners or holders of Notes. DTC, or its nominee, will be the registered holder of the Global Notes for the benefit of its participants including Euroclear and Clearstream, Luxembourg. After payment to the registered holder, the Company will have no responsibility or liability for the payment of interest, principal or other amounts to the owners of book-entry interests. Accordingly, if you own a book-entry interest, you must rely on the procedures of DTC, Euroclear and/or Clearstream, Luxembourg, and if you are not a participant in DTC, Euroclear and/or Clearstream, Luxembourg, on the procedures of the participant through which you own your interest, to exercise any rights and obligations of a holder of the Notes. See "Book-Entry, Delivery and Form".

Unlike holders of the Notes themselves, owners of book-entry interests will not have any direct rights to act upon the Company's solicitations for consents, requests for waivers or other actions from holders of the Notes. Instead, if you own a book-entry interest, you will be permitted to act only to the extent you have received appropriate proxies to do so from DTC, Euroclear and/or Clearstream, Luxembourg or, if applicable, from a participant. There can be no assurance that procedures implemented for the granting of such proxies will be sufficient to enable you to vote on any matters on a timely basis.

Similarly, upon the occurrence of an event of default under the Fiscal and Paying Agency Agreements, unless and until definitive registered Notes are issued in respect of all book-entry interests, if you own a book-entry interest you will be restricted to acting through DTC, Euroclear and/or Clearstream, Luxembourg. There can be no assurance that the procedures to be implemented through DTC, Euroclear and/or Clearstream, Luxembourg will be adequate to ensure the timely exercise of rights under the Notes. See "Book-Entry, Delivery and Form".

Investors in the Notes may have limited recourse against the Company's independent accountants

In respect of the audit reports relating to the annual financial statements included herein, PricewaterhouseCoopers LLP states within its report: "This report, including the opinion, has been prepared for and only for the Company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. PwC does not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing".

Investors in the Notes should understand that these statements are intended to disclaim any liability to parties (such as purchasers of the Notes) other than members of the Company with respect to those reports. The Commission would not permit such limiting language to be included in a registration statement or a prospectus used in connection with an offering of securities registered under the Securities Act, or in a report filed under the Exchange Act. If a US court (or any other court) were to give effect to the language quoted above, the recourse that investors in the Notes may have against the independent auditors based on their reports could be limited.

The Company is a holding company with no revenue-generating operations of its own

The Group's business is carried out in large part its operating subsidiaries and associated companies. The Company will depend upon operating subsidiaries to provide the funds necessary to pay the principal of, and the interest on, the Notes. These operating subsidiaries and associated companies have not guaranteed the Notes, and have no obligation, contingent or otherwise, to pay amounts due under the Notes or to make funds available for these payments, whether in the form of liens, dividends or otherwise. Payments from the operating subsidiaries to the Company might not be able to be made in some circumstances, due to corporate law, contractual or other legal restrictions or other factors.

Holders of the Notes will have a direct claim based on the Notes against the Company, but will not have a direct claim based on the Notes against any operating subsidiaries. The right of the holders of the Notes to receive payments under the Notes will be structurally subordinated to all liabilities of the operating subsidiaries and associated companies. These liabilities include debt that some of the Group's subsidiaries have incurred under bank facilities. In the event of a bankruptcy, liquidation, reorganisation or similar proceeding relating to a subsidiary, the right of the holders of the Notes to participate in a distribution of the assets of such subsidiary will rank behind such subsidiary's and associated companies' creditors (including trade creditors) and preferred stockholders (if any), except to the extent that the Company has a direct claim against such subsidiary.

A holder's effective yield on the Notes may be diminished by the tax impact on that holder of its investment in the Notes

Payments of interest on the Notes, or profits realised by the holder upon the sale or repayment of the Notes, may be subject to taxation in its home jurisdiction or in other jurisdictions in which it is required to pay taxes. However, the tax impact on an individual holder may differ from the situation described for holders generally. All investors are advised to contact their own tax advisers for advice on the tax impact of an investment in the Notes.

A holder may be subject to the EU Savings Directive

EU Council Directive 2003/48/EC on the taxation of savings income (the "EU Savings Directive") requires EU Member States to provide to the tax authorities of other EU Member States details of payments of interest and other similar income paid by a person within its jurisdiction to (or for the benefit of) an individual or certain other persons in that other EU Member State, except that, Luxembourg and Austria will instead operate a withholding system for a transitional period (subject to a procedure whereby on meeting certain conditions, the beneficial owner of the interest or other income may request that no tax be withheld) unless during that period they elect otherwise. The Luxembourg government has announced its intention to elect out of the withholding system in favour of an automatic exchange of information with effect from 1 January 2015.

The European Commission has proposed certain amendments to the EU Savings Directive, which may, if implemented, amend or broaden the scope of the requirements described above.

If a payment were to be made or collected through an EU Member State which has opted for a withholding system and an amount of or in respect of tax were to be withheld from that payment pursuant to the EU Savings Directive or any law implementing or complying with, or introduced in order to conform to, the EU Savings Directive or any other directive implemented at the conclusion of the ECOFIN Council meeting of 26-27 November 2000, no Additional Amounts (as defined in "Description of the Notes—Payment of Additional Amounts") would be payable by the Company.

The Notes are unsecured obligations of the Company and are subordinated to secured obligations on insolvency

Holders of secured obligations of the Company will have claims that are prior to the claims of holders of the Notes to the extent of the value of the assets securing those other obligations. The Notes are effectively subordinated to secured indebtedness to the extent of the value of the assets securing those other obligations. In the event of any distribution of assets or payment in any foreclosure, dissolution, winding-up, liquidation, reorganisation, or other bankruptcy proceeding, the assets securing the claims of secured creditors will be available to satisfy the claims of those creditors, if any, before they are available to unsecured creditors, including the holders of the Notes. In any of the foregoing events, there is no assurance to holders of the Notes that there will be sufficient assets to pay amounts due on the Notes.

Credit ratings may not reflect all risks, are not recommendations to buy or hold securities and may be subject to revision, suspension or withdrawal at any time

One or more independent credit rating agencies may assign credit ratings to the Notes. The ratings may not reflect the potential impact of all risks related to structure, market, additional factors discussed above and other factors that may affect the value of the Notes. A credit rating is not a recommendation to buy, sell or hold securities and may be revised or withdrawn by the rating agency at any time.

The trading market for debt securities may be volatile and may be adversely impacted by many events

The market for debt securities is influenced by economic and market conditions, interest rates and currency exchange rates. Global events may lead to market volatility, which may have an adverse effect on the price of the Notes.

The Company may incur substantially more debt in the future

The Company may incur substantial additional indebtedness in the future, some of which may be secured by some or all of the Company's assets. The terms of the Notes will not limit the amount of indebtedness the Company may incur. Any such incurrence of additional indebtedness could exacerbate the related risks that Centrica now faces as described in this Offering Circular or pose new risks not described in this Offering Circular.

PRESENTATION OF FINANCIAL AND OTHER INFORMATION

General

This Offering Circular contains the audited consolidated financial statements of the Group, including the notes thereto, as of and for the years ended 31 December 2012, 2011 and 2010, referred to as the "2012 Financial Statements", the "2011 Financial Statements" and the "2010 Financial Statements", respectively, and the unaudited consolidated interim financial statements as of and for the six months ended 30 June 2013, referred to as the "Interim Financial Statements" (together with the 2012 Financial Statements, the 2011 Financial Statements and the 2010 Financial Statements, the "Consolidated Financial Statements"). The financial information presented below is derived from, and should be read in conjunction with, the unaudited consolidated financial statements for the six months ended 30 June 2013 and the consolidated financial statements as of and for the years ended 31 December 2012, 2011 and 2010 and the accompanying notes thereto, all of which are included elsewhere in this Offering Circular.

You should read the information set forth below in conjunction with the other sections of this Offering Circular, including "Selected Historical Financial Information" and "Operating and Financial Review", and the Consolidated Financial Statements included elsewhere in this Offering Circular.

The Consolidated Financial Statements are presented in pounds sterling and are prepared in accordance with International Financial Reporting Standards as adopted by the European Union ("IFRS"). The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. These standards also require management to exercise its judgement in the process of applying accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the Group are disclosed in the Consolidated Financial Statements. The Group's accounting policies are also disclosed in the Consolidated Financial Statements.

Certain financial information in the Interim Financial Statements has been restated, to reflect the following standards, amendments, and interpretations effective in 2013:

- International Accounting Standard ("IAS") 19 (revised): "Employee benefits";
- IAS 1: "Presentation of financial statements—Presentation of items of other comprehensive income"; and
- IFRS 13: "Fair value measurement".

In addition, the Group made the following accounting policy changes effective in 2013:

- On 27 February 2013, the Group changed its segmental reporting to reflect the Group's new organisational structure and to align with management reporting. The North American Upstream Gas business has been reallocated from the "Direct Energy—Upstream and wholesale energy" subsegment to the "Centrica Energy—Gas" subsegment and the North American Power and Midstream & Trading businesses have been reallocated from the "Direct Energy—Upstream and wholesale energy" subsegment to the "Direct Energy—Business energy supply" subsegment.
- Where there is a specific link to revenue generation, the presentation of sales commissions and prepayment customers vending fees has been reclassified from operating costs to costs of sales.
- The presentation of current/non-current classification of interest accruals on bank overdrafts, loans and other borrowings has been reclassified from non-current liabilities to current liabilities because the amounts are due for payment within 12 months.
- The presentation of fair value gains and losses on revaluation of derivatives and hedges in financing costs is represented on a net, rather than a gross basis within finance costs.

As a result of the aforementioned changes in accounting standards and accounting policies, the 2012 comparative period in the Interim Financial Statements was restated accordingly. Solely for the purposes of this Offering Circular, management has updated the segmental financial data to reflect the change in the Group's segments as of and for the years ended 31 December 2012, 2011 and 2010 for comparison purposes only (see "Operating and Financial Review").

The Group reflects its underlying financial results in the "business performance" column of the Group's Income Statement. To provide readers with a clear and consistent presentation, the effects of certain re-measurements of financial instruments and exceptional items are reported separately in a different column in the Group's Income Statement and are separately identified in the Notes to the Consolidated

Financial Statements. See "Selected Historical Financial Information" and "Operating and Financial Review" for a reconciliation of business performance to statutory results.

The Consolidated Financial Statements are not intended to comply with Commission reporting requirements. Compliance with such requirements would require the modification or exclusion of certain information presented within this Offering Circular and the presentation of certain other information not included in this Offering Circular.

Certain amounts and percentages, which appear in this Offering Circular have been subject to rounding adjustments and, accordingly, figures shown as totals in certain tables may not be an arithmetic aggregation of the figures that precede them.

Non-IFRS Financial Measures

This Offering Circular contains some measures which are not accounting measures within the scope of IFRS and which the Group uses to assess the financial performance of its businesses. These measures include adjusted operating profit, adjusted earnings, adjusted operating profit margin, EBITDA, net debt, working capital movements, margin calls, net capital expenditure, payments to shareholders, and foreign exchange and other. These non-IFRS measures have been included because the Directors believe that they are helpful to investors in assessing the historical financial performance of the Group. These are not measures of operating performance derived in accordance with IFRS, and should not be considered a substitute for gross profit, operating profit, profit/(loss) before tax, cash flow from operating activities or other income or cash flow statement data as determined in accordance with IFRS, or as a measure of profitability or liquidity. The Group's calculation of such non-IFRS measures may be different from the calculation used by other companies and therefore comparability may be limited. See "Operating and Financial Review" for a reconciliation of adjusted operating profit to operating profit and profit from business performance to statutory profit. See "Selected Historical Financial Information" for a reconciliation of net debt.

Adjusted operating profit

The Group defines adjusted operating profit as operating profit before exceptional items, certain re-measurements and depreciation resulting from fair value uplifts to property, plant and equipment on the acquisitions of strategic investments, including the Group's share of the results from joint ventures and associates before interest and taxation.

Adjusted earnings

The Group defines adjusted earnings as earnings before exceptional items net of taxation, certain re-measurements net of taxation and depreciation of fair value uplifts to PP&E on the acquisition of strategic investments, net of taxation.

Exceptional items

Exceptional items represent those items which are of a non-recurring nature and, in the Group's judgement, need to be disclosed separately by virtue of their nature, size or incidence. In the periods under review, items which were considered exceptional in nature are disposals of businesses, business restructurings, significant onerous contract charges, asset write-downs, deferred tax charges as a result of changes to tax legislation and pension curtailment gains.

Certain re-measurements

The Group is an integrated energy business. This means that it utilises its knowledge and experience across the gas and power (and related commodity) value chains to make profits across the core markets in which it operates. As part of this strategy, the Group enters into a number of forward energy trades to protect and optimise the value of its underlying production, generation, storage and transportation assets (and similar capacity or off-take contracts), as well as to meet the future needs of its customers (downstream demand). These trades are designed to reduce the risk of holding such assets, contracts or downstream demand and are subject to strict risk limits and controls.

Primarily because some of these trades include terms that permit net settlement (i.e., they are prohibited from being designated as "own use"), the rules within IAS 39: "Financial instruments" require them to be individually fair valued. Fair value movements on these commodity derivative trades do not reflect the underlying performance of the business because they are economically related to the Group's upstream assets, capacity/off-take contracts or downstream demand, which are typically not fair valued. Therefore, these certain re-measurements are reported separately and are subsequently reflected in business performance when the underlying transaction or asset impacts profit or loss.

The arrangements discussed above and reflected as certain re-measurements are all managed separately from proprietary energy trading activities where trades are entered into speculatively for the purpose of making profits in their own right. These proprietary trades are included in the "business performance" column (i.e., in the results before certain re-measurements).

Strategic investments

The Group has determined that for strategic investments it is important to separately identify the earnings impact of increased depreciation arising from the acquisition date of fair value uplifts made to plant, property and equipment ("PP&E") over their useful economic lives. As a result of the nature of fair value assessments in the energy industry, the value attributed to strategic assets is a subjective judgement based on a wide range of complex variables at a point in time. The subsequent depreciation of the fair value uplifts bears little relationship to current market conditions, operational performance or underlying cash generation. Management therefore reports and monitors the operational performance of strategic investments before the impact of depreciation on fair value uplifts to PP&E and the segmental results are presented on a consistent basis. The Group has two strategic investments for which reported profits have been adjusted due to the impact of fair value uplifts. These strategic investments related to the 2009 acquisitions of Venture Production plc ("Venture") the operating results of which are included in with the "Centrica Energy—Gas" subsegment and the acquisition of the 20 per cent. interest in Lake Acquisitions Limited, the results of which are included in the "Centrica Energy—Power" subsegment.

Adjusted operating profit margin

The Group defines adjusted operating profit margin as adjusted operating profit divided by revenue.

EBITDA

EBITDA represents operating profit before exceptional items and certain re-measurements, and before amortisation, depreciation and impairments, and share of profits/(losses) in joint ventures and associates, net of taxation.

EBITDA has been included in the Offering Circular because the Directors believe that it would be helpful to investors in assessing the historical financial performance of the Group. Nevertheless, EBITDA should not be considered in isolation from or as a substitute for operating profit, cash flows from operating activities or any other measure for determining the Group's operating performance or liquidity that is calculated in accordance with IFRS.

The following table sets forth a reconciliation from statutory operating profit to EBITDA based on information extracted without material adjustment from the Consolidated Financial Statements:

	Six months ended 30 June		Year ended 31 December		
	2013	2012	2012	2011	2010
	(£m) (unaudited)			(£m)	
Statutory operating profit	**1,590**	**1,767**	**2,625**	**1,414**	**3,074**
Less exceptional items and certain re-measurements	(105)	(421)	(63)	794	(880)
Operating profit before exceptional items and certain re-measurements	**1,485**	**1,346**	**2,562**	**2,208**	**2,194**
Less share of profits/(losses) in joint ventures and associates, net of taxation	(52)	(58)	(140)	(93)	(7)
Add back:					
Amortisation and impairment of intangible assets	103	62	245	140	174
Depreciation and impairment of tangible assets	576	423	983	850	816
Impairment of JVs, associates and available for sale financial assets	—	—	—	23	4
EBITDA	**2,112**	**1,773**	**3,650**	**3,128**	**3,181**

Net debt

The Group defines net debt as current and non-current borrowings, less cash and cash equivalents, less current and non-current securities, less mark-to-market values on derivatives used to hedge offsetting movements in borrowings. In the 2012 Financial Statements, the Group changed its net debt measure to align with management reporting, restating net debt to include mark-to-market values on derivative financial instruments used to hedge offsetting changes in borrowings. Solely for the purposes of this Offering Circular, management has restated net debt for the years ended 31 December 2011 and 2010 for comparison purposes only.

Working capital movements

The Group defines working capital movements as movements in inventories, receivables and payables during the period.

Margin calls

The Group defines margin calls as cash payments made on a daily basis to counterparties to cover the mark-to-market positions on certain wholesale commodity contracts until the trade is fully executed.

Net capital expenditure

The Group defines net capital expenditure as gross cash purchases of PPE/Intangibles plus net cash outflow relating to the acquisition of subsidiaries, and investments in joint ventures and associates less net proceeds received relating to the disposals of PPE/Intangibles and subsidiaries, and relating to the repayment of loans to, and disposal of investments in, joint ventures and associates.

Payments to shareholders

The Group defines payments to shareholders as dividends plus amounts used in connection with its share repurchase programme.

Foreign exchange and other

Included in foreign exchange and other are (i) non-cash movements in net debt including foreign exchange and revaluation, (ii) other cash flows including dividends received from joint ventures and associates and payments relating to exceptional items, and (iii) non-cash items within operating profit that are not included within EBITDA.

Independent Auditors

The Consolidated Financial Statements have been audited by PricewaterhouseCoopers LLP, independent accountants, as stated in their reports appearing herein. The Interim Financial Statements have been reviewed by PricewaterhouseCoopers LLP, independent accountants, as stated in their report appearing herein.

Oil and Gas Reserves

Centrica's reserves estimates are consistent with the guidelines and definitions of the Society of Petroleum Engineers, the Society of Petroleum Evaluation Engineers and the World Petroleum Council's Petroleum Resources Management System. Direct Energy reserves estimates have been evaluated in accordance with the Canadian Oil and Gas Evaluation Handbook ("COGEH") reserves definitions and are consistent with the guidelines and definitions of the Society of Petroleum Engineers and the World Petroleum Council. An annual reserves assessment has been carried out by DeGoyler and MacNaughton for the Group's global reserves.

CURRENCIES AND EXCHANGE RATES

The Group publishes its consolidated financial statements in pounds sterling. In this Offering Circular, references to "$" and "US dollars" are to the lawful currency of the United States of America and references to "pounds", "pounds sterling", "GBP" or "£" are to the lawful currency of the United Kingdom.

The following table sets out, for the periods and dates indicated, the high, low, average and period end Bloomberg Composite Rate expressed as US dollars per £1.00. The Bloomberg Composite Rate is a "best market" calculation, in which, at any point in time, the bid rate is equal to the highest bid rate of all contributing bank indications and the ask rate is set to the lowest ask rate offered by these banks. The Bloomberg Composite Rate is a mid-value rate between the applied highest bid rate and the lowest ask rate. The rates may differ from the actual rates used in the preparation of the consolidated financial statements and other financial information appearing in this Offering Circular. Neither the Company nor the Initial Purchasers represents that the US dollar or pound sterling amounts referred to below could be or could have been converted into pounds sterling at any particular rate indicated or any other rate.

The average rate for a year means the average of the Bloomberg Composite Rates on the last day of each month during a year. The average rate for a month, or for any shorter period, means the average of the daily Bloomberg Composite Rates during that month, or shorter period, as the case may be.

The Bloomberg Composite Rate of pounds sterling on 9 October 2013 was $1.59 per £1.00.

Exchange rates for the previous six months:

	Period End	Average Rate(1)	High	Low
May 2013	1.52	1.53	1.56	1.51
June 2013	1.52	1.55	1.57	1.52
July 2013	1.52	1.52	1.54	1.49
August 2013	1.55	1.55	1.57	1.51
September 2013	1.62	1.59	1.62	1.55
October 2013 (to 9 October 2013)	1.59	1.61	1.62	1.59

Exchange rates for the past three years:

	Period End	Average Rate(2)	High	Low
2010	1.55	1.55	1.64	1.43
2011	1.56	1.60	1.67	1.54
2012	1.62	1.59	1.63	1.53
2013 (to 9 October 2013)	1.59	1.55	1.63	1.49

Notes:

(1) The average of the exchange rates on each business day during the relevant period.

(2) The average of the exchange rates on the last business day of each month during the relevant period.

FORWARD-LOOKING STATEMENTS

This Offering Circular contains statements which are, or may be deemed to be, "forward-looking statements" which are prospective in nature. All statements other than statements of historical fact are forward-looking statements. They are based on current expectations and projections about future events and are therefore subject to risks and uncertainties which could cause actual results to differ materially from the future results expressed or implied by the forward-looking statements. Forward-looking statements are typically identified by words such as "may", "will", "believe", "anticipate", "intend", "estimate", "expect" and other words of similar meaning in connection with a discussion of future operating or financial performance. These may include, among others, statements regarding:

- the impact of movement in commodity prices;
- exposure to falling residential energy consumption in the United Kingdom;
- changes in global economic conditions;
- the ability to operate in competitive markets;
- increased political intervention or regulatory oversight;
- technological developments and changing consumer behaviour;
- changes in weather patterns and other seasonal impacts;
- changes in production volumes;
- failure to fund investment, develop operational assets or identify, execute and finance acquisitions;
- exposure to decommissioning costs;
- changes and fluctuations in interest rates and exchange rates;
- expected capital expenditure spend; and
- changes in the Group's credit ratings.

These forward-looking statements are based on estimates and assumptions made by such entities that, although believed to be reasonable, are inherently uncertain. Therefore, undue reliance should not be placed upon any forward-looking statements. There are important factors that could cause actual results to differ materially from those contemplated by such forward-looking statements.

Important factors that could cause the Group's actual results of operations or financial condition to differ materially from those expressed or implied by forward-looking statements in this Offering Circular include, but are not limited to, the factors indicated in this Offering Circular under "Risk Factors" and "Operating and Financial Review" and include:

- general business and economic conditions globally;
- commodity price volatility;
- competition;
- management of HSSE performance, costs and liabilities;
- changes in government and other regulations; and
- changes in business strategy or development plans.

For further information regarding factors that could affect the business and financial results of the Group and such forward-looking statements, see "Risk Factors".

Such forward-looking statements speak only as of the date of this Offering Circular. Except as required by applicable law or regulation, the Company expressly disclaims any obligation or undertaking, and does not intend to release publicly any updates or revisions to any forward-looking statements contained in this Offering Circular, to reflect any change in the Group's expectations or any change in events, conditions or circumstances, on which any forward-looking statement contained in this Offering Circular is based.

USE OF PROCEEDS

The total net proceeds of the Offering, after underwriting commissions, are expected to be approximately $1,331,469,000.

The estimated fees and expenses related to the admission of the Notes to trading will be approximately $8,000.

The Group will use the net proceeds of the Offering for general corporate purposes, which may include (i) financing announced acquisitions; (ii) refinancing indebtedness originally incurred to finance completed acquisitions or (iii) refinancing other outstanding indebtedness.

BUSINESS DESCRIPTION

Overview

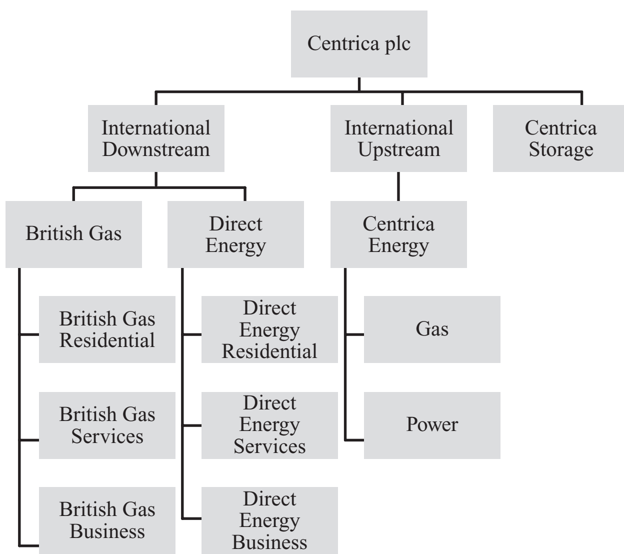
The Group is an integrated energy company that produces, sources and supplies gas and electricity for millions of residential and business customers in the United Kingdom and North America. The Group also provides a range of energy services solutions to its residential and business customers, including installation, maintenance, service and repair contracts, low-carbon and energy efficient products. Centrica was listed in 1997 on the London Stock Exchange following the demerger of the gas supply, service and retail businesses of British Gas plc together with its Morecambe gas field production activities. Since 1997, the Group has evolved significantly, shifting its primary focus from downstream activity in the initial years after listing towards becoming a leading integrated energy company in its chosen markets. The Group seeks to operate across the energy value chain from upstream production to downstream supply, although it focuses its operations on price-deregulated markets.

The Group's operations are broadly divided into three categories: International Downstream (British Gas in the United Kingdom and Direct Energy in North America), International Upstream (Centrica Energy) and Centrica Storage.

International Downstream operations involve the supply of energy to residences and businesses in the United Kingdom (excluding Northern Ireland) and North America and the provision of energy-related services to customers, including installation, maintenance, service and repair contracts, insurance and low carbon and energy efficient products. The Group's downstream operations principally operate under the British Gas and Direct Energy brands in the United Kingdom (excluding Northern Ireland) and North America, respectively.

International Upstream operations comprise exploration, development, production and processing of natural gas and oil assets and power generation. They also include the transaction of major procurement contracts to source gas from around the world for the UK and North American markets, and energy trading activities. The Group's upstream assets located in the UK, Canada, Norway, the Netherlands and Trinidad and Tobago, and procurement contracts provide a stable supply of gas and power to its downstream operations, which in turn, provide a market for the Group's upstream production.

Centrica Storage sells capacity in its Rough gas storage facility, along with ancillary services to customers who typically inject gas in the summer and withdraw during the winter for the UK market. The diagram below shows the Group's organisational structure:



The table below sets forth a breakdown of revenue and adjusted operating profit for the Group by segment for the six months ended 30 June 2013 and 2012 and for the years ended 31 December 2012, 2011 and 2010. Adjusted operating profit is a non-IFRS accounting measure, and should not be considered as an alternative to statutory operating profit as an indicator of the Group's results of operations or as an alternative to cash flows from operations as an indicator of liquidity. The Group's definition of adjusted operating profit may not be comparable to adjusted operating profit as used by other companies. For the

Group's definition of adjusted operating profit, see "Presentation of Financial and Other Information—Non-IFRS Financial Measures".

	Six months ended 30 June				Year ended 31 December					
	2013		2012		2012		2011		2010	
	(£m)	(% of Group)	(£m)	(% of Group)	(£m)	(% of Group)	(£m)	(% of Group)	(£m)	(% of Group)
	(unaudited)									
Revenue										
British Gas	7,842	57.4	7,146	59.7	13,716	57.3	12,315	54.0	12,725	56.7
Direct Energy	3,169	23.2	2,747	22.9	5,639	23.6	5,814	25.5	5,886	26.2
Centrica Energy	2,552	18.7	2,008	16.8	4,423	18.5	4,531	19.9	3,580	16.0
Centrica Storage	88	0.6	76	0.6	164	0.7	164	0.7	232	1.0
	13,651	**100**	**11,977**	**100**	**23,942**	**100**	**22,824**	**100**	**22,423**	**100**
Adjusted Operating Profit										
British Gas	569	35.9	563	38.9	1,093	39.8	1,005	41.6	1,216	50.9
Direct Energy	165	10.4	155	10.7	310	11.3	287	11.9	227	9.5
Centrica Energy	802	50.7	693	47.9	1,251	45.6	1,048	43.4	778	32.6
Centrica Storage	47	3.0	36	2.5	89	3.2	75	3.1	169	7.1
	1,583	**100**	**1,447**	**100**	**2,743**	**100**	**2,415**	**100**	**2,390**	**100**

History

Centrica was formed and listed on the London Stock Exchange in 1997 following the demerger of the gas supply, service and retail businesses of British Gas plc together with its Morecambe gas field production activities. The Group at the time comprised British Gas Trading Limited, British Gas Services Limited, British Gas Energy Centres Limited and Accord Energy Limited, together with the North and South Morecambe gas fields owned through Hydrocarbon Resources Limited and various other subsidiaries. Prior to the start of deregulation of the gas market in 1996, the business now owned by the Group also held the position of incumbent monopoly supplier of gas to homes and businesses in the UK.

Since 1997, the Group has evolved significantly. In the initial years after listing, the Group's focus was primarily on the downstream business. It further developed the British Gas brand and emphasised customer relationship management. In 2000, the Group entered the North American downstream market through the acquisition of its Direct Energy business. Since 2006, the Group's focus has shifted to becoming a leading integrated energy company in its chosen markets with an emphasis on downstream retail energy supply. Centrica Energy was created to consolidate upstream activity in the United Kingdom and the Group subsequently began acquiring various assets and developing onshore and offshore projects, particularly in the North Sea. In 2008, the Group completed a rights issue to fund additional upstream activity including the purchase of a 20 per cent. interest in British Energy and the acquisition of Venture Production plc. More recently, the Group has made further acquisitions of producing gas and oil assets, particularly in the Norwegian North Sea, as well as additional acquisitions in the North American market. In 2013, the Group reorganised its management structure along international business lines.

Strengths and Strategy

Strengths

The Group believes that it has the following key strengths:

Downstream scale and energy services

The Group benefits from the scale and strength of its downstream operations in the United Kingdom. Its principal brand, British Gas, was originally the market incumbent in gas supply and as of 30 June 2013 approximately 16.6 million residential and business gas and electricity accounts. The Group also had approximately four million energy services customers with 8.3 million product holdings. British Gas is the leading residential energy and services provider in Britain by number of customer accounts.

The UK energy market is price-deregulated, which allows the Group flexibility in reflecting its cost base in the tariffs charged to customers. The Group believes that its high profile brand, large scale, good customer service levels and unique energy services offering are key differentiating factors from many of its large competitors in the UK market. As a result, compared to its major competitors in the United Kingdom, the Group has above average operating margins, whilst remaining price competitive.

In North America, the Group is a large supplier of energy to residential customers in price-deregulated markets. In addition to benefiting from scale, the Group is able to share its UK and North American expertise across different competitive markets, which were deregulated more recently. It also offers energy related services, including maintenance and repair services, spread across 46 states and the District of Columbia in the United States and 10 provinces in Canada, differentiating it from many of its North American competitors.

Integrated business model

The Group is an integrated energy company with both upstream and downstream operations in multiple geographies. High-quality upstream assets and procurement contracts provide a stable supply of gas and power to its downstream operations, which in turn provide a ready market for the Group's upstream production. The Upstream business provides a natural economic hedge against exposure to energy price movements.

Upstream optionality

The Group maintains a low level of committed capital expenditure. Although it requires a certain level of capital expenditure to maintain upstream gas production, this can be adjusted in response to a variety of factors, including commodity prices and changes in risk profile. This approach also applies to other areas of the Group's upstream business, in particular UK power generation, allowing the Group to maintain valuable optionality in its levels of capital expenditure, with investment decisions made based on an assessment of available returns.

Financial strength

The Group benefits from a strong balance sheet, stable cash flow and an investment grade credit rating. The Group has leveraged these strengths into a comparatively low cost of funding, which has benefited the growth of both its upstream and downstream operations, organically and via acquisition. This financial strength has been beneficial to the Group in different areas. It has reduced funding costs, limited the amount of collateral required to access key commodity markets and contributed to the Group's ability to enter into agreements with key partners, including multi-year supply agreements with Statoil and Qatargas and, together with QPI, the acquisition of natural gas and crude oil assets in Canada.

Strategy

The Group's vision is to be the leading integrated energy company in its chosen markets, with customers at its core. In February 2013, the Group announced refreshed strategic priorities to position it for future growth, and moved to an international functional organisation with a new management structure aligned to its core competencies of upstream and downstream operations.

Innovate to drive service excellence and growth

The Group's downstream operations are at the core of its business. In order to maintain a market-leading position in its key markets, the Group aims to innovate and lead with high quality service and efficient operations. These goals are supported by the Group's technological capabilities, with the aim of enabling its customers to control their energy use in a simpler, more efficient way. The Group intends to build on its leading capabilities, facilitating growth in its selected markets, in the UK and particularly in North America, through a combination of organic growth and acquisitions.

Integrate its natural gas business, linked to its core markets

The Group's upstream business owns interests in gas and oil assets, and power assets. The Group intends to grow and diversify its gas and oil exploration and production portfolio and intends to maintain a low-carbon power hedge, investing where it sees value. The upstream business also plays an important role in managing the energy requirements of downstream customers, and the Group intends to develop its midstream business to integrate along the gas value chain.

Increase its returns through efficiency and continued capital discipline

The Group intends to continue developing organisational capability to optimise its resources to focus continually on safety, with the aim of delivering value to shareholders through efficient deployment of capital.

Principal Operations

The Group's operations are principally divided into International Downstream (which includes British Gas and Direct Energy), International Upstream (Centrica Energy) and Centrica Storage.

International Downstream—British Gas

The downstream UK business consists of three divisions, residential energy supply, residential services and business energy supply and services. These businesses operate under the name *British Gas* in England and Wales and *Scottish Gas* in Scotland under a combined management team with integrated support functions. British Gas is headquartered in Staines, England and its major regional offices are located in Cardiff, Wales; Manchester, England; Leeds, England and Edinburgh, Scotland.

The following table sets forth a breakdown of customer accounts, average and total gas consumption and average and total electricity consumption by division within British Gas for the six months ended 30 June 2013 and 2012 and for the years ended 31 December 2012, 2011 and 2010.

	For the six months ended 30 June		For the year ended 31 December		
	2013	2012	2012	2011	2010
Customer accounts ('000)					
Residential energy supply	15,674	15,785	15,618	15,881	15,978
Residential services	8,347	8,417	8,402	8,484	8,485
Business energy supply and services	912	974	924	999	1,044
Average gas consumption (therms/account)					
Residential energy supply	311	276	494	443	564
Business energy supply and services	1,480	1,581	2,737	2,629	3,152
Average electricity consumption (kWh/account)					
Residential energy supply	1,936	1,919	3,794	3,805	3,982
Business energy supply and services	14,651	13,507	27,521	25,732	29,326
Total gas consumption (mmth)					
Residential energy supply	2,763	2,515	4,460	4,099	5,291
Business energy supply and services	472	541	940	986	1,250
Total electricity consumption (GWh)					
Residential energy supply	13,146	12,987	25,683	25,602	26,002
Business energy supply and services	8,756	8,529	17,110	16,731	19,060

Liberalisation of the UK gas supply market began in 1996. Prior to liberalisation, British Gas was the United Kingdom's dominant gas supplier. Following the complete liberalisation of the UK gas and electricity markets in 1998, a period of industry consolidation amongst incumbent regional electricity companies followed, and the Group currently faces competition from EDF Energy, E.ON UK, npower, Scottish Power and SSE (together with British Gas, the "Big Six"), along with a number of other smaller suppliers. The Group competes with other suppliers on price, service and other value add propositions, such as energy services, smart technology and online capabilities. The Big Six supply approximately 98 per cent. of both gas and electricity to residential customers in the United Kingdom, and approximately 22 per cent. of gas and approximately 82 per cent. of electricity to business customers in the United Kingdom.

Regulation

Ofgem is the government regulator for electricity and downstream gas markets in the United Kingdom. Among other things, it is responsible for regulating the notification of price changes, conducting reviews and recommending reforms of various aspects of the retail market. It has broad enforcement powers, including the power to implement a fine of up to 10 per cent. of annual revenue for breaches of regulations. Ofgem does not regulate prices directly, therefore the Group is free to choose the tariffs it charges its customers. The Group does rely on the national grid networks for transportation and distribution of gas and power and pays fees regulated by Ofgem for such use.

On 27 August 2013, Ofgem announced its RMR requirements which are aimed at making the residential energy market simpler, fairer and more transparent for consumers. These requirements include, among other things, limiting the number of different tariffs offered by a gas or electricity supplier to four core tariffs, ensuring that dual fuel discounts are applied uniformly across all tariffs, creating uniformity across tariffs through the adoption of a standing charge and unit rate structure, providing customers with information about their energy tariffs and any available cheaper alternatives and banning unfair practices. Ofgem has also published regulations aimed at protecting small businesses from excessively high contract rates resulting from the automatic renewal of energy contracts by ensuring transparency and communication from energy suppliers. These regulations apply to all contracts entered into on or after 18 January 2010. The Group has implemented a number of the Ofgem requirements and is currently working to ensure that its operations align with best practices in the areas of concern to Ofgem.

Since April 2011, DECC has been overseeing the implementation of the smart meter programme, which is designed to provide consumers in the United Kingdom with detailed information about energy consumption. In May 2013, DECC extended the mandate for the installation of smart meters to 2020. British Gas has been at the forefront of the installation of smart meters, providing over one million smart meters to UK residences and businesses as of 30 June 2013.

As part of the UK government's focus on energy efficiency and low carbon solutions, Ofgem has implemented various "green" initiatives, including a requirement that the Group's downstream operations provide a proportion of their sales of electricity from renewable sources and must present Ofgem with sufficient Renewables Obligation Certificates to demonstrate their compliance with their Renewables Obligations or otherwise make a balancing payment. Until December 2012, major energy suppliers were obliged to participate in the CERT scheme and CESP. CERT aimed to improve domestic energy efficiency by achieving specified carbon reductions, while CESP targeted households in areas of social deprivation to improve energy efficiency and reduce fuel bills. Although the Group did not achieve the target completion date of December 2012, it has now completed all work under both schemes. In January 2013, CERT and CESP were replaced by ECO. ECO places legal obligations on the United Kingdom's principal energy suppliers to deliver energy efficiency measures to domestic energy users and requires energy suppliers to improve the insulation of harder to treat properties in the domestic sector and invest resources in reducing heating costs for vulnerable households.

As part of its energy services, British Gas Insurance Limited has been established as an insurer and British Gas Services Limited has been given authority to sell its insurance-based service and repair products. Both companies are regulated by the Financial Conduct Authority to carry out these functions. British Gas Insurance Limited is also overseen by the Prudential Regulation Authority.

Residential energy supply

British Gas Residential competes with the other Big Six suppliers, as well as certain smaller providers. Competitive positioning is based on brand recognition, the range of product propositions offered, the quality of service delivered to customers and the retail price. Each energy supplier is free to set its own retail prices in a fully competitive market.

As at 30 June 2013, British Gas Residential had 15.7 million energy accounts on supply, with 8.8 million gas customers and 6.8 million electricity customers. It is currently the largest supplier of gas and electricity to customers in Britain's deregulated domestic market, with an estimated share of approximately 39 per cent. of the UK residential gas supply market and approximately 25 per cent. of the UK residential electricity supply market. Average gas consumption in 2012 was 494 therms per account and average electricity consumption in 2012 was 3,794 kWh per account.

Residential customers are offered a choice of tariffs. Approximately 85 per cent. of British Gas Residential's energy accounts are on a "variable" tariff, which can be moved up or down to reflect changing costs (with 30 working days' notice required if the tariff move is upwards). The remaining 15 per cent. of the British Gas Residential's energy accounts are on "fixed" tariffs, which remain at the same rates for a fixed term (typically for up to two years from the date of choosing the tariff). The Group analyses various factors in determining tariffs, including wholesale energy costs, transportation and distribution charges, environmental and social policy costs and operating costs, and seeks to maintain a consistent operating margin, given the competitive environmental permits.

The majority of British Gas Residential customers either pay upon receipt of an invoice by cash or cheque or spread the payment profile over a year with equal monthly direct debits. The Group estimates that 17 per cent. of its residential customers are on Pay As You Go tariffs. These customers are provided with cards which can be loaded with funds at certain retail outlets or online and, when inserted in the Pay As You Go meter, ensure the delivery of power and gas.

British Gas Residential's strategy is focused on delivering good customer service, reducing its cost base and providing an attractive environment for employees. Customer service and costs are also managed through customer segmentation. This segmentation helps the Group to develop a better understanding of each customer type and offer the appropriate service and proposition. The segmentation does not affect the tariff options available to the customer. The call centres operated by British Gas Residential together with digital and online platforms, are an essential component of the customer service offering and address customer queries and any complaints. The call centres are organised by customer segment and provide a tailored approach for each type of customer. In recent years, British Gas Residential has worked to improve its online and digital offerings, including added features on its customer website and provision of a British Gas "app" to allow customers to manage their accounts on smart phones. In addition, controls to ensure the confidentiality, availability and integrity of customer and company data remain a core element of system development and service provision.

British Gas Residential's commodity procurement requirements are sourced from the market through Centrica Energy's midstream business. Hedging is typically undertaken up to 24 months in advance, with a larger proportion of the requirements covered by hedges as the time of delivery approaches.

Residential services

The Group believes that British Gas Services is one of the United Kingdom's biggest national providers of energy related maintenance and breakdown services for the home, with approximately 8.3 million product holdings supplied to approximately four million households as of 30 June 2013 and directly employing approximately 9,000 engineers nationwide. British Gas Services provides maintenance and repair contracts and on-demand services for boilers and central heating, as well as plumbing and drains, home electrics and kitchen appliances. British Gas also has its own insulation/cladding business and interests in a range of new energy technologies, with investments in biomass heating, solar, and fuel cell boilers. It owns the franchise business Dyno-Rod, a UK plumbing and drainage specialist. In addition to central heating maintenance and repair contracts and on-demand services, British Gas Services installed 94,000 boilers in 2012 and the Group believes that it is one of the United Kingdom's largest installers of domestic central heating boilers and systems.

British Gas Services' profits are derived principally from its insurance product offerings which cover boilers, heating, plumbing and drains and home electrics, but supplemented by other activities such as "on-demand" call-out services and installation of micro-generation and energy efficiency measures. In April 2013, British Gas Services announced the launch of a British Gas branded home insurance product in partnership with Axa Insurance.

Business energy supply and services

The Group believes that, through British Gas Business, the Group is the largest supplier (by numbers of meter points) for gas and electricity to the UK commercial sector. As of 30 June 2013, British Gas Business supplied gas and electricity to 912,000 supply points, which includes 317,000 gas supply points and 595,000 electricity supply points. British Gas Business customers are predominantly small- to medium-sized businesses and public institutions. Average gas consumption in 2012 was 2,737 therms per supply point and average electricity consumption in 2012 was 27,521 kWh per supply point. Tariffs for business customers are typically sold on a fixed-length contractual basis, usually for a period of between one and three years. Once contracts are signed, the Group locks in the commodity cost for the contractual period. Like British Gas Residential, British Gas Business's commodity procurement requirements are undertaken by Centrica Energy's midstream business.

British Gas Business also continues to develop its services propositions and offers maintenance and compliance services, as well as emergency care for its business customers. Additionally, the business delivers Energy Performance Contracts which offer energy efficient products and services to business customers in order to generate consumption savings. British Gas Business also provides heating and electrical installation and maintenance services to domestic social housing properties owned and managed by local authorities and housing associations.

International Downstream—Direct Energy

In August 2000, the Group entered the North American market with the acquisition of Direct Energy Marketing Limited. Direct Energy remains the Group's principal customer brand in the region and has expanded significantly since 2000 through further acquisitions and organic growth.

Direct Energy supplies energy and related services to residential and business customers across the United States and Canada under the Direct Energy and other brand names. Direct Energy is organised into three pan-North American lines of business: Direct Energy Residential, Direct Energy Business and Direct Energy Services. Direct Energy is headquartered in Houston, Texas with major regional offices in Pittsburgh, Pennsylvania; Sarasota, Florida; Columbus, Ohio; Calgary, Alberta and Toronto, Ontario. The Group owns three gas-fired combined cycle gas turbine ("CCGT") power stations in Texas (the Bastrop, Frontera and Paris Energy Centres) with a total capacity of 1,305MW, and has 684MW of wind farm off-take agreements elsewhere in Texas. Direct Energy is also involved in energy management and procurement activities, wholesale energy trading and midstream gas activities (including managing storage and transportation capacity) in North America.

The following table sets forth a breakdown of customer numbers by division within Direct Energy as at and for the six months ended 30 June 2013 and 2012 and as at and for the years ended 31 December 2012, 2011 and 2010.

	For the six months ended 30 June		For the year ended 31 December		
	2013	**2012**	**2012**	**2011**	**2010**
Residential energy supply					
Customer numbers ('000)	3,397	3,240	3,455	3,364	2,855
Business energy supply					
Gas sales (mmth)	494	421	793	714	633
Electricity sales (GWh)	27,999	23,935	51,378	46,350	39,722
Residential and business services					
Contract relationships ('000)	2,441	2,390	2,401	2,283	2,300

Regulation

Regulatory approaches in the North American energy markets vary by jurisdiction and regulator. However, Direct Energy focuses predominantly on price-deregulated markets. Direct Energy also supplies gas or electricity to businesses in 14 states in the United States and four provinces in Canada. Its principal residential supply markets include Texas, the north-eastern and mid-western United States and the Canadian provinces of Ontario and Alberta. The Direct Energy businesses operate under an extensive group of licences. In the United States, each state that has partially opened its markets to energy competition has done so under a separate regulatory scheme. Each jurisdiction has also promulgated its own regulations around commodities. As a result, each Direct Energy business, and almost every brand, is associated with a licence that is unique to that brand, the relevant state or province, and type of contract sold as well as to the type of consumer. In addition, Direct Energy's supply and trading business is regulated by several federal agencies which require periodic reporting. Direct Energy is one of North America's largest energy and energy related services providers. Direct Energy's main competitors vary by state, typically consisting of incumbent utilities and smaller competitive retailers.

Residential energy supply

Direct Energy Residential has been built from three major acquisitions—Direct Energy in 2000, CPL Retail Energy LP and WTU Retail Energy LP in Texas in 2002 and the acquisition of one million residential gas and electricity customers in Alberta from the ATCO Group in 2004. These major acquisitions have been supplemented with further acquisitions, including Gateway, First Choice Power and Vectren Retail in 2011, Energetix and NYSEG Solutions, Inc. in 2012 and Bounce Energy in 2013, as well as by organic growth.

As of 30 June 2013, Direct Energy Residential supplied natural gas and electricity to 3.4 million residential customers, predominantly in the north-eastern and mid-western United States, Texas, and the Canadian provinces of Alberta and Ontario. Average gas consumption in 2012 was approximately 1,292 therms per account and average electricity consumption in 2012 was approximately 11,362 kWh per account.

Direct Energy offers both fixed and variable electricity and gas prices to residential customers. Prices are set monthly for forward sales and supply, and Direct Energy analyses various factors in determining prices, including prior usage, estimated future consumption, commodity and non-commodity prices and the competitive environment.

The gas and electricity requirements for residential energy customers in North America are procured from the market by the Direct Energy midstream and trading business, which is reported externally as part of the Direct Energy business. In addition, downstream residential energy supply is supported by Direct Energy's three gas-fired power stations and wind offtake power purchase agreements in Texas.

Business energy supply

Direct Energy Business supplies natural gas and electricity to small, medium and large sized businesses, as well as public institutions and government entities, in 15 states and the District of Columbia in the United States and four provinces in Canada. As of 30 June 2013, Direct Energy Business had 0.4 million business accounts. Total gas consumption in 2012 was approximately 793 therms and total electricity consumption in 2012 was approximately 51,378 GWh. Small businesses are offered fixed price electricity and gas contracts, that are set for terms typically ranging from 12 to 24 months, whereas rates for larger businesses are individually negotiated by contract and can allow for prices to be set for as long as five years. Larger business customers are offered a variety of pricing options that include both fixed price and variable pricing products. The fixed price products offered by Direct Energy Business provide large business customer the ability to lock in electricity and gas prices for the full term of their contract up front through a negotiated fixed rate. The variable pricing products offered by Direct Energy Business allow customers to have their prices vary during the entire contract term by tying their electricity and gas rates to established wholesale market indices for these commodities. Like Direct Energy Residential, the energy requirements of Direct Energy Business customers are procured from the market by the Direct Energy midstream and trading business.

In July 2013, the Group announced that it had agreed to acquire the energy marketing business of Hess Corporation for US$731 million in cash plus net working capital, estimated at approximately US$300 million. In 2012, Hess Corporation's energy marketing business supplied over 370 bcf of gas and 28 terawatt hours of power to more than 23,000 customers across 18 states, and also has an extensive portfolio of existing gas and power contracts. The acquisition, which will make Direct Energy the largest business gas supplier in the Eastern United States, is expected to close during the fourth quarter of 2013, subject to regulatory approvals being received and other conditions to closing being satisfied.

Residential and business services

Direct Energy Services was created from three key acquisitions—Enbridge Services Inc., an Ontario home and business services company, in 2002, Residential Services Group, a home services business in the United States, in 2004, and Clockwork Home Services Inc., a home services and franchise business, ("Clockwork"), in 2010. Clockwork provides on-demand services across the United States and Canada supplying heating, cooling, plumbing and electrical services through its wholly owned retail operations, franchise operations and affinity programme for independent contractors. In addition, Direct Energy acquired Home Warranty of America in March 2012 and now has the necessary licences to offer protection plan products across the United States, providing a further platform for growth. On 5 September 2013, Direct Energy announced that it had agreed to acquire AWHR, the largest independent water heater rental business in the US for US$30 million in cash, plus working capital. As of 30 June 2013, Direct Energy Services provided heating, ventilation and air-conditioning services, plumbing, electrical appliance repair, home protection plans and energy advisory activities to 3.1 million households and businesses in 46 states and the District of Columbia in the United States, and 10 provinces in Canada. Many of these take the form of annual or multi-year maintenance contracts, entitling customers to seasonal system checks and tune-ups, and on-demand repair or replacement services. The Group considers that the Direct Energy Services brands are distinct from competitors due to their "on time" model, whereby customers can select guaranteed appointment times for a premium. In addition to the requirement to provide suitable appointment times, Direct Energy Services' contractual and on-demand pricing structure is dependent upon a variety of factors, including the cost of its systems, parts and labour.

International Upstream—Centrica Energy

Centrica Energy owns a number of gas and oil production assets in the United Kingdom, Norway, the Netherlands, Canada and Trinidad and Tobago. The Group also has gas-fired power stations in the United Kingdom, onshore and offshore wind farms in the United Kingdom and a 20 per cent. equity stake in EDF Energy Nuclear Generation, which operates eight UK nuclear power stations in the UK. Centrica Energy sources the gas and electricity needed for British Gas to supply energy to its residential and business customers, and for wholesale and certain industrial gas sales activities, energy procurement optimisation and scheduling operations in all of the Group's markets outside of North America.

Regulation

Centrica Energy's upstream gas and liquids production is sold into price-deregulated markets or to the Group's downstream operations at market prices. The regulation of licences, safety standards and other operational matters is administered by various government bodies, depending on the jurisdiction. The main regulators for the Group's upstream exploration and production businesses are currently DECC and the Health and Safety Executive in the United Kingdom, the Ministry of Petroleum and Energy in Norway, the Petroleum Safety Authority in Norway, the State Supervision of Mining in the Netherlands, the Ministry of Economic Affairs in the Netherlands, the Alberta Energy Regulator in Canada and the Ministry of Energy and Energy Affairs in Trinidad and Tobago. The Group's midstream operations are also subject to regulation by Ofgem and the FCA. Centrica Energy's production businesses use its midstream business to access external markets or sell its production to the Group's Downstream operations.

The upstream power market in the UK is also price deregulated. Power generation is primarily regulated by Ofgem and DECC. Regulation in the UK power market to date has thus far been limited to the Renewables Obligation. This regulatory profile is changing with the introduction of the UK Energy Bill. In November 2012, an energy bill was introduced in the UK parliament based on DECC proposals providing the framework for EMR. The key elements of EMR include Feed-in-Tariffs with Contracts for Difference to support investment in low carbon generation and a mechanism to support the security of supply, including through the use of a capacity market. In June 2013, the UK government announced further details of the UK Energy Bill, in particular draft Contract for Difference strike prices applicable to renewable power generation, including offshore wind projects. The Group is awaiting the final outcome of the consultation to determine the impact that this will have on its investment plans.

Exploration and production

The following table sets forth a breakdown of production volume by energy source for the six months ended 30 June 2013 and 2012 and the years ended 31 December 2012, 2011 and 2010.

	For the six months ended 30 June		For the year ended 31 December		
	2013	2012	2012	2011	2010
Production volumes					
Gas production (mmth)	1,696	1,427	2,990	2,727	2,959
East Irish Sea	344	362	740	817	1,381
Other UK and Netherlands	541	480	883	933	917
Norway	436	176	557	164	175
Canada	252	279	549	567	409
Trinidad and Tobago	123	130	261	246	77
Liquids production (mmboe)	9.8	7.5	17.4	13.2	12.3
UK and Netherlands	3.5	3.9	7.4	7.8	8.5
Norway	5.8	3.0	8.9	4.7	3.3
Canada	0.5	0.6	1.1	0.7	0.5
Hydrocarbon volumes (mmboe)	37.6	30.9	66.8	58.2	64.2
Power generated (GWh)	10,584	11,106	21,489	26,726	32,934
Gas-fired	4,531	4,906	8,952	14,973	22,786
Renewables	290	246	533	596	493
Nuclear	5,763	5,954	12,004	11,157	9,655
Average sales price (Europe, Trinidad & Tobago)					
Gas (p/therm)[(1)]	—	—	54.7	51.6	41.6
Liquids (£/boe)[(1)]	—	—	62.8	57.2	46.8
Achieved gas-fired CSS (£/MWh)	10.0	10.3	10.7	10.1	11.6
Nuclear power price (£/MWh)	52.1	49.2	49.6	48.5	42.9

Note:

(1) On 27 February 2013, the Group changed its segmental reporting to reflect the Group's new organisational structure and to align with management reporting. As a result, average sales price for gas and liquids for Europe and Trinidad and Tobago are no longer reported separately.

The Group has equity interests in approximately 55 producing gas and oil fields in United Kingdom, Dutch, Trinidadian and Norwegian waters and approximately 4,500 oil and gas wells in Canada, as well as a number of development projects and gas exploration licences. The Group's share of estimated total net proven and probable gas and oil reserves were 663 mmboe as at 31 December 2012 (2011: 549 mmboe), 108 mmboe of which is in Canada and 30 mmboe of which is used as cushion gas for Centrica Storage's Rough facility in the United Kingdom. This includes the impact of three North Sea acquisitions completed in 2012 for total consideration of £1.2 billion, which had estimated reserves of 167 mmboe as at the end of 2012.

The Group operates certain of its gas and oil fields and is a joint venture partner in the remaining fields. The following table sets out Centrica Energy's principal producing gas and oil fields:

Region	Fields
East Irish Sea	• South Morecambe • North Morecambe
Central and Northern North Sea	• Greater Kittiwake Area (Kittiwake, Mallard, Goosander and Grouse) • Armada • Chestnut
Southern North Sea	• A fields • York
Norway	• Stafjord • Kvitebjorn • Vale
Netherlands	• Greater Markham Area (GMA) • F3-FA/SIP
Canada	• Foothills • Peace River Arch • Hanlan-Robb • North (Carrot Creek) • South (Medicine Hat)
Trinidad and Tobago	• NCMA Unit Area (Hibiscus, Poinsettia, Chaconia, Bougainvillea and Heliconia)

The Group's principal approved development projects are Valemon (Group share of reserves: 21 mmboe) in Norway and Cygnus (53 mmboe), Kew (7 mmboe) and Grove (5 mmboe) in the United Kingdom. Kew is expected to commence production in the fourth quarter of 2013, Valemon and Grove are expected to commence production in 2014, and Cygnus is expected to commence production in 2015.

In April 2013, the Group announced that, together with Qatar Petroleum International ("QPI"), the international arm and wholly owned subsidiary of Qatar Petroleum, agreed to acquire a package of producing conventional natural gas and crude oil assets and associated infrastructure located in the Western Canadian Sedimentary Basin from Suncor Energy for C$1 billion (£650 million) in cash. The transaction closed in late September 2013. The assets are in a newly established partnership between Centrica (60 per cent. share) and QPI (40 per cent. share), and will be operated by Centrica. The assets include proven and probable reserves estimated by the partners at 978 billion cubic feet equivalent ("bcfe") (90 per cent. natural gas) and 9 mmboe of production. The transaction is expected to add approximately 1,200 oil and gas wells to the Group's holdings in Canada. In June 2013, the Group also announced that it had acquired a 25 per cent. interest in the Bowland shale exploration licence in Lancashire from Cuadrilla Resources Ltd. and AJ Lucas for £40 million.

The Group's own gas production in Europe is currently equivalent to over 50 per cent. of British Gas retail gas demand. Following the acquisition of assets located in the Western Canadian Sedimentary Basin from Suncor Energy but prior to completion of the acquisition Hess Corporation's energy marketing business, the Group's own production in North America is expected to be able to meet around 50 per cent. of Direct Energy's total downstream gas demand. All of Centrica Energy's upstream production in Europe is passed to Centrica Energy's midstream business at market prices. Hedging is typically undertaken up to 24 months in advance, with a larger proportion of the requirements covered by hedges as the time of delivery approaches. In Canada, production is passed through to Direct Energy's midstream business.

Power

In addition to the Group's exploration and production assets, Centrica Energy operates a number of power generation assets, enabling it to deliver a balanced mix of energy supply.

The following table sets out Centrica Energy's principal power generation assets, all of which are located in the United Kingdom:

Type	Station
Gas-fired (combined cycle gas turbine power stations)	• South Humber Bank • Barry • Glanford Brigg • Killingholme • Langage • Peterborough • Kings Lynn (mothballed) • Roosecote (mothballed)
Offshore Wind Farm	• Barrow (50% equity interest) • Lynn (50% equity interest) • Inner Dowsing (50% equity interest) • Lincs (50% equity interest)
Onshore Wind Farm	• Glens of Foudland (50% equity interest)
Nuclear Power Generation (20% equity interest in Lakeland Acquisitions Limited (British Energy))	• Hartlepool (expected closure 2019) • Heysham 1 (expected closure 2019) • Hinkley Point B (expected closure 2023) • Hunterston B (expected closure 2023) • Dungeness B (expected closure 2018) • Heysham 2 (expected closure 2023) • Torness (expected closure 2023) • Sizewell B (expected closure 2035)

The Group owns and operates six gas-fired power stations in England and Wales, with a combined output of 3.7GW. The company also owns the King's Lynn and Roosecote power stations, which were mothballed in 2012 due to market conditions.

The Group also produces renewable power through five joint venture wind farms, of which Centrica's equity share of capacity is 290MW of power. These include the 270MW Lincs offshore wind farm, a joint venture with DONG and Siemens Project Ventures in which the Group owns 50 per cent., from which first power was generated in August 2012 and which is expected to be fully commissioned by the end of 2013. Race Bank, which is the Group's next potential offshore wind project, received planning consent in July 2012, with the development of this project dependent on the investment climate for offshore wind following completion of EMR.

In November 2009, the Group completed the purchase of a 20 per cent. equity stake in Lake Acquisitions Limited (the vehicle through which EDF acquired British Energy) from EDF, for total consideration of £2.3 billion. The acquisition gave the Group rights to 20 per cent. of the total output from EDF's eight nuclear power stations. Since the acquisition, four of the eight power stations have received life extensions of either five or seven years, and current expected close dates for the eight power stations are now between 2018 and 2035. The acquisition also included the right to take up an interest of up to 20 per cent. in a joint venture, NNB Holding Company Limited, to pursue a planned programme to build up to four new nuclear power stations in the United Kingdom. The Group decided not to exercise this option and announced its decision on 4 February 2013.

The aggregate peak output of the Group's own sources of generation in Europe (including its share of the output from British Energy and the other long-term contractual arrangements in the United Kingdom) is equivalent to around 70 per cent. of British Gas residential and business peak electricity demand. All of Centrica Energy's power generation output is passed to Centrica Energy's midstream business at market prices. Hedging is typically undertaken up to 24 months in advance, with a larger proportion of the requirements covered by hedges as the time of delivery approaches.

Centrica Energy midstream

Centrica Energy's midstream operations are responsible for procurement and contracting for energy in the United Kingdom, along with asset-backed optimisation and trading, and principally operates as Centrica

Energy Limited and British Gas Trading Limited. It trades with the major participants in the wholesale European energy markets. Centrica Energy's midstream business is responsible for accessing the external markets on behalf of both the Group's upstream and downstream operations. The Group regularly enters into commodity purchase and sale contracts, including gas and electricity contracts with a number of international energy companies, to supplement energy produced by its own upstream assets.

Centrica Energy also sources energy on behalf of the Group's downstream operations in the United Kingdom. To do this, Centrica Energy uses a combination of the Group's long-term procurement contracts and short-term arrangements to balance energy supplies and customer demand and to optimise the price paid by the Group. To offset adverse fluctuations in prices, the Group also enters into various hedging agreements, including gas storage, and utilises over-the-counter and exchange-traded instruments to optimise the prices paid by the Group.

In gas, the Group has an existing 10-year gas purchase contract with Statoil for the supply of 5 billion cubic metres of gas per year. Upon the contract's expiration in 2015, a new 10-year supply contract with Statoil will come into effect. Under this new contract, Statoil will supply 50 billion cubic metres of gas per year. The Group also has a 10-year contract with GasTerra to deliver 8 billion cubic metres of gas per year through 2016 and a three-year contract with Qatargas to deliver 2.4 million tonnes of liquefied natural gas ("LNG") to the United Kingdom per year through mid-2014. Prices under all of these contracts are linked to the National Balancing Point ("NBP") market price, the price in pence per therm at which gas is traded in the United Kingdom. Contracts and opportunities are reviewed periodically with existing and potential suppliers to optimise supply arrangements and secure supplies for the Group's requirements. In March 2013, the Group announced an agreement with Cheniere Energy Partners L.P. to purchase 91,250,000 mmbtu of annual LNG volumes for export from Sabine Pass in Louisiana in the United States. The Cheniere contract is subject to a number of conditions precedent, including Cheniere receiving necessary regulatory approvals, securing finance, making a final investment decision and issuing a notice to proceed with the fifth LNG train. Should these conditions not be met within a specified time-frame, the Group has the right to withdraw from the deal with no penalty.

Centrica Energy also has capacity rights in the UK-Continent Interconnector pipeline between Bacton on the Norfolk coast and Zeebrugge in Belgium as well as capacity rights at the Isle of Grain LNG regasification terminal. In power, Centrica Energy has tolling agreements in respect of the Spalding power station in the United Kingdom and Rijnmond power station in the Netherlands, and a coal-priced electricity supply contract with Drax Power Limited, owner of the Drax power station in North Yorkshire, England, which provides the Group with access to 300MW of power until September 2015.

Storage UK

Centrica Storage Limited, a wholly owned subsidiary of Centrica, operates the Rough gas storage facility, a seasonal storage facility acquired by the Group in November 2002. The facility consists of a partially depleted gas field (the "Rough Field") in the Southern North Sea ("SNS"), together with an onshore gas processing terminal at Easington. Centrica Storage sells capacity in the Rough storage facility as well as ancillary services to customers who typically inject gas in the summer when prices are lower and withdraw during periods and days when prices are favourable. Customers include energy producers, energy users, traders and suppliers. The Rough storage facility comprises approximately 70 per cent. of the seasonal storage capacity available in the UK market. In addition to providing storage products, Centrica Storage also provides gas processing services for the York field in the SNS.

Following the acquisition by the Group of the Rough facility and a subsequent Competition Commission inquiry, undertakings were given by the Group and Centrica Storage to the Secretary of State for Trade and Industry in 2003 which place certain obligations on Centrica Storage and the Group in respect of the storage business. The undertakings require Centrica Storage to be legally, financially and physically separate from all other Centrica businesses. In particular, Centrica Storage's commercial team is separated from the parts of the Group that deal in gas supply, gas shipping, trading and storage procurement. In addition, there are restrictions prohibiting the disclosure by Centrica Storage of commercially sensitive information to other parts of the Group and prohibiting the solicitation or making use of such information by other parts of the Group. In line with its obligations, Centrica Storage makes available the majority of capacity within the Rough facility to users other than Group companies. In April 2011, the Competition Commission published its final decision on the Group's request for a review of the undertakings based on changes in the gas market since 2002 and the introduction of the EU Third Energy Package. In March 2012, the Company and Centrica Storage signed amended undertakings with certain variations which included an increase in the proportion of capacity that can be purchased by other parts of the Group, the introduction of a mechanism for Ofgem to agree to allow some capacity to be sold as non-Standard Bundled Unit ("SBU") products and a change in the minimum reserve price for auctions of unsold capacity.

In addition, on 23 September 2013, the Group announced its decision not to proceed with its new-build gas storage project at Baird in the UK Southern North Sea and to put its project at Caythorpe in East Yorkshire on hold indefinitely. This decision was taken in light of weak economics for storage projects and the announcement by the UK government on 4 September 2013 ruling out intervention in the market to encourage additional gas storage capacity to be built. As a result of this decision, the Group will write off all costs incurred and committed on these projects and expects to recognise impairments and provisions totalling approximately £240 million as an exceptional cost in the Group's 2013 preliminary financial results.

Reserves and Resources

The Group discloses proven and probable ("2P") gas and liquids reserves, representing the central estimate of future hydrocarbon recovery. Reserves for Centrica-operated fields are estimated by in-house technical teams composed of geoscientists and reservoir engineers. Reserves for non-operated fields are estimated by the operator, but are subject to internal review. An annual reserves assessment has been carried out by DeGoyler and MacNaughton for the Group's global reserves.

European and Trinidad and Tobago reserves estimates are consistent with the guidelines and definitions of the Society of Petroleum Engineers, the Society of Petroleum Evaluation Engineers and the World Petroleum Council's Petroleum Resources Management System using accepted principles. North American reserves estimates have been evaluated in accordance with the Canadian Oil and Gas Evaluation Handbook ("COGEH") reserves definitions and are consistent with the guidelines and definitions of the Society of Petroleum Engineers and the World Petroleum Council.

The following table sets forth the Group's total proven and probable gas and liquids reserves as at 31 December 2012:

	Europe	Trinidad & Tobago[3]	Centrica Energy	Centrica Storage[6]	Direct Energy	Total
Estimated net 2P reserves of gas (bcfe)						
1 January 2012	1,858	161	**2,019**	182	603	**2,804**
Revisions of previous estimates	(73)	(2)	**(75)**	—	(10)	**(85)**
Purchases/(disposals) of reserves in place[1]	632	—	**632**	—	37	**669**
Extensions, discoveries and other additions[2]	39	—	**39**	—	5	**44**
Production[4]	(220)	(19)	**(239)**	—	(54)	**(293)**
31 December 2012	2,236	140	**2,376**	182	581	**3,139**
Estimated net 2P reserves of liquids (million barrels)						
1 January 2012	73	—	**73**	—	8	**81**
Revisions of previous estimates	6	—	**6**	—	2	**8**
Purchases/(disposals) of reserves in place[1]	55	—	**55**	—	2	**57**
Extensions, discoveries and other additions[2]	10	—	**10**	—	—	**10**
Production[4]	(15)	—	**(15)**	—	(1)	**(16)**
31 December 2012	129	—	**129**	—	11	**140**
Estimated net 2P reserves (million barrels of oil equivalent)						
31 December 2012[5]	502	23	**525**	30	108	**663**

Notes:

(1) Reflects the acquisition of additional equity in the Statfjord, Seymour, Armada, Skirne, Vale, Heimdal and Maria fields and the acquisition of equity in the Alba, Kvitebjorn and Valemon fields in Centrica Energy and the Carrot Creek field in Centrica Energy.

(2) Recognition of reserves associated with the Rhyl and Maria fields in Centrica Energy.

(3) The Trinidad and Tobago reserves are subject to a production sharing contract and accordingly have been stated on an entitlement basis (including tax barrels).

(4) Represents total gas and oil produced from the Group's reserves.

(5) Includes the total of estimated gas and liquid reserves at 31 December 2012 in mmboe.

(6) Includes reserves at the Rough storage facility.

Intellectual Property

As part of the demerger in 1997, BG Group plc assigned certain British Gas trademarks and related logos to GB Gas Holdings Limited (a Centrica Group company) for use in the UK. BG Group plc and its subsidiaries have retained ownership of the trademarks and logos in the rest of the world and remain free to use the British Gas trademarks and logos both outside the UK and within the UK for limited purposes relating to their businesses in the rest of the world (subject to certain guidelines agreed with Centrica). Similarly, Centrica and its subsidiaries may use the British Gas name outside of the UK for limited purposes relating to their businesses within the UK, subject to guidelines agreed with BG Group plc.

BG Group plc and Centrica have each undertaken to observe high standards of quality in the goods and services they supply under the British Gas brand, to observe high standards of business ethics in their corporate affairs and, in particular, not to act in a way which is likely to bring the brand into disrepute. BG Group plc and Centrica both have the right to call for all British Gas trademarks and related logos to be assigned to them if control of the other party is acquired by a third party.

In addition to the British Gas trademarks and logos, the Group trades under various other well-known brands, such as Dyno in the United Kingdom and Direct Energy in the United States and Canada. The Group regards the protection of its trademarks and domain names as critical to its success, and relies on all appropriate laws to protect and enforce its proprietary rights.

Health, Safety, Security and Environment ("HSSE")

The Group's operations are inherently hazardous and, as a result, safety is a top priority for Centrica. The Group has ongoing campaigns to raise awareness of process safety risks in its business and in 2012 introduced two programmes (Generation Safe and Live Safe) to strengthen internal views towards safety and reporting unsafe conditions in its upstream business. The Group also undertakes targeted programmes to address specific hazards and monitors and reports regularly on safety metrics. In 2012, the Group had a lost-time injury frequency rate ("LTIFR") of 0.20 per 100,000 hours worked as compared to a LTIFR of 0.45 and 0.25 in 2010 and 2011, respectively. In 2012, the Group had no fatalities at its operations and no significant process safety events, which are defined as an uncontrolled release of flammable gas, steam or hot water under pressure causing a major injury or fatality or the uncontrolled release of an environmentally hazardous substance causing significant impairment of sensitive receivers. The majority of safety risks in the Group's downstream businesses are from working in customers' homes where the integrity of appliances and working conditions is unknown and from road accidents.

The Group is committed to understanding, managing and reducing the environmental impact of its activities through innovation, technology and cultural change through the implementation of environmental management systems ("EMS") throughout its operations. In 2012, the Group maintained its existing ISO 14001 certifications and achieved ISO 14001 certifications in additional areas of its business. In 2012, Centrica was involved in 45 incidents of non-compliance with environmental regulations, the majority of which were minor incidents in the United Kingdom, a decrease from 47 incidents in 2011. In 2010, 30 incidents were reported. The increase in reported incidents between 2010 and 2011 was primarily due to improved reporting processes. During 2013, the Group is undertaking a global biodiversity status review of establish the sensitivity of its operations and the environments in which it operates to enhance the Group's understanding of any environmental impacts and focus on additional mitigation or protection efforts that may be required or that may otherwise be beneficial. The Group is currently remediating contamination at certain of its well sites in Canada, although the Group does not believe that the costs associated with such remediation will materially exceed the related provisions therefor.

The Group's power generation, offshore drilling, hydraulic fracturing and other operations are subject to numerous regulations governing, among other things: (a) the development and operation of high hazard facilities and associated process safety requirements; (b) the generation, storage and handling of hazardous materials and wastes; (c) decommissioning and decontamination of its facilities and assets; (d) air emissions, including of greenhouse gases and other pollutants; (e) the health and safety of the public and its employees; and (f) the generation of electricity, and these regulations may change or increase in the future. The Group is also committed to addressing the challenge of climate change and contributing to government greenhouse gas emission reduction targets that have been set at the UK and European levels. This involves reducing emissions within Centrica's operations, as well as helping customers cut emissions from energy use. Centrica calculates its internal carbon footprint, which encompasses emissions from office energy use, company vehicles and business travel, but does not include emissions from the Group's power stations or gas and oil operations. The Group aims to reduce its internal carbon footprint by 20 per cent. by 2015. In 2012, Centrica's internal carbon footprint was 91,988 tonnes of CO2 equivalent, a 2 per cent. reduction from 2011 (94,092 tonnes). In 2012, the Group's total carbon emissions, which includes those from power generation and gas and oil production was 7.4 million tonnes of CO2 equivalent, compared to 8.1 million tonnes in 2011. This was in part due to the mothballing of King's Lynn and Roosecote power stations due to challenging market conditions. Centrica is also enabling customers to reduce carbon emission by deploying energy efficient measures and other smart technologies, such as the installation of smart meters. In addition, as a result of the work completed under CERT and CESP, Centrica has delivered 102 million tonnes of carbon savings over the life of these programmes.

Employees

For the year ended 31 December 2012, the Group employed an average of 38,642 people worldwide. The following table sets forth a breakdown of employees by business for the years ended 31 December 2012, 2011 and 2010.

	Year ended 31 December		
	2012	**2011**	**2010**
British Gas	30,305	31,278	27,298
Direct Energy[1]	6,243	6,206	5,534
Centrica Energy[1]	1,788	1,658	1,556
Centrica Storage	306	290	255
Other	—	—	327
	38,642	**39,432**	**34,970**

Note:

(1) On 27 February 2013, the Group changed its segmental reporting to reflect the Group's new organisational structure and to align with management reporting. The North American Upstream Gas business has been reallocated from the "Direct Energy—Upstream and wholesale energy" subsegment to the "Centrica Energy—Gas" subsegment. The employee numbers presented in the table are prior to this resegmentation.

For the year ended 31 December 2012, approximately 42 per cent. of the Group's employees in the United Kingdom and North America were members of trade unions. The Group's operations have relationships with a number of different trade unions. In the United Kingdom they are GMB and Unison for British Gas and Unite and Prospect for Centrica Energy and Centrica Storage. In North America they are the Christian Labour Association of Canada, the United Association of Refrigeration Workers, the International Brotherhood of Electrical Workers and the Communications Energy and Paperworkers Union (the "CEP"). On 31 August, CEP merged with the Canadian Auto Workers Union to become Unifor, Canada's largest private sector union. In 2012, the main areas of trade union engagement centred on employee pay and redundancies. As of 30 June 2013, the Group has not experienced any material disruptions to its operations due to industrial action.

CAPITALISATION AND INDEBTEDNESS

The following table sets forth the Group's consolidated cash and cash equivalents, capitalisation and indebtedness as of 30 June 2013 without any adjustment.

You should read this table in conjunction with "Use of Proceeds", "Operating and Financial Review", "Description of the Notes" and the Group's Consolidated Financial Statements, the related notes and the other financial information included in this Offering Circular.

	As of 30 June 2013
	(£m) (unaudited)
Total cash and cash equivalents	**800**
Current borrowings[1]	674
Non-current borrowings	
Bank overdrafts and loans	328
Bonds[2]	4,146
Obligations under finance leases[3]	254
Non-current borrowings	**4,728**
Notes offered hereby	—
Total borrowings	**5,402**
Total equity	**5,864**
Total capitalisation and indebtedness[4]	**11,266**

Notes:

(1) Included in current borrowings is £30 million in bank overdrafts and loans, £317 million in bonds, £156 million in commercial paper, £30 million in obligations under finance leases and £141 million in interest accruals.

(2) During September 2013, bonds increased by £50 million as a result of a tap issue of an outstanding series of notes due 2044, by $80 million as a result of the issuance of floating rate notes and $50 million as a result of the issuance of fixed rate notes.

(3) Obligations under finance leases are principally in respect of property, plant and equipment relating to the Power generation and Gas production and storage categories.

(4) Total capitalisation and indebtedness includes total current borrowings, total non-current borrowings and total equity attributable to owners of the parent.

The Notes offered hereby will increase the Group's total borrowings by £849,056,604. Other than as disclosed herein, there has been no significant change in our capitalisation and indebtedness since 30 June 2013.

SELECTED HISTORICAL FINANCIAL INFORMATION

The following selected historical financial information of the Group is derived from, and should be read in conjunction with, the unaudited consolidated financial statements for the six months ended 30 June 3013 and the consolidated financial statements as of and for the years ended 31 December 2012, 2011 and 2010 and the accompanying notes thereto, all of which are included elsewhere in this Offering Circular.

This Offering Circular contains some measures which are not accounting measures within the scope of IFRS and which the Group uses to assess the financial performance of its businesses. These measures include adjusted operating profit, adjusted earnings, adjusted operating profit margin, EBITDA, net debt, working capital movements, margin calls, net capital expenditure, payments to shareholders, and foreign exchange and other. These non-IFRS measures have been included because the Directors believe that they are helpful to investors in assessing the historical financial performance of the Group. These are not measures of operating performance derived in accordance with IFRS, and should not be considered a substitute for gross profit, operating profit, profit/(loss) before tax, cash flow from operating activities or other income or cash flow statement data as determined in accordance with IFRS, or as a measure of profitability or liquidity. The Group's calculation of adjusted operating profit, adjusted earnings, adjusted operating profit margin, EBITDA, net debt, working capital movements, margin calls, net capital expenditure, payments to shareholders, and foreign exchange and other may be different from the calculation used by other companies and therefore comparability may be limited.

The selected financial and operating data set forth below should be read in conjunction with "Presentation of Financial and Other Information", "Operating and Financial Review", and the Consolidated Financial Statements and the accompanying notes thereto, each of which is included elsewhere in this Offering Circular. See "Presentation of Financial and Other Information" for the Group's definition of "Business performance", "Exceptional items", "Certain re-measurements", "Adjusted earnings", "EBITDA" and other non-IFRS financial measures.

Income Statement Data

The following table sets out the Group's financial performance for the six months ended 30 June 2013 and 2012 and the years ended 31 December 2012, 2011 and 2010:

	Six months ended 30 June						Year ended 31 December								
	2013			2012			2012			2011			2010		
	Business performance	Exceptional items and certain re-measure-ments	Statutory result	Business performance	Exceptional items and certain re-measure-ments	Statutory result	Business performance	Exceptional items and certain re-measure-ments	Statutory result	Business performance	Exceptional items and certain re-measure-ments	Statutory result	Business performance	Exceptional items and certain re-measure-ments	Statutory result
			(£m) (unaudited)								(£m)				
Group revenue	**13,651**	**—**	**13,651**	**11,977**	**—**	**11,977**	**23,942**	**—**	**23,942**	**22,824**	**—**	**22,824**	**22,423**	**—**	**22,423**
Cost of Sales	(10,886)	104	(10,782)	(9,445)	513	(8,932)	(18,676)	514	(18,162)	(17,959)	(658)	(18,617)	(17,595)	1,075	(16,520)
Gross profit	**2,765**	**104**	**2,869**	**2,532**	**513**	**3,045**	**5,266**	**514**	**5,780**	**4,865**	**(658)**	**4,207**	**4,828**	**1,075**	**5,903**
Operating costs	(1,332)	—	(1,332)	(1,244)	(90)	(1,334)	(2,844)	(445)	(3,289)	(2,750)	(110)	(2,860)	(2,641)	(181)	(2,822)
Share of profits/(losses) in joint ventures and associates, net of interest and taxation	52	1	53	58	(2)	56	140	(6)	134	93	(26)	67	7	(14)	(7)
Group operating profit	**1,485**	**105**	**1,590**	**1,346**	**421**	**1,767**	**2,562**	**63**	**2,625**	**2,208**	**(794)**	**1,414**	**2,194**	**880**	**3,074**
Net finance cost	(103)	—	(103)	(102)	—	(102)	(183)	—	(183)	(146)	—	(146)	(265)	—	(265)
Taxation	(649)	(19)	(668)	(521)	(168)	(689)	(1,029)	(140)	(1,169)	(810)	(16)	(826)	(708)	(221)	(929)
Profit from continuing operations after taxation	**733**	**86**	**819**	**723**	**253**	**976**	**1,350**	**(77)**	**1,273**	**1,252**	**(810)**	**442**	**1,221**	**659**	**1,880**
Discontinued operations	—	—	—	—	—	—	—	—	—	13	(34)	(21)	(5)	67	62
Profit for the period	**733**	**86**	**819**	**723**	**253**	**976**	**1,350**	**(77)**	**1,273**	**1,265**	**(844)**	**421**	**1,216**	**726**	**1,942**
Earnings attributable to non-controlling interests	—	—	—	—	—	—	—	—	—	—	—	—	(7)	—	—
Depreciation of fair value uplifts from Strategic Investments, after taxation	34			30			56			68			88		
Adjusted earnings	**767**			**753**			**1,406**			**1,333**			**1,297**		

Balance Sheet Data

The following table summarises the Group's financial position as of 30 June 2013 and as of 31 December 2012, 2011 and 2010:

	As of 30 June	As of 31 December		
	2013	2012	2011	2010
	(£m) (unaudited)		(£m)	
Total non-current assets	15,822	15,812	13,973	13,269
Total current assets	6,022	6,140	5,596	5,551
Total assets	**21,844**	**21,952**	**19,569**	**19,275**(1)
Total non-current liabilities	9,737	9,439	7,699	7,820
Total current liabilities	6,243	6,586	6,270	5,268
Total liabilities	**15,980**	**16,025**	**13,969**	**13,088**
Total equities	**5,864**	**5,927**	**5,600**	**5,819**

Note:

(1) Total assets for the year ended 31 December 2010 included £455 million of assets held for sale at that date.

Cash Flow Data

The following tables summarise the Group's cash flows and changes in net debt position for the six months ended 30 June 2013 and 2012 and for the years ended 31 December 2012, 2011 and 2010:

	Six months ended 30 June		Year ended 31 December		
	2013	2012	2012	2011	2010
	(£m) (unaudited)			(£m)	
Net cash inflow from operating activities	1,411	1,032	2,820	2,337	2,428
Net cash outflow from investing activities	(647)	(1,443)	(2,558)	(1,400)	(1,584)
Net cash (out)/inflow from financing activities	(897)	888	190	(907)	(1,677)
Net (decrease)/increase in cash and cash equivalents	(133)	477	452	30	(833)
Cash and cash equivalents	800	954	931	479	451

	Six months ended 30 June		Year ended 31 December		
	2013	2012	2012	2011	2010
			(£m) (unaudited)		
Opening net debt	**(4,047)**	**(3,292)**	**(3,292)**	**(3,195)**	**(3,055)**
EBITDA(1)	2,112	1,773	3,650	3,128	3,181
Working capital movements(2)	(112)	(333)	(51)	165	(251)
Margin calls(3)	(2)	132	114	(26)	466
Interest paid in cash in the period	(105)	(51)	(172)	(170)	(279)
Taxation paid in cash in the period	(401)	(283)	(524)	(692)	(540)
Net capital expenditure(4)	(755)	(1,525)	(2,727)	(1,601)	(1,669)
Payments to shareholders(5)	(810)	(571)	(815)	(762)	(668)
Foreign exchange and other(6)	(131)	(191)	(230)	(139)	(380)
Closing net debt(7)	**(4,251)**	**(4,341)**	**(4,047)**	**(3,292)**	**(3,195)**

Notes:

(1) EBITDA is defined as operating profit before exceptional items and certain re-measurements, and before amortisation, depreciation and impairments, and share of profits/(losses) in joint ventures and associates, net of taxation. See "Presentation of Financial and Other Information—Non-IFRS Financial Measures" for further detail on the use of EBITDA as a non-IFRS financial measure and a reconciliation thereof.

(2) The Group defines working capital movements as movements in inventories, receivables and payables during the period.

(3) The Group defines margin calls as cash payments made on a daily basis to counterparties to cover the mark-to-market positions on certain wholesale commodity contracts until the trade is fully executed.

(4) The Group defines net capital expenditure as gross cash purchases of PPE/Intangibles, plus net cash outflow relating to the acquisition of subsidiaries, and investment in joint ventures and associates less net proceeds received relating to the disposals of PPE/Intangibles and subsidiaries, and relating to the repayment of loans to, and disposal of investments in, joint ventures and associates.

(5) The Group defines payments to shareholders as dividends plus its share repurchase programme.

(6) Included in foreign exchange and other are (i) non-cash movements in net debt including foreign exchange and revaluation, (ii) other cash flows including dividends received from joint ventures and associates and payments relating to exceptionals, and (iii) non-cash items within operating profit that are not included within EBITDA.

(7) The Group defines net debt as current and non-current borrowings, less cash and cash equivalents, less current and non-current securities, less mark-to-market values on derivatives used to hedge offsetting movements in borrowings.

Operating Segment Data

The following tables set out the Group's revenue and adjusted operating profit by segment for the six months ended 30 June 2013 and 2012 and the years ended 31 December 2012, 2011 and 2010, and reconciles adjusted operating profit to operating profit. Adjusted operating profit is a non-IFRS accounting measure, and should not be considered as an alternative to statutory operating profit as an indicator of the Group's results of operations or as an alternative to cash flows from operations as an indicator of liquidity. The Group's definition of adjusted operating profit may not be comparable to adjusted operating profit as used by other companies. For the Group's definition of adjusted operating profit, see "Presentation of Financial and Other Information—Non-IFRS Financial Measures". For an explanation of the Group's segmental reporting that was implemented in 2013, see "Presentation of Financial and Other Information—General".

	Six months ended 30 June		Year ended 31 December		
	2013	2012	2012	2011	2010
	(£m) (unaudited)			(£m)	
Revenue					
International Downstream					
Residential energy supply	5,486	4,807	9,121	7,930	8,257
Residential services	737	755	1,543	1,563	1,486
Business energy supply and services	1,619	1,584	3,052	2,822	2,982
British Gas	**7,842**	**7,146**	**13,716**	**12,315**	**12,725**
Residential energy supply	1,308	1,210	2,357	2,416	2,502
Business energy supply	1,587	1,284	2,750	2,878	2,899
Residential and business services	274	253	532	520	485
Direct Energy	**3,169**	**2,747**	**5,639**	**5,814**	**5,886**
International Upstream					
Gas	2,037	1,539	3,461	3,122	2,074
Power	515	469	962	1,409	1,506
Centrica Energy	**2,552**	**2,008**	**4,423**	**4,531**	**3,580**
Centrica Storage	**88**	**76**	**164**	**164**	**232**
Total	**13,651**	**11,977**	**23,942**	**22,824**	**22,423**
Adjusted operating profit					
International Downstream					
Residential energy supply	356	345	606	544	761
Residential services	135	125	312	269	225
Business energy supply and services	78	93	175	192	230
British Gas	**569**	**563**	**1,093**	**1,005**	**1,216**
Residential energy supply	99	101	156	161	177
Business energy supply	53	43	121	98	35
Residential and business services	13	11	33	28	15
Direct Energy	**165**	**155**	**310**	**287**	**227**
International Upstream					
Gas(1)	683	519	940	794	573
Power(1)	119	174	311	254	205
Centrica Energy(1)	**802**	**693**	**1,251**	**1,048**	**778**
Centrica Storage	**47**	**36**	**89**	**75**	**169**
Adjusted operating profit—segment operating profit before exceptional items, certain re-measurements and impact of fair value uplifts from Strategic Investments(2)	**1,583**	**1,447**	**2,743**	**2,415**	**2,390**
Share of joint ventures/associates' interest and taxation	(47)	(49)	(85)	(102)	(78)
Depreciation of fair value uplifts to property, plant and equipment—Venture(1)	(27)	(37)	(67)	(64)	(60)
Depreciation of fair value uplifts to property, plant and equipment, net of taxation—associates—British Energy(1)	(24)	(15)	(29)	(41)	(58)
Operating profit—segment reporting profit before exceptional items and certain re-measurements	**1,485**	**1,346**	**2,562**	**2,208**	**2,194**

Notes:

(1) See "Presentation of Financial and Other Information" above, for an explanation of the depreciation on fair value uplifts to PP&E on acquiring Strategic Investments.

(2) Includes results of equity-accounted interests before interest and taxation.

Other key metrics

The following table sets out certain other key financial metrics of the Group for the six months ended 30 June 2013 and 2012 and the years ended 31 December 2012, 2011 and 2010:

	Six months ended 30 June		Year ended 31 December		
	2013	**2012**	**2012**	**2011**	**2010**
			(£m) (unaudited)		
EBITDA[1]	2,112	1,773	3,650	3,128	3,181
Net debt[2]	(4,251)	(4,341)	(4,047)	(3,292)	(3,195)
Net debt to EBITDA ratio[3]	2.01	2.45	1.11	1.05	1.00
Interest cover ratio[4]	18.2	24.0	17.4	16.2	10.9

Notes:

(1) EBITDA is defined as operating profit before exceptional items and certain re-measurements, and before amortisation, depreciation and impairments, and share of profits/(losses) in joint ventures and associates, net of taxation. See "Presentation of Financial and Other Information—Non-IFRS Financial Measures" above for further detail on the use of EBITDA as a non-IFRS financial measure and a reconciliation thereof.

(2) The Group defines net debt as current and non-current borrowings, less cash and cash equivalents, less current and non-current securities, less mark-to-market values on derivatives used to hedge offsetting movements in borrowings.

(3) Net debt to EBITDA ratio is calculated as Net debt divided by EBITDA.

(4) Interest cover ratio is calculated as EBITDA divided by Net financing interest paid.

OPERATING AND FINANCIAL REVIEW

The following review of the Group's financial condition and operating results should be read in conjunction with the "Presentation of Financial and Other Information", "Selected Historical Financial Information" and the Consolidated Financial Statements, including the accompanying notes, included elsewhere in this Offering Circular. Some of the information in the discussion and analysis set forth below and elsewhere in this Offering Circular includes forward-looking statements that involve risks and uncertainties. See "Forward-Looking Statements" and "Risk Factors" for a discussion of important factors that could cause actual results to differ materially from the results described in the forward-looking statements contained in this Offering Circular.

The historical financial information of the Group contained in this operating and financial review is derived from, and should be read in conjunction with, the unaudited consolidated financial statements for the six months ended 30 June 2013 and the consolidated financial statements as of and for the years ended 31 December 2012, 2011 and 2010 and the accompanying notes thereto, all of which are included elsewhere in this Offering Circular.

Overview

The Group is an integrated energy company that produces, sources and supplies gas and electricity for millions of residential and business customers in the United Kingdom and North America. The Group also provides a range of energy services solutions to its residential and business customers, including installation, maintenance, service and repair contracts, low-carbon and energy efficient products. Centrica was listed in 1997 on the London Stock Exchange following the demerger of the gas supply, service and retail businesses of British Gas plc together with its Morecambe gas field production activities. Since 1997, the Group has evolved significantly, shifting its primary focus from downstream activity in the initial years after listing towards becoming a leading integrated energy company in its chosen markets. The Group seeks to operate across the energy value chain from upstream production to downstream supply, although it focuses its operations on price-deregulated markets.

The Group's operations are broadly divided into three categories: International Downstream (British Gas in the United Kingdom and Direct Energy in North America), International Upstream (Centrica Energy) and Centrica Storage.

International Downstream operations involve the supply of energy to residences and businesses in the United Kingdom (excluding Northern Ireland) and North America and the provision of energy-related services to customers, including installation, maintenance, service and repair contracts, insurance and low carbon and energy efficient products. The Group's downstream operations principally operate under the British Gas and Direct Energy brands in the United Kingdom (excluding Northern Ireland) and North America, respectively. British Gas is the leading residential energy and services provider in Britain by number of customer accounts.

International Upstream operations comprise exploration, development, production and processing of natural gas and oil assets and power generation. They also include the transaction of major procurement contracts to source gas from around the world for the UK and North American markets, and energy trading activities. The Group's upstream assets located in the UK, Canada, Norway, the Netherlands and Trinidad and Tobago, and procurement contracts provide a stable supply of gas and power to its downstream operations, which in turn, provide a market for the Group's upstream production.

Centrica Storage sells capacity in its Rough gas storage facility, along with ancillary services to customers who typically inject gas in the summer and withdraw during the winter for the UK market.

Segmental analysis

The Group manages its business across four primary reporting segments: British Gas (International Downstream), Direct Energy (International Downstream), Centrica Energy (International Upstream) and Centrica Storage. British Gas comprises the Group's downstream operations in the United Kingdom, including its residential energy supply business, its residential services business and its business energy supply and services business. Direct Energy comprises the Group's downstream operations in North America, including its residential energy supply business, its business energy supply business (including the Group's North American Power and Midstream and Trading operations), and its residential and business services business. Centrica Energy comprises the Group's International Gas business and the Power business in the United Kingdom. Centrica Storage comprises the Group's gas storage business in the United Kingdom.

Changes to operating segments

On 27 February 2013, the Group changed its segmental reporting to reflect the Group's new organisational structure and to align with management reporting. The North American Upstream Gas business has been reallocated from the "Direct Energy—Upstream and wholesale energy" subsegment to the "Centrica Energy—Gas" subsegment and the North American Power and Midstream and Trading businesses have been reallocated from the "Direct Energy—Upstream and wholesale energy" subsegment to the "Direct Energy—Business energy supply" subsegment. This change was reflected in the unaudited interim financial statements as of and for the six months ended 30 June 2013, with the prior period comparatives restated accordingly. As a result, for the purposes of this Offering Circular segmental financial information has been updated to reflect this change in the Group's segments as of and for the years ended 31 December 2012, 2011 and 2010 for comparison purposes only. For an explanation of the Group's segmental reporting that was implemented in 2013, see "Presentation of Financial and Other Information—General".

Key factors affecting results of operations

Commodity prices

The Group's results of operations and financial condition depend on prevailing wholesale market prices of gas and power. Market prices for these commodities are subject to volatile trading patterns in the commodity futures markets. Market prices for gas and power impact the cost base of the downstream energy supply businesses and, to the extent that changes in wholesale commodity prices cannot be passed on to customers, any changes in market commodity prices may affect the results of operations and financial condition of the downstream energy supply businesses and, ultimately, the Group in future periods.

The upstream businesses of the Group may also be affected, with changes in wholesale market prices ultimately being reflected in the revenues of the gas and power businesses once any forward hedges are no longer in place. The interaction between commodity prices may also affect the Group's results of operations, as well as the Group's fleet of gas-fired power stations, whose profitability is affected by the differential between market gas and power prices and the Centrica Storage business, in which revenue is driven by the differential between summer and winter gas prices.

Energy consumption

Gas sales volumes and electricity sales volumes are impacted by a variety of short- and long-term factors which may impact the Group's results of operations. Short-term factors include weather, economic conditions and gas and electricity prices. Long-term factors include initiatives by governments and others to reduce the use of energy by consumers and the impact of new technologies being developed and applied in response to these factors (such as more energy efficient boilers, micro-combined heat and power units, smart metering and insulation). In recent years, the UK government in particular has focused on energy efficiency and carbon reduction policy. Adjusted for weather impacts, average residential gas and electricity consumption in the UK have fallen during the periods under review, reflecting these long-term factors.

Seasonality of operations

Certain activities of the Group are affected by weather and temperature conditions. Customer demand for gas in the United Kingdom and North America is driven primarily by heating load and is generally higher in the winter than in the summer, and higher from January to June than from July to December. Customer demand for electricity in the United Kingdom generally follows a similar pattern to gas, but the variation is less pronounced. Customer demand for electricity in North America is also more stable than gas but is driven by heating load in the winter and cooling load in the summer. Generally demand for electricity in North America is higher in the winter and summer than it is in the spring and autumn, and higher from July to December than it is from January to June.

Customer demand for home services in the United Kingdom is generally higher in the winter than it is in the summer, and higher in the earlier part of the winter reflecting a greater number of heating system break downs, so that customer demand from July to December is higher than from January to June. Customer demand for home services in North America is higher in the summer as a result of residential new construction in the United States and the servicing of cooling systems, e.g. air conditioners.

Gas production volumes in the United Kingdom are generally higher in the winter when gas prices are higher. Gas production volumes are generally higher from January to June than they are from July to December as outages are generally planned for the summer months when gas demand and prices are lower. Gas production volumes in North America are generally not seasonal. The Centrica Storage business is particularly seasonal, with customers typically injecting gas at the Rough Storage facility in the summer when prices are lower and withdrawing in the winter when prices tend to be more favourable.

Gas-fired power generation volumes are dependent on spark spread prices, which is the difference between the price of electricity and the price of gas multiplied by a conversion rate. As a result, they are not as seasonal as gas production volumes in the United Kingdom, as wholesale prices for both gas and electricity are generally higher in the winter than they are in the summer. Nuclear power generation volumes are generally not seasonal, but rather are dependent on both planned and unplanned outages. Likewise, wind power generation volumes are not seasonal and depend on wind availability. Power generation volumes in North America are generally higher in the summer than in the winter, reflecting higher demand for air conditioning. The impact of seasonality on customer demand and wholesale prices has a direct effect on the Group's financial performance and cash flows.

Asset performance

The Group's results of operations are also dependent on the performance of its physical gas and power assets. Any unplanned outages of gas and oil fields, gas-fired power stations, nuclear power stations, wind farms, or gas storage assets in which the Company has interests may adversely affect the Group's results of operations. The aggregate peak output of the Group's own sources of generation in Europe (including its share of the output from British Energy and the other long-term contractual arrangements in the United Kingdom) is equivalent to around 70 per cent. of British Gas residential and business peak electricity demand. The Group's own gas production in Europe is currently equivalent to over 50 per cent. of British Gas retail gas demand. Material changes in the output of these assets would have an impact on the performance of the Group's downstream operations.

Regulation

The energy markets in the United Kingdom, North America and Europe are regulated by a variety of regulatory bodies. The Group is subject to comprehensive operating requirements, supply and wholesale industry procedures, as well as regulated charges for the transportation and distribution of energy. Any material changes to the requirements or regulations or increases in charges could have an impact on the Group's results of operations, in some circumstances, materially so.

In the United Kingdom, the Government's EMR programme will potentially affect the Group's power generation business while Ofgem's RMR may affect the downstream energy supply businesses. The Group has already implemented a number of the changes proposed under RMR and it continues to review and assess the implications of EMR for new power generation projects. As part of the UK government's focus on energy efficiency and low carbon solutions, the Group was also obliged to participate in CERT and CESP. In January 2013, CERT and CESP were replaced by ECO. ECO places legal obligations on the United Kingdom's principal energy suppliers to deliver energy efficiency measures to domestic energy users and requires energy suppliers to improve the insulation of harder to treat properties in the domestic sector and invest resources in reducing heating costs for vulnerable households. For the six months ended 30 June 2013, the Group recognised a £300 million charge relating to ECO, which is in line with its expected total required expenditure of £1.4 billion until the end of the programme in March 2015

Economic conditions

Certain of the Group's activities are affected by the prevailing economic conditions in its markets. In particular, weak economic conditions may impact the Group's ability to sell more discretionary products, such as energy services contracts or new equipment. It may also increase the risk of bad debt for energy customers, in particular, business customers. Economic conditions may affect the demand for gas, oil and electricity, which may in turn affect the market prices for these commodities and therefore the profitability of the upstream gas and power businesses.

Applicable tax rates

The Group's results of operations are impacted by the relative contributions of its business segments to its profit before taxes. Profits from extraction activities in the United Kingdom, including the Group's oil and gas exploration activities, are subject to a corporation tax "ring fence", which means that profits from these activities cannot be reduced by any losses or other tax relief from other business activities. Profits within the corporation tax "ring fence" are subject to a supplementary corporation tax charge of 32 per cent. (revised upwards from 20 per cent. in March 2011), in addition to the usual 30 per cent. rate. In addition to corporation tax, profits on certain fields in the United Kingdom are subject to petroleum revenue tax ("PRT"). PRT is currently charged at a rate of 50 per cent. on profits from oil and gas extraction, but is deductible in calculating profits for corporation tax purposes. As a result, profits from gas production and development are generally taxed at applicable tax rates between 62 per cent. for non-PRT paying fields and 81 per cent. for PRT paying fields. This compares to the profits of the Group's other business segments in the United Kingdom that are currently taxed at the standard tax rate for UK corporations of 23 per cent. (which has declined from 28 per cent. in 2010). Norwegian upstream profits are taxed at the standard rate of 28 per cent. plus a special tax of 50 per cent., resulting in an aggregate tax rate of 78 per cent. Taxation for other jurisdictions is calculated at the rates prevailing in those respective jurisdictions.

Exchange rates

The Group is exposed to exchange rate risk through foreign currency denominated transactions (transaction currency risk) and through its net investments in foreign operations (translational currency risk). The Group's primary functional currencies are pounds sterling in the United Kingdom, Canadian dollars in Canada, US dollars in the United States, the Norwegian krone in Norway and euros in Europe.

Transactional currency risk arises if the functional currency value of cash flows varies as a result of exchange rate movement. The Group hedges all material transactional exposure using forward contracts to fix the functional currency value of non-functional currency cash flows.

The Group's translational currency risk is that the pounds sterling value of the net assets of foreign operations will decrease with changes in foreign exchange rates or that its reported pounds sterling results will fluctuate as a result of changes in currency exchange rates. Where possible, the Group protects against the risk that the pounds sterling value of the net assets of foreign operations will decrease with changes in foreign exchange rates by holding foreign currency debt, using foreign currency derivatives or a combination of both. See "—Qualitative and quantitative disclosures about financial risk management".

Market dynamics

In the UK downstream energy supply market, the Group principally competes with the other Big Six suppliers. These suppliers are all broadly exposed to the same input costs and competitive positioning is based on brand recognition, the range of product propositions offered, the quality of service delivered to customers and the retail price. There is a certain level of churn in residential customers that is common among the Group and its principal competitors. However, levels of departing customers have historically been broadly replaced by new customers and the impact on the Group's results as a consequence of this churn has been limited. The same dynamics apply to business customers and business customer turnover has been higher over the period under review in part due to competitive pressures.

The North American markets in which the Group operates are generally less mature than the UK market as they have been price deregulated more recently. Consequently, the Group experiences competitive pressure from market incumbents and there is a greater level of churn as compared to the UK market. In order to strengthen its position in these markets and as part of its overall strategy in North America, the Group has entered into and intends to continue to evaluate and enter into acquisitions which would improve its scale and competitive position in these markets.

Description of key line items

The Group's revenue is derived from the business activities of its principal segments including the supply of gas, electricity and energy services to residential and business customers in the UK and North America, exploration, development, production and processing of natural gas and oil and power generation and the Group's storage business. Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be measured reliably. Revenue includes amounts receivable for goods and services provided in the normal course of business, net of discounts, rebates, VAT and other sales-related taxes.

Cost of sales in the downstream businesses are principally comprised of gas and power costs, transportation, distribution and metering costs and environmental costs such as the cost of meeting Renewables Obligations and ECO. Cost of sales in the upstream and storage businesses are principally comprised of costs related to the operation of gas and power assets, including depreciation.

Operating costs are principally comprised of employee costs, including wages, salaries and social security costs, depreciation, amortisation and write-downs, impairment of trade receivables and other costs associated with the downstream and upstream businesses, which include marketing costs and irrecoverable VAT.

Results of operations

Overview

The Group reflects its underlying financial results in the "business performance" column of its Income Statement. Unless otherwise stated, the discussion below reflects "business performance" measures, stated prior to exceptional items and certain re-measurements.

The Group's results of operations also include a discussion of adjusted operating profit. Adjusted operating profit is a non-IFRS accounting measure, and should not be considered as an alternative to statutory operating profit as an indicator of the Group's results of operations or as an alternative to cash flows from operations as an indicator of liquidity. The Group's definition of adjusted operating profit may not be comparable to adjusted operating profit as used by other companies. For the Group's definition of adjusted operating profit, see "Presentation of Financial and Other Information—Non-IFRS Financial Measures".

Six months ended 30 June 2013 compared to six months ended 30 June 2012

The following table sets out the Group's financial performance for the six months ended 30 June 2013 and 2012 and reconciles profit from business performance to statutory results. For further detail on certain of the measures described below, please see "Presentation of Financial and Other Information".

	Six months ended 30 June					
	2013			2012		
	Business performance	Exceptional items and certain re-measurements	Statutory result	Business performance	Exceptional items and certain re-measurements	Statutory result
	(£m) (unaudited)					
Group revenue	**13,651**	**—**	**13,651**	**11,977**	**—**	**11,977**
Cost of sales	(10,886)	104	(10,782)	(9,445)	513	(8,932)
Gross profit	**2,765**	**104**	**2,869**	**2,532**	**513**	**3,045**
Operating costs	(1,332)	—	(1,332)	(1,244)	(90)	(1,334)
Share of profits/(losses) in joint ventures and associates, net of interest and taxation	52	1	53	58	(2)	56
Group operating profit	**1,485**	**105**	**1,590**	**1,346**	**421**	**1,767**
Net finance cost	(103)	—	(103)	(102)	—	(102)
Taxation	(649)	(19)	(668)	(521)	(168)	(689)
Profit from continuing operations after taxation	**733**	**86**	**819**	**723**	**253**	**976**
Discontinued operations	—	—	—	—	—	—
Profit for the period	**733**	**86**	**819**	**723**	**253**	**976**
Earnings attributable to non-controlling interests	—	—	—	—	—	—
Depreciation of fair value uplifts from Strategic Investments, after taxation	34			30		
Adjusted earnings	**767**			**753**		

Group revenue

Group revenue increased by 14.0 per cent. during the six months ended 30 June 2013 to £13,651 million (2012: £11,977 million). The increase reflected increases in revenue across all primary segments.

The following table sets out the Group's revenue by segment for the six months ended 30 June 2013 and 2012.

	Six months ended 30 June	
	2013	**2012**
	(£m)	**(unaudited)**
International Downstream		
Residential energy supply	5,486	4,807
Residential services	737	755
Business energy supply and services	1,619	1,584
British Gas	**7,842**	**7,146**
Residential energy supply	1,308	1,210
Business energy supply	1,587	1,284
Residential and business services	274	253
Direct Energy	**3,169**	**2,747**
International Upstream		
Gas	2,037	1,539
Power	515	469
Centrica Energy	**2,552**	**2,008**
Centrica Storage	**88**	**76**
	13,651	**11,977**

Revenue from British Gas increased by 9.7 per cent. during the six months ended 30 June 2013 to £7,842 million (2012: £7,146 million). British Gas residential energy supply revenue increased by 14.1 per cent., primarily due to a 13 per cent. increase in average gas consumption as a result of sustained cold weather during the period and the impact of a 6 per cent. increase in retail gas and electricity prices implemented in November 2012. British Gas business energy supply and services revenue increased by 2.2 per cent. and British Gas residential services revenue decreased by 2.4 per cent.

Revenue from Direct Energy increased by 15.4 per cent. during the six months ended 30 June 2013 to £3,169 million (2012: £2,747 million), primarily due to higher average residential energy and residential and business services customer numbers during the period resulting predominantly from acquisitions, increased business gas and power consumption resulting from a higher number of customers and higher gas and power retail prices.

Revenue from Centrica Energy increased by 27.1 per cent. during the six months ended 30 June 2013 to £2,552 million (2012: £2,008 million), primarily due to gas production volumes increasing by 19 per cent. and liquids production volumes increasing by 31 per cent. given the full period impact of the North Sea asset purchases completed in 2012, and a 19 per cent. increase in the achieved price for gas and a 5 per cent. increase in the achieved price for liquids.

Revenue from Centrica Storage increased by 15.8 per cent. during the six months ended 30 June 2013 to £88 million (2012: £76 million), primarily due to higher seasonal gas spreads being reflected in the 2012/13 Standard Bundled Unit ("SBU") price for the first four months of the year and strong optimisation performance.

Cost of sales before exceptional items and certain re-measurements[(1)]

Cost of sales before exceptional items and certain re-measurements increased by 15.3 per cent. during the six months ended 30 June 2013 to £10,886 million (2012: £9,445 million). The increase was driven primarily

(1) Where there is a specific link to revenue generation, the Group has reclassified sales commissions paid to brokers or agents (or similar arrangements) and prepayment customer vending fees, from operating costs to cost of sales. The effect has been to reduce operating costs and increase cost of sales by £87 million for the six months ended 30 June 2013 and by £82 million for the six months ended 30 June 2012. No such reclassifications have been made for the years ended 31 December 2012, 2011 and 2010.

by increased commodity costs in British Gas and Direct Energy reflecting both higher wholesale gas and power prices and higher consumption, and additional upstream costs given the full period impact of the North Sea asset purchases completed in 2012.

Operating costs before exceptional items and certain re-measurements

Operating costs before exceptional items and certain re-measurements increased by 7.1 per cent. during the six months ended 30 June 2013 at £1,332 million (2012: £1,244 million). The increase was driven primarily by the impact of 2012 acquisitions in the North Sea and in North America and cost inflation.

Share of profits in joint ventures and associates, net of interest and taxation

Share of profits in joint ventures and associates, net of interest and taxation, decreased by 10.3 per cent. during the six months ended 30 June 2013 to £52 million (2012: £58 million).

Group adjusted operating profit

Group adjusted operating profit increased by 9.4 per cent. during the six months ended 30 June 2013, to £1,583 million (2012: £1,447 million) as a result of increased profitability across each of the Group's operations.

The following table sets out the Group's adjusted operating profit by segment for the six months ended 30 June 2013 and 2012 and reconciles adjusted operating profit to operating profit. For additional information about adjusted operating profit, see "—Results of operations—Overview" above.

	Six months ended 30 June	
	2013	**2012**
	(£m)	**(unaudited)**
International Downstream		
Residential energy supply	356	345
Residential services	135	125
Business energy supply and services	78	93
British Gas	**569**	**563**
Residential energy supply	99	101
Business energy supply	53	43
Residential and business services	13	11
Direct Energy	**165**	**155**
International Upstream		
Gas(1)	683	519
Power(1)(2)	119	174
Centrica Energy	**802**	**693**
Centrica Storage	**47**	**36**
Adjusted operating profit—segment operating profit before exceptional items, certain re-measurements and impact of fair value uplifts from Strategic Investments(2)	**1,583**	**1,447**
Share of joint ventures/associates' interest and taxation	(47)	(49)
Depreciation of fair value uplifts to property, plant and equipment—Venture(1)	(27)	(37)
Depreciation of fair value uplifts to property, plant and equipment, net of taxation—associates—British Energy(1)	(24)	(15)
Operating profit—segment reporting profit before exceptional items and certain re-measurements	**1,485**	**1,346**

Notes:

(1) See "Presentation of Financial and Other Information—Non-IFRS Financial Measures", for an explanation of the depreciation on fair value uplifts to PP&E on acquiring Strategic Investments.

(2) Includes results of equity-accounted interests before interest and taxation.

Adjusted operating profit from British Gas increased by 1.1 per cent. during the six months ended 30 June 2013 to £569 million (2012: £563 million). British Gas residential energy supply profit increased by 3.2 per cent. with higher revenue being mostly offset by higher wholesale commodity, transportation and environmental costs and adjusted operating profit margin was 6.5 per cent. (2012: 7.2 per cent.). British Gas business energy supply and services profit decreased by 16.1 per cent. reflecting the challenging economic and competitive environment, which put pressure on contract renewal rates and on margins. Consequently, adjusted operating profit margin was reduced to 4.8 per cent. (2012: 5.9 per cent.). British Gas residential services profit increased by 8.0 per cent. primarily reflecting cost efficiency measures and adjusted operating profit margin was 18.3 per cent. (2012: 16.6 per cent.).

Adjusted operating profit from Direct Energy increased by 6.5 per cent. during the six months ended 30 June 2013 to £165 million (2012: £155 million), primarily due to revenue growth, mostly offset by increased commodity costs as a result of higher wholesale gas and electricity prices and higher costs as a result of the increased scale of the business. Adjusted operating profit margin at Direct Energy was 5.2 per cent. (2012: 5.6 per cent.).

Adjusted operating profit from Centrica Energy increased by 15.7 per cent. during the six months ended 30 June 2013 to £802 million (2012: £693 million), primarily due to higher gas and liquids production and achieved prices, which more than offset increased unit costs in the gas segment. Profits decreased in the power segment as a result of the loss of free carbon emissions allowances and lower CCGT volumes reflecting low market spark spreads.

Adjusted operating profit from Centrica Storage increased by 30.6 per cent. during the six months ended 30 June 2013 to £47 million (2012: £36 million), primarily due to a higher 2012/13 SBU price for the first four months of the year.

Net finance cost

Net finance cost remained broadly flat during the six months ended 30 June 2013 at £103 million (2012: £102 million).

Taxation before exceptional items and certain re-measurements

Taxation charges before exceptional items and certain re-measurements increased by 24.6 per cent. during the six months ended 30 June 2013 at £649 million (2012: £521 million) principally due to the higher level of operating profit and an increased proportion of upstream gas operating profit, which is more heavily taxed. The effective tax rate on profits from business performance for the six months ended 30 June 2013 was 47 per cent. (2012: 42 per cent.).

Profit for the period

Statutory profit for the period was £819 million (2012: £976 million). The reconciling items between profit from business performance and statutory profit are certain re-measurements and, in 2012, an exceptional item as described below.

Exceptional items

No exceptional charges were incurred during the six months ended 30 June 2013. In the first half of 2012, a pre-tax £90 million exceptional restructuring charge was recorded (post-tax £66 million), relating to staff reductions following the announcement of a Group-wide cost reduction programme.

Certain re-measurements

For the six months ended 30 June 2013, net gains of £86 million (pre-tax £105 million) relate to certain re-measurements. In 2012, a net gain of £319 million (pre-tax £511 million) was recorded.

Year ended 31 December 2012 compared to year ended 31 December 2011

The following table sets out the Group's financial performance for the years ended 31 December 2012 and 2011 and reconciles profit from business performance to statutory results. For further detail on certain of the measures described below, please see "Presentation of Financial and Other Information".

	Year ended 31 December					
	2012			2011		
	Business performance	Exceptional items and certain re-measurements	Statutory result	Business performance	Exceptional items and certain re-measurements	Statutory result
	(£m)					
Group revenue	**23,942**	**—**	**23,942**	**22,824**	**—**	**22,824**
Cost of sales	(18,676)	514	(18,162)	(17,959)	(658)	(18,617)
Gross profit	**5,266**	**514**	**5,780**	**4,865**	**(658)**	**4,207**
Operating costs	(2,844)	(445)	(3,289)	(2,750)	(110)	(2,860)
Share of profits/(losses) in joint ventures and associates, net of interest and taxation	140	(6)	134	93	(26)	67
Group operating profit	**2,562**	**63**	**2,625**	**2,208**	**(794)**	**1,414**
Net finance cost	(183)	—	(183)	(146)	—	(146)
Taxation	(1,029)	(140)	(1,169)	(810)	(16)	(826)
Profit from continuing operations after taxation	**1,350**	**(77)**	**1,273**	**1,252**	**(810)**	**442**
Discontinued operations	—	—	—	13	(34)	(21)
Profit for the period	**1,350**	**(77)**	**1,273**	**1,265**	**(844)**	**421**
Earnings attributable to non-controlling interests	—	—	—	—	—	—
Depreciation of fair value uplifts from Strategic Investments, after taxation	56			68		
Adjusted earnings	**1,406**			**1,333**		

Group revenue

Group revenue increased by 4.9 per cent. during 2012, to £23,942 million (2011: £22,824 million). The increase was driven primarily by increased revenue in British Gas, which more than offset decreases in revenue in Direct Energy and Centrica Energy.

The following table sets out the Group's revenue by segment for the years ended 31 December 2012 and 2011.

	Year ended 31 December 2012	2011
	(£m)	
International Downstream		
Residential energy supply	9,121	7,930
Residential services	1,543	1,563
Business energy supply and services	3,052	2,822
British Gas	**13,716**	**12,315**
Residential energy supply	2,357	2,416
Business energy supply	2,750	2,878
Residential and business services	532	520
Direct Energy	**5,639**	**5,814**
International Upstream		
Gas	3,461	3,122
Power	962	1,409
Centrica Energy	**4,423**	**4,531**
Centrica Storage	**164**	**164**
	23,942	**22,824**

Revenue from British Gas increased by 11.4 per cent. for the year ended 31 December 2012 to £13,716 million (2011: £12,315 million). British Gas residential energy supply revenue increased by 15.0 per cent. primarily due to a 12 per cent. increase in average gas consumption as a result of colder than normal weather in 2012 compared to warmer than normal weather in 2011 and the impact of an 18 per cent. increase in retail gas prices and a 16 per cent. increase in retail electricity prices implemented in August 2011. British Gas business energy supply and services revenue increased by 8.2 per cent., with higher average tariffs in response to higher wholesale commodity costs, and British Gas residential services revenue decreased by 1.3 per cent.

Revenue from Direct Energy decreased by 3.0 per cent. for the year ended 31 December 2012 to £5,639 million (2011: £5,814 million), with higher average residential energy and residential and business services customer numbers during the year and increased business energy consumption being more than offset by the impact on retail tariffs of lower wholesale energy prices.

Revenue from Centrica Energy decreased by 2.4 per cent. for the year ended 31 December 2012 to £4,423 million (2011: £4,531 million), primarily due to the impact of lower gas-fired power generation volumes, which decreased by 40 per cent., and reduced midstream activity following the closure of the Group's German wholesale business in 2011. These more than offset the impact of higher gas volumes, which increased by 10 per cent., and higher liquids volumes, which increased by 32 per cent.

Revenue from Centrica Storage remained flat for the year ended 31 December 2012 at £164 million (2011: £164 million).

Cost of sales before exceptional items and certain re-measurements

Cost of sales before exceptional items and certain re-measurements increased by 4.0 per cent. for the year ended 31 December 2012 to £18,676 million (2011: £17,959 million), primarily due to increased commodity costs in British Gas reflecting higher UK wholesale gas and power prices and higher consumption, partially offset by the impact of lower North American commodity prices in Direct Energy and reduced Centrica Energy midstream activity.

Operating costs before exceptional items and certain re-measurements

Operating costs before exceptional items and certain re-measurements increased by 3.4 per cent. for the year ended 31 December 2012 to £2,844 million (2011: £2,750 million). The increase was driven primarily by the impact of North American acquisitions and cost inflation.

Share of profits in joint ventures and associates, net of interest and taxation

Share of profits in joint ventures and associates, net of interest and taxation, increased by 50.5 per cent. for the year ended 31 December 2012 to £140 million (2011: £93 million), primarily due to an 8 per cent. increase in nuclear power generation output and an increase in the achieved nuclear sales price.

Group adjusted operating profit

Group adjusted operating profit increased by 13.6 per cent. during 2012, to £2,743 million (2011: £2,415 million) as a result of increased profitability across the Group's operations.

The following table sets out the Group's adjusted operating profit by segment for the years ended 31 December 2012 and 2011 and reconciles adjusted operating profit to operating profit. For additional information on adjusted operating profit, see "—Results of operations—Overview" above.

	Year ended 31 December	
	2012	2011
	(£m)	
International Downstream		
Residential energy supply	606	544
Residential services	312	269
Business energy supply and services	175	192
British Gas	**1,093**	**1,005**
Residential energy supply	156	161
Business energy supply	121	98
Residential and business services	33	28
Direct Energy	**310**	**287**
International Upstream		
Gas[1]	940	794
Power[1][2]	311	254
Centrica Energy	**1,251**	**1,048**
Centrica Storage	**89**	**75**
Adjusted operating profit—segment operating profit before exceptional items, certain re-measurements and impact of fair value uplifts from Strategic Investments[2]	**2,743**	**2,415**
Share of joint ventures/associates' interest and taxation	(85)	(102)
Depreciation of fair value uplifts to property, plant and equipment—Venture[1]	(67)	(64)
Depreciation of fair value uplifts to property, plant and equipment, net of taxation—associates—British Energy[1]	(29)	(41)
Operating profit—segment reporting profit before exceptional items and certain re-measurements	**2,562**	**2,208**

Notes:

(1) See "Presentation of Financial and Other Information—Non-IFRS Financial Measures" for an explanation of the depreciation on fair value uplifts to PP&E on acquiring Strategic Investments.

(2) Includes results of equity-accounted interests before interest and taxation.

Adjusted operating profit from British Gas increased by 8.8 per cent. for the year ended 31 December 2012 to £1,093 million (2011: £1,005 million). British Gas residential energy supply profit increased by 11.4 per cent., primarily due to the impact of higher gas consumption and gas and electricity unit prices, which more than offset increased wholesale commodity, transportation and environmental costs, and adjusted operating profit margin was 6.6 per cent. (2011: 6.9 per cent.). British Gas business energy supply and services profit decreased by 8.9 per cent., reflecting the challenging economic and competitive environment, which put pressure on contract renewal rates and on margins. As a consequence, adjusted operating profit margin was reduced to 5.7 per cent. (2011: 6.8 per cent.). British Gas residential services profit increased by 16.0 per cent, due to cost efficiency measures and higher sales of energy efficiency measures such as insulation, and adjusted operating profit margin was 20.2 per cent. (2011: 17.2 per cent.).

Adjusted operating profit from Direct Energy increased by 8.0 per cent. for the year ended 31 December 2012 to £310 million (2011: £287 million), primarily due to an 11 per cent. increase in both gas and electricity sales volumes in business energy supply. Adjusted operating profit margin at Direct Energy was 5.5 per cent. (2011: 4.9 per cent.).

Adjusted operating profit from Centrica Energy increased by 19.4 per cent. for the year ended 31 December 2012 to £1,251 million (2011: £1,048 million), primarily due to higher gas and liquids production and achieved prices in the gas segment and higher nuclear power generation more than offsetting the impact of reduced gas-fired power generation volumes in the power segment.

Adjusted operating profit from Centrica Storage increased by 18.7 per cent. for the year ended 31 December 2012 to £89 million (2011: £75 million), primarily due to improved seasonal price differentials during the first quarter of the year and the subsequent positive impact on gross revenue and additional profit arising from improved optimisation performance.

Net finance cost

Net finance cost increased 25.3 per cent. during the year ended 31 December 2012 to £183 million (2011: £146 million), reflecting £1.2 billion of net debt issuances during the year.

Taxation before exceptional items and certain re-measurements

Taxation charges before exceptional items and certain re-measurements increased 27.0 per cent. during the year ended 31 December 2012 to £1,029 million (2011: £810 million), primarily due to higher levels of operating profit and an increased proportion of upstream gas operating profit, which is more heavily taxed. The effective tax rate on profits from business performance for the year ended 31 December 2012 was 43 per cent. (2011: 39 per cent.).

Profit for the year

Statutory profit for the year was £1,273 million (2011: £421 million). The reconciling items between profit from business performance and statutory profit comprise certain re-measurements and the exceptional items described below, as well as a £21 million loss from discontinued operations in 2011.

Exceptional items

The Group recorded a pre-tax exceptional charge of £534 million (post-tax £441 million) for the year ended 31 December 2012. The exceptional charge consisted of the following elements:

- an impairment charge of £231 million upon taking the decision not to proceed with nuclear new build investment;
- a restructuring charge of £214 million principally relating to staff reductions following the announcement of a Group-wide cost reduction programme; and
- an onerous contract charge of £89 million related to certain North American wind farm power purchase agreements following a decrease in power prices.

A tax charge of £40 million was also recognised upon the UK government substantively enacting the restriction on the rate of tax relief on oil and gas decommissioning costs. Net post-tax exceptional items for 2012 was £481 million.

Certain re-measurements

For the year ended 31 December 2012, net gains of £404 million (pre-tax £597 million) relate to certain re-measurements. In 2011, a net charge of £344 million (pre-tax £463 million) from continuing operations was recorded.

Year ended 31 December 2011 compared to year ended 31 December 2010

The following table sets out the Group's financial performance for the years ended 31 December 2011 and 2010 and reconciles profit from business performance to statutory results. For further detail on certain of the measures described below, please see "Presentation of Financial and Other Information".

	Year ended 31 December					
	2011			2010		
	Business performance	Exceptional items and certain re-measurements	Statutory result	Business performance	Exceptional items and certain re-measurements	Statutory result
	(£m)					
Group revenue	**22,824**	**—**	**22,824**	**22,423**	**—**	**22,423**
Cost of sales	(17,959)	(658)	(18,617)	(17,595)	1,075	(16,520)
Gross profit	**4,865**	**(658)**	**4,207**	**4,828**	**1,075**	**5,903**
Operating costs	(2,750)	(110)	(2,860)	(2,641)	(181)	(2,822)
Share of profits/(losses) in joint ventures and associates, net of interest and taxation	93	(26)	67	7	(14)	(7)
Group operating profit	**2,208**	**(794)**	**1,414**	**2,194**	**880**	**3,074**
Net finance cost	(146)	—	(146)	(265)	—	(265)
Taxation	(810)	(16)	(826)	(708)	(221)	(929)
Profit from continuing operations after taxation	**1,252**	**(810)**	**442**	**1,221**	**659**	**1,880**
Discontinued operations	13	(34)	(21)	(5)	67	62
Profit for the period	**1,265**	**(844)**	**421**	**1,216**	**726**	**1,942**
Earnings attributable to non-controlling interests	—	—	—	(7)	—	—
Depreciation of fair value uplifts from Strategic Investments, after taxation	68			88		
Adjusted earnings	**1,333**			**1,297**		

Group revenue

Group revenue increased by 1.8 per cent. during 2011 to £22,824 million (2010: £22,423 million). The increase was driven primarily by an increase in revenue in Centrica Energy, partially offset by a decrease in revenue in British Gas.

The following table sets out the Group's revenue by segment for the years ended 31 December 2011 and 2010.

	Year ended 31 December	
	2011	2010
	(£m)	
International Downstream		
Residential energy supply	7,930	8,257
Residential services	1,563	1,486
Business energy supply and services	2,822	2,982
British Gas	**12,315**	**12,725**
Residential energy supply	2,416	2,502
Business energy supply	2,878	2,899
Residential and business services	520	485
Direct Energy	**5,814**	**5,886**
International Upstream		
Gas	3,122	2,074
Power	1,409	1,506
Centrica Energy	**4,531**	**3,580**
Centrica Storage	**164**	**232**
	22,824	**22,423**

Revenue from British Gas decreased by 3.2 per cent. for the year ended 31 December 2011 to £12,315 million (2010: £12,725 million). British Gas residential energy supply revenue decreased by 4.0 per cent., primarily due to a 21 per cent. reduction in average gas consumption, reflecting warmer than normal weather in 2011 compared to much colder than normal weather in 2010, more than offsetting the impact of an 18 per cent. increase in retail gas prices and a 16 per cent. increase in retail electricity prices implemented in August 2011 and a 7 per cent. increase in retail gas and electricity prices implemented in December 2010, both in response to rising wholesale gas and power prices. British Gas business energy supply and services revenue decreased by 5.4 per cent., primarily as a result of average gas consumption decreasing by 17 per cent. due to the warmer weather conditions, partially offset by higher tariffs resulting from higher wholesale commodity prices. British Gas residential services revenue increased by 5.2 per cent.

Revenue from Direct Energy decreased by 1.2 per cent. for the year ended 31 December 2011 to £5,814 million (2010: £5,886 million), primarily due to the impact of lower wholesale commodity prices on tariffs more than offsetting the impact of higher average customer numbers and business energy consumption.

Revenue from Centrica Energy increased by 26.6 per cent. for the year ended 31 December 2011 to £4,531 million (2010: £3,580 million), primarily due to higher wholesale gas prices being reflected in the price achieved.

Revenue from Centrica Storage decreased by 29.3 per cent. for the year ended 31 December 2011 to £164 million (2010: £232 million), reflecting a narrowing of seasonal gas price differentials.

Cost of sales before exceptional items and certain re-measurements

Cost of sales before exceptional items and certain re-measurements increased by 2.1 per cent. for the year ended 31 December 2011 to £17,959 million (2010: £17,595 million). The increase was driven primarily by higher unit commodity costs in the United Kingdom, which was partially offset by reduced consumption.

Operating costs before exceptional items and certain re-measurements

Operating costs before exceptional items and certain re-measurements increased by 4.1 per cent. for the year ended 31 December 2011 at £2,750 million (2010: £2,641 million), primarily as a result of the impact of acquisitions and cost inflation.

Share of profits in joint ventures and associates, net of interest and taxation

Share of profits in joint ventures and associates, net of interest and taxation, increased to £93 million for the year ended 31 December 2011 (2010: £7 million), primarily due to improved performance from the Group's share of nuclear power generation assets.

Group adjusted operating profit

Group adjusted operating profit increased by 1.0 per cent. during 2011, to £2,415 million (2010: £2,390 million) as a result of increased profitability in Centrica Energy and Direct Energy, which was mostly offset by lower British Gas and Centrica Storage profitability.

The following table sets out the Group's adjusted operating profit by segment for the years ended 31 December 2011 and 2010 and reconciles adjusted operating profit to operating profit. For additional information on adjusted operating profit, see "—Results of operations—Overview" above.

	Year ended 31 December	
	2011	**2010**
	(£m)	
International Downstream		
Residential energy supply	544	761
Residential services	269	225
Business energy supply and services	192	230
British Gas	**1,005**	**1,216**
Residential energy supply	161	177
Business energy supply	98	35
Residential and business services	28	15
Direct Energy	**287**	**227**
International Upstream		
Gas(1)	794	573
Power(1)(2)	254	205
Centrica Energy	**1,048**	**778**
Centrica Storage	**75**	**169**
Adjusted operating profit—segment operating profit before exceptional items, certain re-measurements and impact of fair value uplifts from Strategic Investments(2)	**2,415**	**2,390**
Share of joint ventures/associates' interest and taxation	(102)	(78)
Depreciation of fair value uplifts to property, plant and equipment—Venture(1)	(64)	(60)
Depreciation of fair value uplifts to property, plant and equipment, net of taxation—associates—British Energy(1)	(41)	(58)
Operating profit—segment reporting profit before exceptional items and certain re-measurements	**2,208**	**2,194**

Notes:

(1) See "Presentation of Financial and Other Information—Non-IFRS Financial Measures" for an explanation of the depreciation on fair value uplifts to PP&E on acquiring Strategic Investments.

(2) Includes results of equity-accounted interests before interest and taxation.

Adjusted operating profit from British Gas decreased by 17.4 per cent. for the year ended 31 December 2011 to £1,005 million (2010: £1,216 million). British Gas residential energy supply profit decreased by 28.5 per cent., primarily due to the impact of lower gas consumption, increased unit wholesale commodity costs and increased transportation and environmental costs, and adjusted operating profit margin was 6.9 per cent. (2010: 9.2 per cent.). British Gas business energy supply and services profit decreased by 16.5 per cent., due to the impact of lower gas consumption and challenging economic and competitive conditions, and adjusted operating margin was 6.8 per cent. (2010: 7.7 per cent.). British Gas residential services profit increased by 19.6 per cent., due to cost efficiency measures and higher sales of energy efficiency measures such as insulation, and adjusted operating profit margin was 17.2 per cent. (2010: 15.1 per cent).

Adjusted operating profit from Direct Energy increased by 26.4 per cent. for the year ended 31 December 2011 to £287 million (2010: £227 million), primarily due to improved performance leading to improved margins in the business energy supply division. Adjusted operating profit margin at Direct Energy was 4.9 per cent. (2010: 3.9 per cent.).

Adjusted operating profit from Centrica Energy increased by 34.7 per cent. for the year ended 31 December 2011 to £1,048 million (2010: £778 million), primarily due to the impact of higher gas, oil and power wholesale commodity prices had on achieved prices and a 16 per cent. increase in nuclear power generation.

Adjusted operating profit from Centrica Storage decreased by 55.6 per cent. for the year ended 31 December 2011 to £75 million (2010: £169 million), reflecting a narrowing of seasonal gas price spreads.

Net finance cost

Net finance cost decreased 44.9 per cent. during the year ended 31 December 2011 to £146 million (2010: £265 million), reflecting the lower level of average gross debt during the year.

Taxation before exceptional items and certain re-measurements

Taxation charges before exceptional items and certain re-measurements increased 14.4 per cent. during the year ended 31 December 2011 to £810 million (2010: £708 million), primarily due to higher UK upstream tax rates, reflecting both an increased proportion of upstream gas operating profit, which is more heavily taxed and the increase in the supplementary corporation tax rate from 20 per cent. to 32 per cent. The effective tax rate on profits from business performance for the year ended 31 December 2011 was 39 per cent. (2010: 37 per cent.).

Profit for the year

Statutory profit for the year was £421 million (2010: £1,942 million). The reconciling items between profit from business performance and statutory profit are certain re-measurements and exceptional items as described below, as well as a £21 million loss from discontinued operations (2010: £62 million gain).

Exceptional items

The Group recorded a pre-tax net exceptional charge from continuing operations of £331 million (post-tax £262 million) for the year ended 31 December 2011. The exceptional charge consisted of the following elements:

- a curtailment gain of £333 million as a result of changes to the terms of various pension plans;
- an impairment charge of £226 million on UK power generation assets as a result of low spark spreads;
- a restructuring charge of £154 million relating to staff reductions following the announcement of a Group-wide cost reduction programme;
- a charge of £111 million for onerous European gas transportation contracts no longer utilised by the business after the decision was made to exit Europe and close the German wholesale business;
- a charge of £110 million related to the Rijnmond tolling contract in the Netherlands as a result of low market spark spreads; and
- a charge of £63 million for the migration of a significant supplier contract following its termination in December 2010.

A deferred tax charge of £204 million was also recognised following the increase in the supplementary corporation tax rate applicable to Upstream profits in the United Kingdom.

The Group recorded a pre-tax net exceptional charge of £283 million (post-tax £165 million) for the year ended 31 December 2010. The exceptional charge consisted of the following elements:

- an impairment charge of £96 million relating to generation, exploration and production assets in the UK was incurred as a result of low spark spreads and updated reserves data and changes to infrastructure development expectations;
- an impairment charge of £67 million relating to North American exploration and production assets was incurred as a result of declining commodity prices;
- an increase in the provision for North American wind power purchase agreements of £67 million following deterioration in North American power prices, to reflect the fair value of the obligation to purchase power above its net realisable value;
- an exceptional charge of £43 million relating to a major contract renegotiation in British Gas; and
- a further charge of £35 million to provide against an onerous gas procurement contract in Centrica Energy.

The Group disposed of its investment in Hummingbird Oil Pte, which was acquired as part of the wider Venture acquisition in 2009, which resulted in a profit on disposal of £25 million.

Certain re-measurements

For the year ended 31 December 2011 net charges of £344 million (pre-tax £463 million) related to certain re-measurements from continuing operations. In 2010, a net gain of £824 million (pre-tax £1,163 million) was recorded.

Liquidity and capital resources

The Group's liquidity requirements principally relate to cash required to operate its business, in particular payments for energy costs, margin payments required to support energy trading contracts, capital expenditure, payments to shareholders, interest and tax. The Group funds itself through a combination of working capital generated by its business lines, bank lending and capital markets debt.

Cash flows

The following table sets out the Group's cash flows for the six months ended 30 June 2013 and 2012 and for the years ended 31 December 2012, 2011 and 2010.

	Six months ended 30 June		Year ended 31 December		
	2013	2012	2012	2011	2010
	(£m)	(unaudited)		(£m)	
Net cash flow from operating activities	1,411	1,032	2,820	2,337	2,428
Net cash flow from investing activities	(647)	(1,443)	(2,558)	(1,400)	(1,584)
Net cash flow from financing activities	(897)	888	190	(907)	(1,677)
Cash and cash equivalents	800	954	931	479	451

Six months ended 30 June 2013 compared to six months ended 31 June 2012

Group operating cash flow before movements in working capital increased to £2,058 million for the six months ended 30 June 2013 from £1,681 million for the six months ended 30 June 2012. After working capital movements, and payments related to operating interest, tax and exceptional items, net cash flow from operations increased to £1,411 million (2012: £1,032 million). This increase in operating cash flow is primarily due to contributions resulting from the completion of the three North Sea acquisitions by Centrica Energy in 2012. The net cash outflow from investing activities decreased to £647 million (2012: £1,443 million). This decrease in outflow is primarily due to lower levels of acquisition activity during the first half of 2013 compared to 2012 when the Group acquired North Sea gas and oil assets from Statoil, ConocoPhillips and Total. The net cash outflow from financing activities was £897 million (2012: inflow of £888 million). The outflow was primarily due to interest paid, dividends paid and shares bought under the share repurchase scheme announced in February 2013. The 2012 inflow reflects the issue of bonds and commercial paper.

Year ended 31 December 2012 compared to year ended 31 December 2011

Group operating cash flow before movements in working capital increased to £3,542 million for the year ended 31 December 2012 from £3,065 million for the year ended 31 December 2011. After working capital movements, and payments related to operating interest, tax and exceptional items, net cash flow from operations increased to £2,820 million (2011: £2,337 million). This increase in operating cash flow was primarily due to contributions resulting from the completion of the North Sea acquisitions by Centrica Energy during the year. The net cash outflow from investing activities increased to £2,558 million (2011: £1,400 million). This increase in outflow was primarily due to the North Sea acquisitions. The net cash inflow from financing activities was £190 million (2011: outflow of £907 million). The 2012 inflow was primarily due to the net issuance of borrowings during the year exceeding dividends paid.

Year ended 31 December 2011 compared to year ended 31 December 2010

Group operating cash flow before movements in working capital increased to £3,065 million for the year ended 31 December 2011 from £3,010 million for the year ended 31 December 2010. After working capital movements, and payments related to operating interest, tax and exceptional items, net cash flow from operations decreased to £2,337 million (2010: £2,428 million). This decrease was mainly due to higher petroleum revenue tax payments. The net cash outflow from investing activities decreased to £1,400 million (2010: £1,584 million). The decrease was primarily due to higher cash outflows for acquisitions in 2010. The net cash outflow from financing activities was £907 million (2010: £1,677 million). The outflow in both years was primarily due to dividends and financing interest paid and in 2010 due to a net £684 million repayment of debt.

Capital expenditure

The Group seeks to maintain a low level of committed capital expenditure in order to have maximum flexibility in its investment choices and the Group anticipates spending approximately £1,100 million per annum to sustain its upstream oil and gas production. The Group has a range of capital investment options across its portfolio including a pipeline of upstream gas investment opportunities, choices in offshore wind, new-build CCGT and gas storage where the regulatory climate permits and acquisition opportunities in the North American downstream area. Major items of acquisition and disposal in 2012 included the cash payments for the Norwegian asset purchase from Statoil, an additional interest in the Statfjord field, a package of UK North Sea assets from Total, and the acquisitions of Home Warranty of America, the Carrot Creek assets and Energetix and NYSEG Solutions.

The following table sets out the Group's capital expenditure and acquisition expenditure by segment for the six months ended 30 June 2013 and 2012 and for the years ended 31 December 2012 and 2011.

	Six months ended 30 June		Year ended 31 December	
	2013	2012	2012	2011
	(£m)	(unaudited)	(£m)	
British Gas	80	66	161	211
Direct Energy	28	16	50	39
Centrica Energy Gas	495	332	906	644
Centrica Energy Power	53	168	314	300
Centrica Storage	27	33	37	59
Other	22	25	59	48
Total pre-acquisitions	705	640	1,527	1,301
Acquisitions and disposals	50	885	1,200	300
Total	755	1,525	2,727	1,601

The Group's capital expenditure for the year ended 31 December 2010 was £1,626 million.

The following table sets out the Group's additions to property, plant and equipment and intangible assets by segment for the six months ended 30 June 2013 and for the years ended 31 December 2012, 2011 and 2010.

	Property, plant and equipment				**Intangible Assets**			
	Six months ended 30 June 2013	**Year ended 31 December 2012**	**2011**	**2010**	**Six months ended 30 June 2013**	**Year ended 31 December 2012**	**2011**	**2010**
	(£m) (unaudited)	**(£m)**			**(£m) (unaudited)**	**(£m)**		
Residential energy supply	10	7	28	15	159	230	240	256
Residential services	18	44	26	6	5	9	22	15
Business energy supply and services	—	9	3	1	10	91	75	68
British Gas	28	60	57	22	174	330	337	339
Residential energy supply	1	—	—	—	3	3	4	2
Business energy supply	9	17	6	7	24	29	22	14
Residential and business services	1	3	2	2	—	2	1	5
Direct Energy	11	20	8	9	27	34	27	21
Gas	434	1,795	519	396	69	392	101	236
Power	8	76	89	82	2	8	6	28
Centrica Energy	442	1,871	608	478	71	400	107	264
Storage UK	17	42	59	33	2	1	—	—
Other	5	17	26	16	21	64	49	29
Total	503	2,010	758	558	295	829	520	653

Indebtedness

The Group seeks to maintain an efficient capital structure with a balance of debt and equity. Debt levels are restricted to limit the risk of financial distress and, in particular, to maintain strong credit ratings. The Group monitors its current and projected capital position on a regular basis, considering a medium-term view of three to five years, and different stress case scenarios, including the impact of changes in the Group's credit ratings and significant movements in commodity prices. A number of financial ratios are monitored, including those used by the credit rating agencies, such as debt to cash flow ratios and EBITDA to gross interest expense.

British Gas Insurance Limited ("BGIL") is required under PRA ("Prudential Regulation Authority") regulations to hold a minimum capital amount and has complied with this requirement in all of the periods under review. For the Group as a whole, net debt is limited to the greater of £5.0 billion and three times adjusted capital and reserves, which as of 31 December 2012 was £17.8 billion. This restriction can be amended or removed by the shareholders of the Company passing a special resolution.

As of 30 June 2013, with the exception of finance leases, all material debt issuances and loans were issued by the Company. None of these debt instruments contain any restrictive financial covenants.

The following tables set out a summary of the Group's net debt as of 30 June 2013 and 2012.

	Cash and cash equivalents	Current and non-current securities	Current and non-current borrowings	Derivatives	Net debt
			(£m)		
1 January 2013	**931**	**206**	**(5,328)**	**144**	**(4,047)**
Cash outflow from purchase of securities	(6)	6	—	—	—
Cash inflow from additional debt	72	—	(72)	—	—
Cash outflow from payment of capital element of finance leases	(15)	—	15	—	—
Cash outflow from repayment of other debt	(37)	—	37	—	—
Net cash outflow increasing net debt	(147)	—	—	—	(147)
Revaluation	—	(2)	42	(41)	(1)
(Increase)/decrease in interest payable	—	—	(44)	37	(7)
Exchange adjustments	2	1	(52)	—	(49)
30 June 2013	**800**	**211**	**(5,402)**	**140**	**(4,251)**

	Cash and cash equivalents	Current and non-current securities	Current and non-current borrowings	Derivatives	Net debt (restated)[1]
			(£m)		
1 January 2012	**518**	**218**	**(4,171)**	**143**	**(3,292)**
Cash inflow from net sale of securities	25	(25)	—	—	—
Cash inflow from additional debt	1,533	—	(1,533)	—	—
Cash outflow from payment of capital element of finance leases	(14)	—	14	—	—
Cash outflow from repayment of other debt	(15)	—	15	—	—
Net cash outflow increasing net debt	(1,052)	—	—	—	(1,052)
Revaluation	—	3	(2)	5	6
(Decrease)/increase in interest payable	—	—	(73)	44	(29)
Acquisitions	—	5	—	—	5
Exchange adjustments	(2)	1	15	—	14
Other non-cash movements	2	—	5	—	7
30 June 2012	**995**	**202**	**(5,730)**	**192**	**(4,341)**

Note:

(1) To align with management reporting, net debt has been restated to include mark-to-market values on derivative financial instruments used to hedge offsetting changes in borrowings.

Contractual Obligations

The following table summarises the maturity profile for the Group's debt and pension funding obligations and operating lease commitments as of 30 June 2013.

		Maturity split					
	Total	**<1 year**	**1-2 years**	**2-3 years**	**3-4 years**	**4-5 years**	**>5 years**
				(£m)			
Long-term debt obligations:							
Bank overdrafts and loans	**358**	30	0	0	0	0	328
Bonds	**4,463**	317	439	0	328	0	3,379
Commercial paper	**156**	156	0	0	0	0	0
Interest accruals	**141**	141	0	0	0	0	0
Finance lease obligations(1)	**284**	30	34	36	34	31	119
Total debt obligations(2)	**5,402**	674	473	36	362	31	3,826
Pension funding obligations(3)	**336**	84	84	84	84	0	0
Operating lease obligations(4)	**1,158**	269	150	132	83	74	450
Total contractual obligations	**6,896**	1,027	707	252	529	105	4,276

Note:

(1) Finance lease obligations are principally in respect of property, plant and equipment relating to the Power generation and Gas production and storage capabilities.

(2) Represents future debt repayment obligations at 30 June 2013, on a discounted basis, excluding future finance charges.

(3) Represents all future committed pension deficit payments agreed with the trustees of the Group's pension schemes, due on an undiscounted basis.

(4) Represents all future minimum lease payments under non-cancellable operating leases. In accordance with IFRS, operating lease obligations are not held on the Group's balance sheet.

Financial position

Net assets

The Group had net assets of £5,864 million and £5,927 million as at 30 June 2013 and 31 December 2012, respectively.

Goodwill acquired through business combinations and indefinite-lived intangible assets is allocated for impairment testing purposes to individual or groups of CGUs each representing the lowest level within the Group at which the goodwill or indefinite-lived intangible asset is monitored for internal management purposes. Value in use calculations have been used to determine recoverable amounts for all of the goodwill and indefinite-lived intangible asset balances, with the exception of the impairment tests for Centrica Energy—Upstream gas and oil CGUs, where fair value less costs to sell has been used as the basis for determining recoverable amounts. For further detail, please see Note 14 to the 2012 Financial Statements.

The Group's share of joint ventures' and associates' gross assets and gross liabilities principally comprise its interests in certain wind farms and nuclear facilities.(2) On 4 February 2013, the Group announced its decision not to proceed with the nuclear new build investment and recorded an exceptional impairment which included the carrying value of its investment in NNB Holding Company Limited and the value attributable to nuclear new build in the British Energy acquisition, both of which had been previously included under interests in associates. For further detail, please see Note 16 to the 2012 Financial Statements and Note 13 to the Interim Results.

Reflected within net assets are provisions for decommissioning costs. Provision is made for the estimated net present cost of decommissioning gas production and storage facilities at the end of their useful lives. The majority of the provision is expected to be utilised between 2020 and 2030. The estimate is based on 2P reserves, price levels and technology at the relevant balance sheet date. A provision was also made for the estimated net present cost of decommissioning British Energy's nuclear power stations and the costs of waste management and spent fuel. As at 31 December 2012, the Group's decommissioning provision was £2,171 million.

(2) The Group has a 50 per cent. equity interest in both GLID Wind Farms TOPCO Ltd and Lincs Wind Farms Ltd, each of which contains non-recourse project finance debt. The combined total of these project finance loans and facilities is approximately £1.35 billion.

Commitments

The Group procures commodities through a mixture of production from gas fields, power stations, wind farms and procurement contracts. Procurement contracts include short-term forward market purchases of gas and electricity at fixed and floating prices. They also include gas and electricity contracts indexed to market prices and long-term gas contracts with non-gas indexation. The commitments in relation to commodity purchase contracts disclosed below are stated net of amounts receivable under commodity sales contracts, where there is a right of set-off with the counterparty. The total volume of gas to be taken under certain long-term structured contracts depends on a number of factors, including the actual reserves of gas that are eventually determined to be extractable on an economic basis. The commitments disclosed below are based on the minimum quantities of gas that the Group is contracted to buy at estimated future prices. These commitments are not held on the Group's balance sheet because they are bilateral executory contracts and the Group's obligation does not become effective until the relevant counterparty performs. All liabilities are recorded in accordance with IFRS as applied through the Group's accounting policies.

The following table sets out the Group's commitments as of 31 December 2012.

	As of 31 December 2012
	(£m)
Commitments in relation to the acquisition of property, plant and equipment:	
Development of Norwegian oil and gas assets	283
Development of Cygnus gas field	88
Other capital expenditure	21
Commitments in relation to the acquisition of intangible assets:	
Renewable obligation certificates to be purchased from joint ventures(1)	1,376
Renewable obligation certificates to be purchased from other parties	784
EUAs and CERs	42
Other intangible assets(2)	105
Other commitments:	
Commodity purchase contracts(3)	51,933
LNG capacity	844
Transportation capacity	936
Outsourcing of services	277
Commitments to invest in joint ventures	174
Other long-term commitments	562
Operating lease commitments:	
Future minimum lease payments under non-cancellable operating leases(2)(4)	974

Notes:

(1) Renewable obligation certificates are purchased from several joint ventures which produce power from wind energy under long-term offtake agreements (up to 15 years). The commitments disclosed above are the gross contractual commitments and do not take into account the Group's economic interest in the joint venture.

(2) Included within future minimum lease payments and other intangible assets are commitments of £67 million relating to exploration activity.

(3) As of 31 December 2012, the maturity analysis for commodity purchase contracts was: <1 year £9.2 billion, 1-2 years £7.2 billion, 2-3 years £5.9 billion, 3-4 years £5.1 billion, 4-5 years £3.0 billion and >5 years £21.5 billion.

(4) As of 31 December 2012, the maturity analysis for the total minimum lease payments under non-cancellable operating leases was: <1 year £222 million, 1-2 years £98 million, 2-3 years £82 million, 3-4 years £64 million, 4-5 years £54 million and >5 years £454 million.

On 25 March 2013, the Group announced that it had entered into a 20 year agreement with Cheniere to purchase 92bcf per annum of LNG volumes for export from the Sabine Pass liquefaction plant in Louisiana in the United States, subject to a number of project milestones and regulatory approvals being achieved. Under the terms of the agreement and subject to these approvals, the Group will make commodity purchases and capacity payments of up to £10 billion based on current gas prices. The target date for first commercial delivery is September 2018.

Qualitative and quantitative disclosures about financial risk management

During the period, financial risk management was overseen by the Group Financial Risk Management Committee ("GFRMC") according to objectives, targets and policies set by the Board. Commodity price risk management is carried out in accordance with individual business unit Financial Risk Management Committees and their respective financial risk management policies, as approved by the GFRMC under delegated authority of the Board. The Financing & Treasury policy, which includes management of currency risk, interest rate risk, equity price risk and liquidity risk, is approved by the Board. The wholesale credit risks associated with commodity trading and treasury positions are managed in accordance with the Group's credit risk policy. Downstream credit risk management is carried out in accordance with individual business unit credit policies.

Market risk management

Commodity price risk management

During the six months ended 30 June 2013, the Group continued to be exposed to commodity price risk in its upstream assets, energy procurement contracts, downstream and proprietary energy trading activities. Specific limits are used to manage the exposure to commodity prices associated with the Group's activities to an acceptable level. Volumetric limits are supported by Profit at Risk ("PaR") and Value at Risk ("VaR") metrics in the United Kingdom and in North America to measure the Group's exposure to commodity price risk. Limits are also set on PaR and VaR measurements as a further control over exposure to market prices.

The Group measures and manages the commodity price risk associated with the Group's entire energy procurement, upstream and downstream portfolio. Only certain of the Group's energy procurement, upstream and downstream contracts constitute financial instruments under IAS 39.

The net gain of £105 million from operations during the six months ended 30 June 2013 (six months ended 30 June 2012: £511 million) on the re-measurement of energy contracts included within Group operating profit largely represents the unwinding of mark-to-market positions created by gas and power purchase contracts which were priced above the current wholesale market value of energy at the start of the period, partially offset by the impact of wholesale market price movements during the period. These balance sheet mark-to-market positions are calculated with reference to forward energy prices and therefore the extent of the economic gain or loss arising over the life of these contracts is uncertain, and entirely dependent upon the level of future wholesale energy prices. Generally, subject to short-term balancing, the ultimate net charge to cost of sales will be consistent with the price of energy agreed in these contracts and the fair value adjustments will reverse as the energy is supplied over the life of the contract.

Currency risk management

The Group is exposed to transactional exposure (currency risk on foreign currency denominated forecast transactions, firm commitments, monetary assets and liabilities) and translational exposure (currency risk on net investments in foreign operations).

The Group is exposed to transactional currency risk on transactions denominated in currencies other than the underlying functional currency of the commercial operation transacting. The Group's primary functional currencies are pounds sterling in the United Kingdom, Canadian dollars in Canada, US dollars in the US, Norwegian krone in Norway and euros in Europe. The risk is that the functional currency value of cash flows will vary as a result of movements in exchange rates. Transactional exposure arises from the Group's energy procurement activities in the United Kingdom and in Canada, where a proportion of transactions are denominated in euros or US dollars and on certain capital commitments denominated in foreign currencies. In addition, in order to optimise the cost of funding, the Group has, in certain cases, issued foreign currency denominated debt, primarily in US dollars, New Zealand dollars, euros or Japanese yen. The Group principally manages its transactional exposure through forward currency hedges.

The Group is exposed to translational currency risk as a result of its net investments in North America and Europe. The risk is that the pounds sterling value of the net assets of foreign operations will decrease with changes in foreign exchange rates. The Group's policy is to protect the pounds sterling book value of its net investments in foreign operations where possible, subject to certain parameters, by holding foreign currency debt, entering into foreign currency derivatives, or a mixture of both.

Interest rate risk management

In the normal course of business, the Group borrows to finance its operations. The Group is exposed to interest rate risk because the fair value of fixed rate borrowings and the cash flows associated with floating rate borrowings fluctuate with changes in interest rates. The Group's policy is to manage the interest rate risk on long-term borrowings by ensuring the exposure to floating interest rates remains within a 30 to 70 per cent. range, including the impact of interest rate derivatives.

Credit risk management

During the six months ended 30 June 2013, counterparty credit exposure issues remained a focal point and the Group continues to be vigilant in managing counterparty risks in accordance with its approved financial risk management policies. The economic environment continues to impact the markets in which the Group is active; however, the Group has not altered its rating thresholds for counterparty credit limits and continues to operate within its limits. In the United States and the United Kingdom, there is a continuing emphasis on understanding the impact of regulatory changes which may result in an increase in trading over exchanges or via zero threshold margined contracts. This helps to reduce counterparty credit risk, but carries increased liquidity requirements.

Liquidity risk management

The Group has a number of treasury and risk policies to monitor and manage liquidity risk. Cash forecasts identifying the Group's liquidity requirements are produced regularly and are stress-tested for different scenarios, including, but not limited to, reasonably possible increases or decreases in commodity prices and the potential cash implications of a credit rating downgrade. The Group seeks to ensure that sufficient financial headroom exists for at least a 12-month period to safeguard the Group's ability to continue as a going concern. It is the Group's policy to maintain committed facilities and/or available surplus cash resources of at least £1,200 million, to raise at least 75 per cent. of its net debt (excluding non-recourse debt) in the long-term debt market and to maintain an average term to maturity in the recourse long-term debt portfolio greater than five years.

At 30 June 2013, the Group held £800 million (31 December 2012: £931 million) of cash and cash equivalents and had undrawn committed credit facilities of £3,444 million (31 December 2012: £3,029 million). 123 per cent. (31 December 2012: 130 per cent.) of the Group's net debt has been raised in the long-term debt market and the average term to maturity of the long-term debt portfolio was 12.3 years (31 December 2012: 12.6 years).

The Group holds cash as collateral against counterparty balances and also pledges cash as collateral, principally under margin calls, to cover exposure to mark-to-market positions on certain wholesale commodity contracts. Generally, cash paid or received as collateral is interest-bearing and is free from any restriction over its use by the holder.

Critical accounting judgements

The Group makes judgements in applying its accounting policies that have a significant effect on the Group's Consolidated Financial Statements. For a further discussion of the Group's critical accounting judgements refer to Notes to the Consolidated Financial Statements.

Metering contracts

The DECC has modified the UK gas and electricity supply licences requiring all domestic premises to be fitted with compliant smart meters for measuring energy consumption by 31 December 2020. The Group has a number of existing rental contracts for non-compliant meters that include penalty charges if these meters are removed from use before the end of their deemed useful lives. The Group considers that these contracts are not onerous until the meters have been physically removed from use and therefore only recognises a provision at that point.

Energy Company Obligation

ECO requires UK-licenced energy suppliers to improve the energy efficiency of domestic households from 1 January 2013. Targets are set in proportion to the size of historic customer bases and must be delivered by 31 March 2015. The Group continues to judge that it is not legally obligated by this order until

31 March 2015. Accordingly, the costs of delivery are recognised as incurred, when cash is spent or unilateral commitments made resulting in obligations that cannot be avoided.

Key sources of estimation uncertainty

The Group makes assumptions concerning future and other key sources of estimation uncertainty at balance sheet dates that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the subsequent financial year.

Revenue recognition—unread gas and electricity meters

Revenue for energy supply activities includes an assessment of energy supplied to customers between the date of the last meter reading and the year end (unread). Unread gas and electricity comprises both billed and unbilled revenue. It is estimated through the billing systems, using historical consumption patterns, on a customer-by-customer basis, taking into account weather patterns, load forecasts and the differences between actual meter reads being returned and system estimates. Actual meter reads continue to be compared to system estimates between the balance sheet date and the finalisation of the accounts. An assessment is also made of any factors that are likely to materially affect the ultimate economic benefits which will flow to the Group, including bill cancellation and re-bill rates. To the extent that the economic benefits are not expected to flow to the Group, the value of that revenue is not recognised. The judgements applied, and the assumptions underpinning these judgements, are considered to be appropriate. However, a change in these assumptions would have an impact on the amount of revenue recognised.

Industry reconciliation process—cost of sales

Industry reconciliation procedures are required as differences arise between the estimated quantity of gas and electricity the Group deems to have supplied and billed customers, and the estimated quantity industry system operators deem the individual suppliers, including the Group, to have supplied to customers. Difference in deemed supply is referred to as imbalance. The reconciliation procedures can result in either a higher or lower value of industry deemed supply than has been estimated as being supplied to customers by the Group, but in practice tends to result in a higher value of deemed supply. The Group then reviews the difference to ascertain whether there is evidence that its estimate of amounts supplied to customers is inaccurate or whether the difference arises from other causes. The Group's share of the resulting imbalance is included within commodity costs charged to cost of sales. Management estimates the level of recovery of imbalance which will be achieved either through subsequent customer billing or through developing industry settlement procedures.

Decommissioning costs

The estimated cost of decommissioning at the end of the producing lives of fields (including storage assets) is reviewed periodically and is based on reserves, price levels and technology at the balance sheet date. Provision is made for the estimated cost of decommissioning at the balance sheet date. The payment dates of total expected future decommissioning costs are uncertain and dependent on the lives of the facilities, but are currently anticipated to be incurred until 2055, with the majority of the costs expected to be paid between 2020 and 2030.

Significant judgements and estimates are also made about the costs of decommissioning British Energy's nuclear power stations and the costs of waste management and spent fuel. These estimates impact the carrying value of the Group's investment. Various arrangements and indemnities are in place with the UK Secretary of State with respect to these costs.

Determination of fair values—energy derivatives

Fair values of energy derivatives are estimated by reference in part to published price quotations in active markets and in part by using valuation techniques. More detail on the assumptions used in determining fair values is provided in Note 24 to the 2012 Financial Statements.

Gas and liquids reserves

The volume of proven and probable ("2P") gas and liquids reserves is an estimate that affects the unit of production method of depreciating assets which produce gas and liquids as well as being a significant estimate affecting decommissioning and impairment calculations. The factors impacting gas and liquids estimates and the process for estimating reserve quantities and reserve recognition are described in the "Gas and Liquids Reserves" disclosure in the Notes to the 2012 Financial Statements.

The impact of a change in estimated 2P reserves is dealt with prospectively by depreciating the remaining book value of producing assets over the expected future production. If 2P reserves estimates are revised downwards, earnings could be affected by higher depreciation expense or an impairment of the asset's book value.

Impairment of long-lived assets

The Group has several material long-lived assets that are assessed or tested for impairment at each reporting date in accordance with the Group's accounting policy. The Group makes judgements and estimates in considering whether the carrying amounts of these assets or cash generating units ("CGUs") are recoverable. The key assets that are subjected to impairment tests are upstream gas and oil assets, power generation assets, storage facility assets, nuclear investment (investment in associate) and goodwill. A discussion of the assumptions used to determine recoverable amounts is included in Notes 14 and S2 to the 2012 Financial Statements.

Credit provisions for trade and other receivables

The methodology for determining provisions for credit losses on trade and other receivables and the level of such provisions is set out in Note 18 to the 2012 Financial Statements. Although the provisions recognised are considered appropriate, the use of different assumptions or changes in economic conditions could lead to changes in the provisions and therefore impact profit or loss.

Pensions and other post employment benefits

The cost of providing benefits under defined benefit schemes is determined separately for each of the Group's schemes under the projected unit credit actuarial valuation method. Actuarial gains and losses are recognised in full in the period in which they occur. The key assumptions used for the actuarial valuation are based on the Group's best estimate of the variables that will determine the ultimate cost of providing post-employment benefits, on which further detail is provided in Note 29 to the 2012 Financial Statements.

Provisions for onerous contracts

The Group has entered into a number of commodity procurement and capacity contracts related to specific assets in the ordinary course of its business. Where the unavoidable costs of meeting the obligations under these contracts exceed the associated, expected future net benefits, an onerous contract provision is recognised. The calculation of these provisions will involve the use of estimates. Key onerous provisions relate to the Rijnmond power station operating lease in the Netherlands, certain European gas transportation capacity contracts and Direct Energy wind farm power purchase agreements. Further detail is provided in Note 3 to the 2012 Financial Statements.

DIRECTORS

Board of Directors

The Directors of the Company are as follows and their profiles are set out below:

Name	Age	Role
Sir Roger Carr	67	Chairman of the Board[(1)]
Sam Laidlaw	57	Chief Executive Officer
Margherita Della Valle	48	Non-Executive Director
Mary Francis CBE	65	Senior Independent Director
Mark Hanafin	53	Managing Director, International Upstream
Lesley Knox	60	Non-Executive Director
Mike Linn	61	Non-Executive Director
Nick Luff	46	Group Finance Director
Ian Meakins	57	Non-Executive Director
Paul Rayner	59	Non-Executive Director
Chris Weston	49	Managing Director, International Downstream

(1) On 4 October 2013, the Group announced the appointment of Richard Haythornthwaite as Chairman of the Board, with effect from 1 January 2014. He will be joining the Board as a non-executive director on 14 October 2013.

The business address of the directors of the Company is c/o Centrica plc, Millstream, Maidenhead Road, Windsor, Berkshire SL4 5GD. There are no potential conflicts of interest between the duties to the Company of the directors and their private interests and/or other duties.

Sir Roger Carr, aged 67 (Chairman of the Board)

Sir Roger Carr joined the Board as a Non-Executive Director on 1 January 2001. He was appointed Chairman of the Board in May 2004 and is chairman of the nominations committee. He is a member of the United Kingdom Prime Minister's Business Advisory Group and is a member of the Confederation of British Industry ("CBI") having been the CBI president between 2011 and 2013. He remains deputy chairman and senior independent director of the Court of the Bank of England. He is also a senior adviser to Kohlberg Kravis Roberts and a trustee of the Landau Forte Charitable Trust. He has previously held a number of senior appointments including chairman of Mitchells & Butlers plc and Cadbury plc. He is a fellow of the Royal Society for the encouragement of the Arts, Manufacturers and Commerce and a visiting fellow to the Said Business School, Oxford. Throughout his career he has served on a number of external committees including the Higgs Committee on Corporate Governance and Business for New Europe.

Sir Roger Carr holds a B.A. in Business Studies from Nottingham Trent University.

Sir Roger Carr will step down as Chairman of the Board on 31 December 2013 following his decision to join the board of BAE Systems plc as a non-executive director and chairman designate on 1 October 2013.

Sam Laidlaw, aged 57 (Chief Executive Officer)

Sam Laidlaw joined Centrica as Chief Executive Officer ("CEO") on 1 July 2006. He is chairman of the executive committee and the disclosure committee. In January 2008, he was appointed a non-executive director of HSBC Holdings plc and in December 2010 he was appointed as the lead non-executive director on the board of the Department for Transport. He was also a member of the United Kingdom Prime Minister's Business Advisory Group. Previously he was executive vice president of the Chevron Corporation, CEO at Enterprise Oil and president and chief operating officer at Amerada Hess. He is a trustee of the medical charity RAFT.

Sam Laidlaw holds an M.A. in Law from Cambridge University (Gonville & Caius College), an M.B.A. from INSEAD and was admitted as a solicitor in 1980.

Margherita Della Valle, aged 48 (Non-Executive Director)

Margherita Della Valle joined the Board on 1 January 2011 and became chairman of the audit committee on 1 July 2013. In October 2010, she was appointed group financial controller of Vodafone Group Plc, prior to which she was chief financial officer of Vodafone's European region from April 2007 to October 2010 and chief financial officer of Vodafone Italy from 2004 to 2007. Previously, she joined Omnitel Pronto

Italia in Italy in 1994 and held various consumer marketing positions in business analytics and customer base management prior to moving to finance. Omnitel was acquired by Vodafone Group in 2000.

Margherita Della Valle holds a degree in Economics and Social Services from Bocconi University, Milan.

Mary Francis CBE, aged 65 (Senior Independent Director)

Mary Francis CBE joined the Board on 22 June 2004 and is Senior Independent Director, chairman of the corporate responsibility committee and deputy chair of the nominations committee. In October 2012 she was appointed to the board of Swiss Reinsurance Company Ltd, in April 2013 she was appointed as a non-executive director of the Swiss Re Group and in May 2013 she was appointed as a non-executive director of Ensco plc. She is a senior adviser to Chatham House and chair of governors of James Allen's Girls' School. She is a former non-executive director of Aviva plc, Cable & Wireless Communications Plc, the Bank of England, Alliance & Leicester plc and St. Modwen Properties plc. She is a former director general of the Association of British Insurers, and was a senior civil servant in the Treasury and the Prime Minister's Office.

Mary Francis CBE holds an M.A. in history from Cambridge University (Newnham College).

Mark Hanafin, aged 53 (Managing Director, International Upstream)

Mark Hanafin was appointed Managing Director, International Upstream on 1 July 2013. He joined Centrica as managing director, Centrica Energy on 14 July 2008 and was appointed as a non-executive director of EDF Energy Nuclear Generation Group Limited in November 2009. Previously he spent 21 years with Royal Dutch Shell, most recently as CEO of Shell Energy North America in Houston. Prior to joining Shell, he worked for General Electric Company having qualified as a chartered engineer.

Mark Hanafin holds a BSc in Mechanical Engineering from Brunel University and is a Chartered Engineer.

Lesley Knox, aged 60 (Non-Executive Director)

Lesley Knox joined the Board on 1 January 2012 and is chairman of the remuneration committee. She is a non-executive director of SABMiller Plc and is a trustee of the Grosvenor Estates and chairman of Grosvenor Group Limited. She was previously with British Linen Bank in 1997, becoming governor in 1999, and was subsequently a founder director of British Linen Advisers from 1999 to 2003. She was previously senior non-executive director of Hays Plc and also spent 15 years with Kleinwort Benson from 1981 to 1996, first in corporate finance and then as chief executive of the institutional asset management business.

Lesley Knox holds an MA (Hons) in Law from Cambridge University (Churchill College).

Mike Linn, aged 61 (Non-Executive Director)

Mike Linn joined the Board on 1 June 2013. In 2003, he founded LINN Energy, LLC, and serves on the board as a non-executive director having previously been chairman, CEO and president. He is also a director of Nabors Industries and Black Stone Minerals and senior adviser to Quantum Energy Partners. Mike sits on the National Petroleum Council and the Board of the Independent Petroleum Association of America. He is a Texas representative for the Legal and Regulatory Affairs Committee of the Interstate Oil and Gas Compact Commission. Amongst his other roles, Mike was previously president of Allegheny Interests (2000-2003) and president and CEO of Meridian Exploration Company, Pittsburgh (1990-2000).

Mike Linn holds a BA in Political Science from Villanova University and a JD from the University of Baltimore.

Nick Luff, aged 46 (Senior Independent Director)

Nick Luff joined Centrica as Group Finance Director on 1 March 2007. He was appointed as a non-executive director of Lloyds Bank Group in March 2013. He was previously chief financial officer of The Peninsular & Oriental Steam Navigation Company (P&O) and has held a number of other senior financial roles at P&O, having qualified as a chartered accountant at KPMG. Until December 2010, he was a non-executive director of QinetiQ Group plc.

Nick Luff holds a BSc in Mathematics from Oxford University and is a member of the Institute of Chartered Accountants in England and Wales and a member of the Association of Corporate Treasurers.

Ian Meakins, aged 57 (Non-Executive Director)

Ian Meakins joined the Board on 1 October 2010. In July 2009, he joined the Wolseley Group as CEO. He was previously CEO of Travelex Holdings Limited and for two years prior to that he was CEO of Alliance Unichem plc until their merger with Boots in 2006. He spent 12 years with Diageo including four years as president European major markets and global supply. His early career was with Procter and Gamble.

Ian Meakins holds a BA in Natural Sciences from the University of Cambridge (St. Catharine's College).

Paul Rayner, aged 59 (Non-Executive Director)

Paul Rayner joined the Board on 22 September 2004. He will step down from the Board on 31 December 2014 having stepped down as chairman of the audit committee on 1 July 2013. In 2008, he was appointed a non-executive director of Qantas Airways Limited and Boral Limited. In May 2011 he was also appointed as a non-executive director of Treasury Wine Estates Limited in Australia and was appointed chairman in September 2012. He was finance director of British American Tobacco plc from 2002 until April 2008. In 1991 he joined Rothmans Holdings Limited in Australia, holding senior executive appointments, and became chief operating officer of British American Tobacco Australasia Limited in September 1999.

Paul Rayner holds a Bachelor of Economics from the University of Tasmania and a Master of Administration from Monash University, Melbourne and is a member of the Australian Institute of Company Directors.

Chris Weston, aged 49 (Managing Director, International Downstream)

Chris Weston was appointed to the Board on 1 July 2009 and on 1 July 2013 he was appointed Managing Director, International Downstream. He was previously managing director, North America from July 2009. Prior to this, he was managing director, British Gas Services from June 2005 and managing director, British Gas Business from January 2002. He joined the Group in November 2001, following the acquisition of One Tel where he was the managing director of Europe. Previously, he worked for Cable & Wireless and also spent seven years in the army with the Royal Artillery.

Chris Weston holds a PhD from Imperial College, London.

Corporate Governance

The Board structure

As at the date of this document, the Board consists of the Chairman, four Executive Directors and six Non-Executive Directors.

The Board supports high standards of corporate governance. As at the date of this Offering Circular, the Board is compliant with the United Kingdom Corporate Governance Code and will continue to comply with its terms.

Board committees

The Board has established the following committees:

Audit committee

The audit committee meets not less than three times per year and has responsibility for, among other things, monitoring the integrity of the Group's financial statements and reviewing its summary financial statements. It oversees the Group's relationship with its external auditors and reviews the effectiveness of the external audit process. The committee gives due consideration to laws and regulations, the provisions of the United Kingdom Corporate Governance Code and the requirements of the Listing Rules. It also has responsibility for reviewing the effectiveness of the Group's system of internal controls and risk management systems. The ultimate responsibility for reviewing and approving the interim and annual financial statements remains with the Directors.

Executive committee

The Committee regularly considers financial and operational performance against an operating plan, health and safety performance, human resourcing issues including employee engagement, senior management changes and succession planning and strategic investments including proposed acquisitions and divestments. In particular, major proposed transactions are considered by the executive committee prior to consideration by the Board together with progress made on major operational projects.

Nominations committee

The nominations committee meets not less than twice per year and has responsibility for making recommendations to the Board on the composition of the Board and its committees, retirements and appointments of additional and replacement Directors and ensuring compliance with the United Kingdom Corporate Governance Code.

Remuneration committee

The remuneration committee normally meets four times per year and has responsibility for determining and making recommendations to the Board on the Group's framework and policy for the remuneration of the Chairman of the Board, the Executive Directors and other senior executives. The remuneration committee will also ensure compliance with the United Kingdom Corporate Governance Code in this respect.

Corporate responsibility

The corporate responsibility committee normally meets four times per year and is responsible for endorsing the Group's corporate responsibility strategy, policies, processes and standards, assist periodic reviews of them and oversee the effectiveness of management's implementation. The committee also reviews the effectiveness of the Group's communications about corporate responsibility strategy and performance externally and internally.

Disclosure

The disclosure committee meets as and when required in accordance with its terms of reference and is responsible for the implementation and monitoring of systems and controls in respect of the management and disclosure of inside information and for ensuring that regulatory announcements, shareholder circulars, prospectuses and other documents issued by the Group comply with applicable legal or regulatory requirements.

Board compensation

The total remuneration for the Directors of the Group for the year ended 31 December 2012 was £17,402,000. The total emoluments, including contributions made in respect of pension plans, for the Directors of the Group for the year ended 31 December 2012 was £8,799,000.

SIGNIFICANT SHAREHOLDERS

As of 27 February 2013 (being the latest practicable date prior to the publication of this Offering Circular), the Company had been notified, pursuant to the FCA's Disclosure and Transparency Rules, of the following material shareholdings:

Shareholder	Number of Shares	Percentage of Group Ordinary Share Capital
Invesco Limited	258,200,185	4.97

Save as disclosed above, the Group Directors are not aware of any other person who, directly or indirectly, has a material shareholding in the issued ordinary share capital of the Group.

None of the Group's major shareholders has, or will have, different voting rights attached to the ordinary shares they hold.

DESCRIPTION OF THE NOTES

The following is a summary of the material provisions of the Notes and the Fiscal and Paying Agency Agreements (as described below). The summary does not purport to be complete and is qualified in its entirety by reference to all of the provisions of the Notes and the Fiscal and Paying Agency Agreements. It does not restate those agreements in their entirety. A copy of each Fiscal and Paying Agency Agreement will be available for inspection during normal business hours at any time after the initial issue date of the Notes at the specified office of the Fiscal and Paying Agent. See "General Information—Documents on Display". In this section, references to the "Company", mean Centrica plc and not its Subsidiaries. Any capitalised term used herein but not defined shall have the meaning assigned to such term in the Fiscal and Paying Agency Agreements.

General

The $750,000,000 4.000 per cent. senior notes due 2023 (the "2023 Notes") and $600,000,000 5.375 per cent. senior notes due 2043 (the "2043 Notes" and, together with the 2023 Notes, the "Notes" and each separately a "Note") will be issued in registered form each under a Fiscal and Paying Agency Agreement to be dated, in each case, as of 16 October 2013 (collectively, the "Fiscal and Paying Agency Agreements") between Centrica plc (the "Company") and Citibank, N.A., London Branch as paying agent, transfer agent and registrar (referred to collectively in such capacities as the "Fiscal and Paying Agent" and, in each such several capacities as the "Paying Agent", "Transfer Agent" and "Registrar"). The Fiscal and Paying Agency Agreements are not required to be, and will not be, qualified under the US Trust Indenture Act of 1939, as amended (the "Trust Indenture Act"), and will not incorporate by reference the provisions of the Trust Indenture Act. Consequently, the Holders of Notes generally will not be entitled to the protections provided under the Trust Indenture Act to holders of debt securities issued under a qualified indenture, including those requiring a trustee to resign in the event of certain conflicts of interest and to inform the holders of Notes of certain relationships between it and the Company. In this "Description of the Notes", the terms "Holder", "Noteholder" and other similar terms refer to a registered holder of Notes, and not to a beneficial owner of a book-entry interest in any Notes, unless the context otherwise clearly requires.

For so long as any Notes remain outstanding and are "restricted securities" within the meaning of Rule 144(a)(3) under the Securities Act, the Company will, during any period in which it is neither subject to Section 13 or 15(d) of the US Securities Exchange Act of 1934, as amended (the "Exchange Act"), nor exempt from reporting pursuant to Rule 12g3-2(b) under the Exchange Act, make available to any Holder (or any beneficial owner of a book-entry interest in such Notes designated by the holder thereof) in connection with any sale thereof and to any prospective purchaser of Notes or a book-entry interest in Notes designated by such Holder, in each case upon request of such Holder, the information specified in, and meeting the requirements of, Rule 144A(d)(4) under the Securities Act. As of the date of this Offering Circular, the Company is exempt from reporting pursuant to Rule 12g3-2(b) under the Exchange Act.

The Regulation S Notes will be resold outside the United States in offshore transactions in reliance on Regulation S under the Securities Act.

Principal, Maturity and Interest

The Notes will be unsecured and unsubordinated obligations of the Company (except for the provisions of "—Covenants—Negative pledge" below). The 2023 Notes are initially issuable in an aggregate principal amount of $750,000,000 and will mature on 16 October 2023. The 2043 Notes are initially issuable in an aggregate principal amount of $600,000,000 and will mature on 16 October 2043. The 2023 Notes will bear interest at 4.000 per cent. per annum, and the 2043 Notes will bear interest at 5.375 per cent. per annum, in each case from the date of the initial issuance of the Notes or from the most recent Interest Payment Date to which interest has been paid or provided for, payable semi-annually in arrears on 16 April and 16 October of each year (each, an "Interest Payment Date") commencing on 16 April 2014 to the person in whose name any 2023 Note or 2043 Note, as applicable, is registered at the close of business on 1 April or 1 October (whether or not a Business Day) immediately preceding such Interest Payment Date (each, a "Record Date"), notwithstanding any transfer or exchange of such Notes subsequent to the Record Date and prior to such Interest Payment Date, except that, if and to the extent the Company shall default in the payment of the interest due on such Interest Payment Date and the applicable grace period shall have expired, such defaulted interest may at the option of the Company be paid to the persons in whose names outstanding Notes are registered at the close of business on a subsequent Record Date (which shall not be less than 10 days prior to the date of payment of such defaulted interest) established by notice given by first class mail by or on behalf of the Company to the Holders (which term means registered holders) of the

2023 Note or 2043 Note, as applicable, not less than 15 days preceding such subsequent Record Date. Interest will be computed on the basis of a 360 day year consisting of twelve 30 day months or in the case of an incomplete month, the number of days elapsed. If the date on which any interest payment, principal payment or Additional Amount is to be made is not a Business Day, such payment will be made on the next day which is a Business Day without any further interest or other amounts being paid or payable in connection therewith.

Optional Redemption

The Company may redeem any series of Notes in whole or in part, at the Company's option, at any time and from time to time at a redemption price equal to (i) if such redemption occurs prior to 16 July 2023 in the case of the 2023 Notes or 16 April 2043 in the case of the 2043 Notes, the greater of (a) 100 per cent. of the principal amount of the Notes to be redeemed and (b) as determined by the Independent Investment Banker, the sum of the present values of the applicable Remaining Scheduled Payments discounted to the date of redemption (the "Redemption Date") on a semi-annual basis (assuming a 360 day year consisting of twelve 30 day months or, in the case of an incomplete month, the number of days elapsed) at the Treasury Rate plus 25 basis points in the case of the 2023 Notes and 25 basis points in the case of the 2043 Notes, or (ii) if such redemption occurs on or after 16 July 2023 in the case of the 2023 Notes or 16 April 2043 in the case of the 2043 Notes, 100 per cent. of the principal amount of the Notes to be redeemed, together, in each case, with accrued and unpaid interest on the principal amount of the Notes to be redeemed to but excluding the Redemption Date.

In connection with such optional redemption the following defined terms apply:

- "Comparable Treasury Issue" means the United States Treasury security selected by the Independent Investment Banker that would be utilised, at the time of selection and in accordance with customary financial practice, in pricing new issues of corporate debt securities of comparable maturity to the remaining term of the 2023 Notes or the 2043 Notes, as the case may be.
- "Comparable Treasury Price" means, with respect to any Redemption Date, (a) the average of the bid and asked prices for the Comparable Treasury Issue (expressed in each case as a percentage of its principal amount) on the third Business Day preceding that Redemption Date, as set forth in the daily statistical release designated H.15 (519) (or any successor release) published by the Federal Reserve Bank of New York and designated "Composite 3.30 p.m. Quotations for US Government Notes" or (b) if such release (or any successor release) is not published or does not contain such prices on such Business Day, (i) the average of the Reference Treasury Dealer Quotations for that Redemption Date, after excluding the highest (or, if there is more than one such highest quotation, only one of such quotations) and lowest (or, if there is more than one such lowest quotation, only one of such quotations) of such Reference Treasury Dealer Quotations or (ii) if the Independent Investment Banker for the Notes obtains fewer than four such Reference Treasury Dealer Quotations, the average of all such Quotations.
- "Independent Investment Banker" means one of the Reference Treasury Dealers appointed by the Company to act as the Independent Investment Banker.
- "Primary Treasury Dealer" means a primary US Government securities dealer in New York City.
- "Reference Treasury Dealer" means each of Barclays Capital Inc., Citigroup Global Markets Inc., Deutsche Bank Securities Inc. and J.P. Morgan Securities LLC and their respective successors and other nationally recognised investment banking firms that are Primary Treasury Dealers specified from time to time by the Company; provided, however, that if any of the foregoing shall cease to be a Primary Treasury Dealer and there would as a result be less than four Reference Treasury Dealers, the Company shall substitute therefor another nationally recognised investment banking firm that is a Primary Treasury Dealer.
- "Reference Treasury Dealer Quotation" means, with respect to each Reference Treasury Dealer and any Redemption Date, the average, as determined by the Independent Investment Banker, of the bid and asked prices for the Comparable Treasury Issue (expressed in each case as a percentage of its principal amount) quoted in writing to the Independent Investment Banker by such Reference Treasury Dealer at 3.30 p.m., New York City time, on the third Business Day preceding that Redemption Date.
- "Remaining Scheduled Payments" means, with respect to each Note to be redeemed, the remaining scheduled payments of the principal thereof and interest thereon that would be due after the related

Redemption Date but for such redemption (but excluding interest accrued and unpaid up to the date fixed for redemption); provided, however, that if that Redemption Date is not an Interest Payment Date with respect to such Notes, the amount of the next succeeding scheduled interest payment thereon will be reduced by the amount of interest accrued thereon to but excluding that Redemption Date.

- "Treasury Rate" means, with respect to any Redemption Date, the rate per annum equal to the semi-annual equivalent yield to maturity (computed as of the third Business Day immediately preceding that Redemption Date) of the Comparable Treasury Issue, assuming a price for the Comparable Treasury Issue (expressed as a percentage of its principal amount) equal to the Comparable Treasury Price for that Redemption Date.

Notice of any optional redemption will be given in accordance with the provisions set forth in "—Notice" below at least 30 days but not more than 60 days before the Redemption Date to each Holder of the Notes to be redeemed.

Change of Control Investor Put

If a Put Event occurs, the Holder of each applicable Note shall have the option (the "Put Option") to require the Company to redeem or, at the Company's option, purchase (or procure the purchase of) all of such Note on the Put Date (as defined below) at an amount equal to 101 per cent. of its principal amount (the "Optional Redemption Amount") together with accrued and unpaid interest to but excluding the date of redemption or purchase.

Within 30 days of the Company becoming aware that a Put Event has occurred, the Company shall, and at any time upon the Fiscal and Paying Agent becoming similarly so aware the Fiscal and Paying Agent may, and if so requested by the Holders of at least one-quarter in principal amount of a series of Notes then outstanding, shall (subject in each case to being indemnified to its satisfaction), give notice (a "Put Event Notice") to the Holders in accordance with "—Notices" below specifying the nature of the Put Event and the procedure for exercising the Put Option and offering to repurchase the applicable Notes on the date specified in the Put Event Notice, which date will be no less than 30 nor more than 60 days from the date the Put Event Notice is mailed (the "Put Date").

If 80 per cent. or more in principal amount of the applicable series of Notes outstanding as at the day immediately preceding the day on which the Put Event Notice was given have been redeemed pursuant to this "—Change of Control Investor Put", the Company may, on giving not less than 30 nor more than 60 days' notice to the Holders (such notice to be given within 30 days after the Put Date), redeem, at its option, all, but not some only, of the remaining applicable Notes at the Optional Redemption Amount plus interest accrued and unpaid to but excluding the date of such redemption.

The Fiscal and Paying Agent is under no obligation to ascertain whether a Put Event or Change of Control, or any event which could lead to the occurrence of, or could constitute, a Put Event or Change of Control, has occurred and, until it shall have actual knowledge or notice pursuant to the applicable Fiscal and Paying Agency Agreement to the contrary, the Fiscal and Paying Agent may assume that no Put Event or Change of Control or other such event has occurred.

The Company will comply with the requirements of Rule 14e-1 under the Exchange Act, and any other securities laws and regulations thereunder to the extent that those laws and regulations are applicable in connection with the repurchase of the Notes as a result of a Put Event. To the extent that the provisions of any such securities laws or regulations conflict with the Put Event provisions of the Notes, the Company will comply with those securities laws and regulations and will not be deemed to have breached the Company's obligations under the Put Event provisions of the Notes by virtue of any such conflict.

The Notes will not specifically prohibit the Company from entering into a merger, consolidation or similar combination with or into another party, or transferring all or substantially all of its assets to another party, whether or not the other party becomes liable for the Company's obligations under the Notes. Such a transaction may, however, constitute a Change of Control. See "—Covenants—Limitation on mergers, consolidations, amalgamations and combinations" below.

The Change of Control provisions above may deter certain mergers, tender offers and other attempts involving the Company by increasing the capital required to effectuate such transactions.

A "Put Event" will be deemed to occur if:

(a) any person (being an individual, partnership, company, corporation, unincorporated organisation, trust or joint venture, or any governmental agency or political subdivision thereof) or any persons acting in concert (as defined in the United Kingdom Takeover Code) or any person or persons acting on behalf of any such person(s) (the "Relevant Person") at any time directly or indirectly own(s) or acquire(s): (i) more than 50 per cent. of the issued or allotted ordinary share capital of the Company, or (ii) such number of shares in the capital of the Company carrying more than 50 per cent. of the total voting rights attached to the issued or allotted share capital of the Company that are normally exercisable at a general meeting of the Company (such event being a "Change of Control"), provided that a Change of Control shall be deemed not to have occurred if all or substantially all of the shareholders of the Relevant Person are, or immediately prior to the event which would otherwise have constituted a Change of Control were, the shareholders of the Company with the same (or substantially the same) pro rata interest in the share capital of the Relevant Person as such shareholders have or, as the case may be, had in the share capital of the Company; and

(b) on the date (the "Relevant Announcement Date") that is the earlier of: (x) the date of the first public announcement of the relevant Change of Control, and (y) the date of the earliest Relevant Potential Change of Control Announcement (if any), the Notes carry from any Rating Agency:

    (i) an investment grade credit rating (Baa3/BBB-, or equivalent, or better), and such rating from any Rating Agency is within the Change of Control Period either downgraded to a non-investment grade credit rating (Ba1/BB+, or equivalent, or worse) or withdrawn and is not within the Change of Control Period subsequently (in the case of a downgrade) upgraded or (in the case of a withdrawal) reinstated to an investment grade credit rating by such Rating Agency; or

    (ii) a non-investment grade credit rating (Ba1/BB+, or equivalent, or worse), and such rating from any Rating Agency is within the Change of Control Period downgraded by one or more notches (for illustration, Ba1/BB+ to Ba2/BB being one notch) or withdrawn and is not within the Change of Control Period subsequently (in the case of a downgrade) upgraded or (in the case of a withdrawal) reinstated to its earlier credit rating or better by such Rating Agency; or

    (iii) no credit rating, and no Rating Agency assigns within the Change of Control Period an investment grade credit rating to the Notes,

    provided that, if on the Relevant Announcement Date the Notes carry a credit rating from more than one Rating Agency, at least one of which is investment grade, then sub-paragraph (i) will apply; and

(c) in making the relevant decision(s) referred to above, the relevant Rating Agency announces publicly or confirms in writing to the Company or the Fiscal and Paying Agent that such decision(s) resulted, in whole or in part, from the occurrence of the Change of Control or the Relevant Potential Change of Control Announcement.

If the rating designations employed by a Rating Agency are changed from those which are described in paragraph (b) above, or if a rating is procured from a Substitute Rating Agency, the Company shall determine the rating designations of such Rating Agency or such Substitute Rating Agency (as appropriate) as are most equivalent to the prior rating designations of such Rating Agency and paragraph (b) above shall be read accordingly.

"Change of Control Period" means the period commencing on the Relevant Announcement Date and ending 90 days after the Change of Control (or such longer period for which the applicable series of Notes are under consideration (such consideration having been announced publicly within the period ending 90 days after the Change of Control) for rating review or, as the case may be, rating by a Rating Agency, such period not to exceed 60 days after the public announcement of such consideration).

"Rating Agency" means Moody's Investors Service Ltd or Standard & Poor's Credit Market Services Europe Limited or their respective successors or any rating agency (a "Substitute Rating Agency") substituted for any of them by the Company from time to time.

"Relevant Potential Change of Control Announcement" means any public announcement or statement by the Company, any actual or potential bidder or any adviser thereto relating to any potential Change of Control provided that within 180 days following the date of such announcement or statement a Change of Control occurs.

Form and Denomination

The Notes will be issued in fully registered form and only in denominations of $200,000 and integral multiples of $1,000 in excess thereof. Each series of Notes will be issued initially in the form of a global note.

Further Issues

The Company may, from time to time, without notice to or the consent of the Holders of the applicable series of Notes, reopen any series of the Notes and create and issue additional notes ("Additional Notes") having identical terms and conditions as the applicable series of Notes (or in all respects except for the issue date, issue price, payment of interest accruing prior to the issue date of such Additional Notes and/or the first payment of interest following the issue date of such Additional Notes) so that the Additional Notes are consolidated and form a single series of notes with the applicable series of the Notes, as the case may be.

The Company will not issue any Additional Notes having the same CUSIP, ISIN or other identifying number as the applicable outstanding Notes of any series unless such Additional Notes are fungible with the outstanding Notes of such series for US federal income tax purposes.

Status of the Notes

The Notes will be unsecured and unsubordinated obligations of the Company (except for the provisions of "—Covenants—Negative pledge" below) and will rank *pari passu* in right of payment among themselves and with all other unsecured and unsubordinated indebtedness of the Company (save for certain obligations required to be preferred by law).

Payment of Additional Amounts

The Company will make all payments of, or in respect of, principal, premium (if any) and interest on the Notes without withholding or deduction for or on account of any present or future taxes or duties of whatever nature imposed or levied by or on behalf of any Tax Jurisdiction ("Taxes"), unless such withholding or deduction is required by law.

If the Company is required to deduct or withhold any amount in respect of Taxes for the account of a Tax Jurisdiction the Company will pay to a Holder of a Note such additional amounts ("Additional Amounts") as may be necessary so that the net amount received by such Holder will not be less than the amount such Holder would have received if such Taxes had not been withheld or deducted; provided, however, that the Company shall not be required to pay any Additional Amounts for or on account of:

(a) any Taxes that would not have been so imposed, assessed, levied or collected but for the fact that the Holder or beneficial owner of the applicable Note is or has been a domiciliary, national or resident of, or engaging or having been engaged in a trade or business or maintaining or having maintained a permanent establishment or being or having been physically present in, the Tax Jurisdiction imposing the tax or otherwise having or having had some connection with such Tax Jurisdiction other than the mere holding or ownership of, or the collection of principal of, and premium (if any) or interest on, a Note;

(b) any Taxes that would not have been so imposed, assessed, levied or collected but for the fact that, where presentation is required in order to receive payment, the applicable Note was presented more than 30 days after the date on which such payment became due and payable or was provided for, whichever is later, except to the extent that the holder would have been entitled to Additional Amounts had the applicable Note been presented for payment on any day during such 30-day period;

(c) any estate, inheritance, gift, sales, transfer, personal property or similar Taxes;

(d) any Taxes that are payable otherwise than by deduction or withholding from payments on or in respect of the applicable Note;

(e) any Taxes that would not have been so imposed, assessed, levied or collected but for the failure by the holder or the beneficial owner of the applicable Note to comply with a reasonable written request to the holders (i) to provide any certification, identification, information, documents or other evidence concerning the nationality, residence or identity of the holder or the beneficial owner or its connection with the Tax Jurisdiction or (ii) to make any valid or timely declaration or claim or satisfy any other reporting, information or procedural requirements relating to such matters if, in either case, compliance is required by statute, regulation or administrative practice of the Tax Jurisdiction as a condition to relief or exemption from such Taxes;

(f) any withholding or deduction that is required to be made pursuant to Council Directive 2003/48/EC or any other Directive implementing the conclusion of the EU Economic and Financial affairs council meeting of 26-27 November 2000 on the taxation of savings income or any law implementing or complying with, or introduced in order to conform to, such Directive;

(g) any withholding or deduction that is imposed on the applicable Note that is presented for payment, where presentation is required, by or on behalf of a holder who would have been able to avoid such withholding or deduction by presenting such Note to another paying agent in a member state of the EU; or

(h) any combination of the Taxes described in paragraphs (a) to (g) above.

In addition, Additional Amounts will not be paid in respect of any payment in respect of the applicable series of Notes to any holder of the applicable Notes that is a fiduciary, a partnership, a limited liability company or any person other than the sole beneficial owner of such Notes to the extent such payment would be required by the laws of a Tax Jurisdiction to be included in the income for tax purposes of a beneficiary or settlor with respect to such fiduciary, a member of such partnership, an interestholder in such limited liability company or a beneficial owner that would not have been entitled to such amounts had such beneficiary, settlor, member, interestholder or beneficial owner been the holder of such Notes.

Upon request, the Company shall furnish to the registered Holder, within 60 days after the date the payment of any Taxes deducted or withheld is due pursuant to applicable law, either certified copies of tax receipts evidencing such payment or, if such receipts are not obtainable, other evidence of such payments.

Unless otherwise stated, references in any context to the payment of principal of, and any premium or interest on, any Note, will be deemed to include payment of Additional Amounts to the extent that, in such context, Additional Amounts are, were or would be payable in respect thereof.

"Relevant Taxing Jurisdiction" means the United Kingdom (or any jurisdiction in which a successor entity is organised or tax resident) or any political subdivision or any authority thereof or therein having power to tax.

"Tax Jurisdiction" means a Relevant Taxing Jurisdiction or any other jurisdiction through which payments on the Notes are made by or on behalf of the Company.

Redemption for Tax Reasons

Each series of Notes is redeemable by the Company, in whole but not in part, upon not less than 30 nor more than 60 days' notice as provided for herein, at 100 per cent. of the principal amount of such Notes plus accrued and unpaid interest if any to but excluding the applicable Redemption Date at the Company's option at any time prior to their maturity if due to a Change in Tax Law (as defined below) (a) the Company in accordance with the terms of the applicable series of Notes has, or would, become obliged to pay any Additional Amounts to the Holders of the Notes of that series; and (b) such obligation cannot be avoided by the Company taking reasonable measures available to it, provided, that no such notice of redemption shall be given earlier than 90 days prior to the earliest date on which the Company would be obliged to pay any such Additional Amounts were a payment in respect of the applicable series of Notes then due. Prior to the giving of any such notice of redemption, the Company must deliver to the Fiscal and Paying Agent (A) a certificate signed by two directors of the Company stating that the Company is entitled to effect such redemption and setting forth a statement of facts showing that the conditions precedent to the right of the Company so to redeem have occurred and (B) an opinion of independent counsel of recognised standing with respect to tax matters of the Relevant Taxing Jurisdiction to the effect that the Company has, or would, become obliged to pay such Additional Amounts as a result of such Change in Tax Law.

For the purposes hereof, "Change in Tax Law" shall mean (a) any changes in, or amendment to, any law of a Relevant Taxing Jurisdiction (including any regulations or rulings promulgated thereunder but not including, for this purpose, any treaty entered into by the Relevant Taxing Jurisdiction) or any amendment to or change in the application or official interpretation (including judicial or administrative interpretation) of such law, which change or amendment becomes effective, or, in the case of an official interpretation, is announced, on or after the Issue Date of the Notes or (b) if the Company consolidates, merges, amalgamates or combines with, or transfers or leases its assets substantially as an entirety to, any person that is incorporated or tax resident under the laws of any jurisdiction other than a Relevant Taxing Jurisdiction as of the date of such transaction and as a consequence thereof such person becomes the successor obligor to the Company in respect of Additional Amounts that may become payable (in which case, for purposes of this redemption provision, all references to the Company shall be deemed to be and include references to such person), any change in, or amendment to, any law of the jurisdiction of incorporation or tax residence of such person or any successor entity, or any political subdivision or taxing authority thereof or therein for purposes of taxation (including any regulations or rulings promulgated thereunder but not including, for this purpose, any treaty entered into by the Relevant Taxing Jurisdiction), or any amendment to or change in the application or official interpretation (including judicial or administrative interpretation) of such law, which change or amendment becomes effective, or, in the case of an official interpretation, is announced, on or after the date of such consolidation, merger, amalgamation, combination or other transaction.

Redemption—General

Upon presentation of any Note redeemed in part only, the Company will execute and the Fiscal and Paying Agent will authenticate and deliver (or cause to be transferred by book-entry) to or on the order of the Holder thereof, at the expense of the Company, a new Note or Notes, of authorised denominations, in principal amount equal to the unredeemed portion of the Note so presented.

On or before any Redemption Date, the Company shall deposit with the Fiscal and Paying Agent money sufficient to redeem on the Redemption Date all the Notes so called for redemption at the appropriate redemption price, together with accrued interest to but excluding the date fixed for redemption (other than Notes or portions thereof called for redemption on that date which have been delivered by the Company to the Fiscal and Paying Agent for cancellation). If less than all the Notes are to be redeemed, the Fiscal and Paying Agent will select Notes for redemption *pro rata*, by lot, or by such other method as the Fiscal and Paying Agent in its sole discretion shall deem fair and appropriate and is consistent with the rules of DTC and/or Euroclear and/or Clearstream, Luxembourg.

On and after any Redemption Date, to the extent the Company has deposited sufficient moneys with the Fiscal and Paying Agent as provided in the preceding paragraph, interest will cease to accrue on the Notes or any portion thereof called for redemption.

Maturity

Unless previously purchased or redeemed and cancelled by the Company or any of its Subsidiaries, the principal amount of the 2023 Notes will mature and become due and payable on 16 October 2023 and the principal amount of the 2043 Notes will mature and become due and payable on 16 October 2043, each in an amount equal to their principal amount, with accrued and unpaid interest to but excluding such date.

Reacquisition

There is no restriction on the ability of the Company or any of its Subsidiaries to purchase or repurchase Notes, provided that any Notes so purchased or repurchased shall be cancelled and not reissued.

Covenants

Negative pledge

So long as any of the applicable series of Notes remains outstanding, the Company will ensure that no Relevant Indebtedness of the Company or any of its Principal Subsidiaries will be secured by any Security Interest upon, or with respect to, any of the present or future business, undertaking, assets or revenues (including any uncalled capital) of the Company or any of its Principal Subsidiaries unless the Company shall, in the case of the creation of the Security Interest, before or at the same time and, in any other case, promptly, take any and all action necessary to ensure that:

(a) all amounts payable by it under the Notes are secured by the Security Interest equally and rateably with the Relevant Indebtedness; or

(b) such other Security Interest or other arrangement (whether or not it includes the giving of a Security Interest) is provided either (i) not materially less beneficial to the interests of the Holders or (ii) as shall be approved by the holders of not less than 75 per cent. in aggregate principal amount of the applicable series of Notes at the time outstanding.

Limitation on mergers, consolidations, amalgamations and combinations

So long as any of the Notes remain outstanding, the Company may not consolidate with or merge into any other person or sell, convey, transfer or lease its properties and assets as an entirety or substantially as an entirety to any person (other than any sale or conveyance by way of a lease in the ordinary course of business), unless (i) any successor person assumes the Company's obligations on the applicable Notes and under the applicable Fiscal and Paying Agency Agreement; (ii) immediately after giving effect to such transaction, no Event of Default, and no event which, after notice or lapse of time or both, would become an Event of Default, shall have occurred and be continuing; (iii) such successor person agrees to pay any Additional Amounts imposed by the jurisdiction in which such successor person is incorporated or otherwise a resident for tax purposes or through which payments are made and resulting therefrom or otherwise; and (iv) if as a result of such consolidation or merger or such sale, conveyance, transfer or lease, properties or assets of the Company would become subject to a mortgage, pledge, security interest, lien or similar encumbrance to secure payment of any indebtedness for borrowed money (as defined below) of the Company which would not be permitted by the applicable Notes or under the applicable Fiscal and Paying Agency Agreement, the Company or such successor person, as the case may be, shall take such steps as shall be necessary to effectively secure the Notes equally and rateably with (or prior to) all indebtedness for borrowed money secured thereby.

The limitation on mergers, consolidations, amalgamations and combinations contained in this section shall not apply to any consolidation, merger, amalgamation or combination in which the Company is the surviving corporation except that, in such case, the provisions of clauses (ii) and (iv) above shall apply such that: (x) immediately after giving effect to such transaction, no Event of Default, and no event which, after notice or lapse of time or both, would become an Event of Default, shall have occurred and be continuing; and (y) if as a result of such consolidation or merger or such sale, conveyance, transfer or lease, properties or assets of the Company would become subject to a mortgage, pledge, security interest, lien or similar encumbrance to secure payment of any indebtedness for borrowed money of the Company which would not be permitted by the applicable Notes or under the applicable Fiscal and Paying Agency Agreement, the Company shall take such steps as shall be necessary to effectively secure the Notes equally and ratably with (or prior to) all indebtedness for borrowed money secured thereby.

The Fiscal and Paying Agency Agreements will not contain covenants or other provisions to afford protection to Holders of the Notes in the event of a highly leveraged transaction or a change in control of the Company except as provided above.

Upon certain mergers or consolidations involving the Company, or upon certain sales or conveyances of the properties of the Company, the obligations of the Company under the applicable Notes shall be assumed by the person formed by such merger or consolidation or which shall have acquired such property and upon such assumptions such person shall succeed to and be substituted for the Company and then the Company will be relieved from all obligations under the Notes. The term "Company", as used in the Notes and the Fiscal and Paying Agency Agreements, also refers to any such successors or assigns so substituted.

Certain Definitions

Set forth below is a summary of certain of the defined terms used in the Notes and the applicable Fiscal and Paying Agency Agreement. You should refer to the Notes and the applicable Fiscal and Paying Agency Agreement for the full definition of all defined terms as well as any other terms used herein for which no definition is provided.

"borrowed money" means (a) moneys borrowed and any fixed or minimum premiums and accrued interest in respect thereof, (b) liabilities under or in respect of any acceptance or acceptance credit and (c) the principal and such premium as aforesaid (if any) and accrued interest in respect of any notes, bonds, debentures, loan stock or other securities whether issued in whole or in part for cash or other consideration.

"Business Day" means each day which is not, in London or New York or any other Place of Payment, a Saturday, Sunday or legal holiday or a day on which banking institutions are authorised or obliged by law or regulation to close.

"Excluded Subsidiary" at any time means a Subsidiary of the Company:

(a) (i) which is either (x) a special purpose company whose principal assets are constituted by a project or projects or (y) is incorporated and conducts its business primarily outside the United Kingdom; and

(ii) none of whose indebtedness is directly or indirectly the subject of security or a guarantee, indemnity or any other form of assurance, undertaking or support from the Company or any of its Principal Subsidiaries or, where such security, guarantee or indemnity or other form of assurance, undertaking or support is provided, the liability of the Company and its Principal Subsidiaries thereunder is contractually limited to and cannot in any circumstances exceed at any time an amount equal to £50,000,000 or its equivalent in any other currency or currencies; and

(iii) which has been designated as such by the Company by written notice to the Fiscal and Paying Agent;

provided that the Company may give written notice to the Fiscal and Paying Agent at any time that any Excluded Subsidiary is no longer an Excluded Subsidiary, whereupon it shall cease to be an Excluded Subsidiary; or

(b) which has a banking licence or its equivalent in any jurisdiction.

"person" means any individual, corporation, partnership, joint venture, association, limited liability company, joint stock company, trust, unincorporated organisation or government or any agency or political subdivision thereof.

"Places of Payment" means in London, England an office or agency (a) where the Notes may be presented for payment, (b) where the Notes may be presented for registration of transfer and for exchange as provided in the applicable Fiscal and Paying Agency Agreement and (c) where notices and demands to or upon the Company in respect of the Notes or the applicable Fiscal and Paying Agency Agreement may be served.

"Principal Subsidiary" means a Subsidiary of the Company (not being an Excluded Subsidiary):

(a) (i) whose total assets represent not less than 20 per cent. of the consolidated total assets of the Company and its Subsidiaries taken as a whole; or

(ii) whose external turnover is more than 20 per cent. of the consolidated turnover of the Company and its Subsidiaries,

all as calculated by reference to the then latest audited consolidated accounts of the Company and the then latest audited accounts of its Subsidiaries; or

(b) to which is transferred all or substantially all of the business, undertaking or assets of a Subsidiary which immediately prior to such transfer is a Principal Subsidiary whereupon the transferor Subsidiary shall immediately cease to be a Principal Subsidiary and the transferee Subsidiary shall immediately become a Principal Subsidiary but shall cease to be a Principal Subsidiary under this -paragraph (b) (but without prejudice to the provisions of paragraph (a) above) upon publication of its next audited accounts.

A report by two directors of the Company that in their opinion a Subsidiary of the Company is or was or was not at any particular time or throughout any specified period a Principal Subsidiary shall, in the absence of manifest error, be conclusive and binding on all parties.

"Relevant Indebtedness" means:

(a) any indebtedness for or in respect of any notes, bonds or other debt securities having an original maturity of more than one year which (with the consent of the issuer of the indebtedness) are for the time being listed or traded on a stock exchange or other recognised securities market, other than any notes, bonds or other debt securities issued by an acquired Subsidiary prior to the date of the acquisition and not issued in contemplation of such acquisition; and

(b) any guarantee or indemnity in respect of any such indebtedness.

"Security Interest" means any mortgage, charge, lien, pledge or other security interest, but shall not include any security interest over cash created or arising solely or principally in connection with, and for the purpose of, a defeasance arrangement.

"Subsidiary" means a subsidiary within the meaning of Section 1159 of the Companies Act 2006.

Events of Default

The following will be Events of Default (each an "Event of Default") with respect to the applicable series of Notes:

(a) default is made (i) for more than 14 days in the payment on the due date of interest or Additional Amounts in respect of the Notes as and when the same shall become due and payable, or (ii) for more than three days in the payment on the due date of all or any part of the principal or premium, if any, of any Note as and when the same shall become due and payable either at maturity, upon any redemption, by declaration or otherwise; or

(b) there is a failure in the performance of any obligation under the applicable Notes or the applicable Fiscal and Paying Agency Agreement (other than an obligation to make payment of any principal or interest thereunder) which continues for the period of 30 days after written notification requiring such failure to be remedied has been given to the Company by the Fiscal and Paying Agent; or

(c) (except for the purpose of a reconstruction, an amalgamation or, in the case of a Principal Subsidiary, a voluntary winding-up) an order is made (and not discharged or stayed within a period of 30 days) or an effective resolution is passed for the winding-up of the Company or any of its Principal Subsidiaries or an administration order is made in relation to the Company or any of its Principal Subsidiaries; or

(d) an administrative or other receiver is appointed of the whole or substantially the whole of the assets of the Company or any of its Principal Subsidiaries and is not removed, paid out or discharged within 30 days or, following such 30-day period, the appointment is not being disputed in good faith; or

(e) the Company or any of its Principal Subsidiaries makes a general assignment for the benefit of its creditors; or

(f) (i) any loan or other indebtedness for borrowed money (as defined in the applicable Fiscal and Paying Agency Agreement) of the Company or any of its Principal Subsidiaries, amounting in aggregate to not less than £40,000,000 or its equivalent in other currencies, becomes due and repayable prematurely by reason of an event of default (however described) or is not repaid on its final maturity date (as extended by any applicable grace period); or

(ii) any security given by the Company or any of its Principal Subsidiaries for any loan or indebtedness for borrowed money amounting in aggregate to not less than £40,000,000 or its equivalent in other currencies becomes enforceable and steps are taken to enforce the same; or

(iii) default is made by the Company or any of its Principal Subsidiaries in making any payment due under any guarantee or indemnity given by it in respect of any loan or indebtedness for borrowed money amounting in aggregate to not less than £40,000,000 or its equivalent in other currencies.

Each Fiscal and Paying Agency Agreement will provide that if an Event of Default occurs and is continuing, then and in each and every such case (other than certain Events of Default specified in paragraph (c) above with respect to the winding-up or dissolution of the Company), unless the principal of all the applicable Notes shall have already become due and payable, the Holders of not less than 25 per cent. in aggregate principal amount of the applicable series of Notes then outstanding, by notice in writing to the Company and the Fiscal and Paying Agent, may declare the entire principal amount of all applicable Notes issued pursuant to the applicable Fiscal and Paying Agency Agreement and interest accrued and unpaid thereon, if any, to be due and payable immediately, and upon any such declaration the same shall become immediately due and payable, without any further declaration or other act on the part of any Holder. If certain Events of Default described in paragraph (c) above occur with respect to the winding-up or dissolution of the Company and are continuing, the principal amount of and accrued and unpaid interest on all applicable Notes issued pursuant to the applicable Fiscal and Paying Agency Agreement shall become immediately due and payable, without any declaration or other act on the part of the Fiscal and Paying Agent or any Holder. Under certain circumstances, the Holders of a majority in aggregate principal amount of the applicable Notes then outstanding, by written notice to the Company and the Fiscal and Paying Agent, may waive defaults and rescind and annul declarations of acceleration and its consequences, but no such waiver or rescission and annulment shall extend to or shall affect any subsequent default or shall impair any right consequent thereon.

The Holders of a majority in aggregate principal amount of the applicable Notes of such series then outstanding will have the right to direct the time, method and place of conducting any proceeding for any remedy available to the Fiscal and Paying Agent, or exercising any trust or power conferred on the Fiscal and Paying Agent, subject to certain limitations to be specified in the applicable Fiscal and Paying Agency Agreement.

An Event of Default with respect to the 2023 Notes or the 2043 Notes would not necessarily constitute an event of default with respect to the other series of Notes.

Each Fiscal and Paying Agency Agreement will also provide that no Holder of any Notes may institute any action or proceeding at law or in equity or in bankruptcy or otherwise upon or under or with respect to the applicable Fiscal and Paying Agency Agreement, or for the appointment of a trustee, receiver, liquidator, custodian or other similar official or for any other remedy under the applicable Fiscal and Paying Agency Agreement (except suits for the enforcement of payment of overdue principal or interest), unless the Holders of not less than 25 per cent. in aggregate principal amount of the applicable series of Notes then outstanding shall have collectively instituted such action or proceeding and shall have provided notice in writing of the institution of such action or proceeding to the Company and the Fiscal and Paying Agent.

Each Fiscal and Paying Agency Agreement will also provide that the Company will furnish to the Fiscal and Paying Agent, within 30 days of a written request of the Fiscal and Paying Agent, a certificate from an officer of the Company as to his or her best knowledge of the Company's compliance with all conditions and covenants under the applicable Fiscal and Paying Agency Agreement (or if non-compliance has occurred, giving details of it), which certificate may merely state that such officer has no knowledge of any such non-compliance.

Defeasance

The Fiscal and Paying Agency Agreement will provide that the Company will have the option either (a) to be deemed to have paid and discharged the entire indebtedness represented by, and obligations under, the applicable series of Notes and to have satisfied all the obligations under the Fiscal and Paying Agency Agreement (except for certain obligations, including those relating to the defeasance trust and obligations to register the transfer or exchange of Notes, to pay Additional Amounts, to replace mutilated, destroyed, lost or stolen Notes and to maintain paying agencies) on the 91st day after the applicable conditions described below have been satisfied or (b) to cease to be under any obligation to comply with the covenants described above under "—Covenants—Negative pledge" and the condition relating to the absence of any events of default under "—Covenants—Limitation on mergers, consolidations, amalgamations and combinations" under the Notes, and non-compliance with such covenants and the occurrence of certain events described above under "—Events of Default" any such sections or provisions will not give rise to any Event of Default under the Notes, at any time after the applicable conditions described below have been satisfied.

In order to exercise either defeasance option, the Company must deposit with the Fiscal and Paying Agent or with the Fiscal and Paying Agent's agent as the Fiscal and Paying Agent directs, irrevocably in trust, money, Government Obligations (as defined in the applicable Fiscal and Paying Agency Agreement) or for the payment of principal of, premium, if any, and interest on the applicable outstanding Notes on the dates such instalments of interest or principal are due or to and including the Redemption Date irrevocably designated by the Company on or prior to the date of deposit of such money or Government Obligations, and must (i) comply with certain other conditions as stated in the applicable Fiscal and Paying Agency Agreement, including delivering to the Fiscal and Paying Agent an opinion of United States counsel of recognised standing with respect to U.S. federal income tax matters, or a ruling received from the United States Internal Revenue Service, to the effect that beneficial owners of the applicable series of Notes will not recognise income, gain or loss for U.S. federal income tax purposes as a result of such defeasance and will be subject to U.S. federal income tax on the same amount and in the same manner and at the same time as would have been the case if such defeasance had not occurred and, in the case of (a) above, such opinion must state that it is based on a change of law after the Issue Date of the Notes and (ii) pay in full all other amounts due and owing under the applicable Fiscal and Paying Agency Agreement.

Modification and Waiver

Without consent of noteholders

Each Fiscal and Paying Agency Agreement will contain provisions permitting the Company and the Fiscal and Paying Agent, without notice to or the consent of the Holders of any of the applicable Notes of the relevant series at any time outstanding, from time to time and at any time, to enter into a fiscal and paying agency agreement or paying agency agreements supplemental thereto:

- to convey, transfer, assign, mortgage or pledge to the Holders of the applicable Notes or any person acting on their behalf as security for the applicable Notes any property or assets;
- to evidence the succession of another person to the Company, or successive successions, and the assumption by such person(s) of the covenants, agreements and obligations of the Company pursuant to the applicable Fiscal and Paying Agency Agreement;
- to evidence and provide for the acceptance of appointment of a successor or successors to the Fiscal and Paying Agent and/or the Paying Agent, Transfer Agent or Registrar, as applicable;
- to add to the covenants of the Company, such further covenants, restrictions, conditions or provisions as the Company and the Fiscal and Paying Agent shall consider to be for the protection of the Holders of the applicable Notes, and to make the occurrence, or the occurrence and continuance, of a default in any such additional covenants, restrictions, conditions or provisions an Event of Default under the applicable Notes permitting the enforcement of all or any of the several remedies provided in the applicable Fiscal and Paying Agency Agreement; provided that, in respect of any such additional covenant, restriction, condition or provision, such supplemental fiscal and paying agency agreement may provide for a particular period of grace after default (which may be shorter or longer than that allowed in the case of other defaults) or may limit the remedies available to the Fiscal and Paying Agent upon such an Event of Default or may limit the right of Holders of a majority in aggregate principal amount of the applicable Notes to waive such an Event of Default;
- to modify the restrictions on, and procedures for, resale and other transfers of the applicable Notes pursuant to law, regulation or practice relating to the resale or transfer of restricted securities generally;
- to cure any ambiguity or to correct or supplement any provision contained in the applicable Fiscal and Paying Agency Agreement which may be defective or inconsistent with any other provision contained therein or in any supplemental fiscal and paying agency agreement or to make such other provisions in regard to matters or questions arising under the applicable Fiscal and Paying Agency Agreement or under any supplemental fiscal and paying agency agreement as the Company or the Fiscal and Paying Agent may deem necessary or desirable and which will not adversely affect the interests of the Holders of the applicable Notes in any material respect; and
- to reopen the applicable series of Notes and create and issue Additional Notes having identical terms and conditions as the applicable Notes (or in all respects except for the issue date, issue price, payment of interest accruing prior to the issue date of such additional notes and/or the first payment of interest following the issue date of such additional notes) so that the Additional Notes are consolidated and form a single series with the outstanding applicable Notes.

With consent of noteholders

Each Fiscal and Paying Agency Agreement will contain provisions permitting the Company and the Fiscal and Paying Agent, with the consent of the Holders of not less than a majority in aggregate principal amount of the applicable Notes of the relevant series at the time outstanding (including consents obtained in connection with a tender offer or exchange offer for the applicable Notes), from time to time and at any time, to enter into a fiscal and paying agency agreement or fiscal and paying agency agreements supplemental thereto for the purpose of adding any provisions to or changing in any manner or eliminating any of the provisions of the applicable Notes or of modifying in any manner the rights of the Holders of the applicable Notes, provided that no such fiscal and paying agency agreement may, without the consent of the Holder of each of the Notes so affected:

- change the stated maturity of, or the date for payment of any principal of, or instalment of interest on, any applicable Note; or

- reduce the principal amount of or the rate or amount of interest on any applicable Note or Additional Amounts payable with respect thereto or reduce the amount payable thereon in the event of redemption or default; or
- change the currency of payment of principal of or interest on any applicable Note or Additional Amounts payable with respect thereto; or
- change the obligation of the Company to pay Additional Amounts (except as otherwise permitted by such applicable Note); or
- impair the right to institute suit for the enforcement of any such payment on or with respect to any applicable Note; or
- reduce the percentage of the aggregate principal amount of any applicable Notes outstanding, the consent of whose Holders is required for any such supplemental fiscal and paying agency agreement; or
- reduce the aggregate principal amount of any applicable Note outstanding necessary to modify or amend the applicable Fiscal and Paying Agency Agreement or any such Note or to waive any future compliance or past default or reduce the quorum requirements or the percentage of aggregate principal amount of any applicable Notes outstanding required for the adoption of any action at any meeting of Holders of such Notes or to reduce the percentage of the aggregate principal amount of such Notes outstanding necessary to rescind or annul any declaration of the principal of all accrued and unpaid interest on any Note to be due and payable,

provided that no consent of any Holder of any applicable Note shall be necessary to permit the Fiscal and Paying Agent and the Company to execute supplemental fiscal and paying agency agreements as described under "—Without consent of noteholders" above.

Any modifications, amendments or waivers to a Fiscal and Paying Agency Agreement or to the conditions of the applicable series of Notes will be conclusive and binding on all Holders of the applicable Notes, whether or not they have consented to such action or were present at the meeting at which such action was taken, and on all future Holders of the applicable Notes, whether or not notation of such modifications, amendments or waivers is made upon such Notes. Any instrument given by or on behalf of any Holder of such a Note in connection with any consent to any such modification, amendment or waiver will be irrevocable once given and will be conclusive and binding on all subsequent registered Holders of such Note.

Restrictions on Transfer

The Initial Purchasers propose to resell the Rule 144A Notes to certain qualified institutional buyers in the United States in reliance upon Rule 144A under the Securities Act. The Rule 144A Notes may not be sold or otherwise transferred except, in the United States, pursuant to registration under the Securities Act or in accordance with Rule 144A or, outside the United States, pursuant to Rule 904 of Regulation S thereunder or, in either case, in a resale transaction that is otherwise exempt from such registration requirements, and each global note representing Rule 144A Notes will bear a legend to this effect. In light of current US securities laws, subject to certain exceptions, an exemption should be available for a sale or transfer of a Rule 144A Note after its Specified Date. The "Specified Date" means (A) with respect to any Rule 144A Note, the date following the expiration of the applicable required holding period determined pursuant to Rule 144 of the Securities Act (such period, the "applicable holding period") from the later of (i) the date of acquisition of such Rule 144A Note from the Company or an affiliate of the Company and (ii) any resale of such Rule 144A Note in reliance on Rule 144 under the Securities Act for the account of either the acquiror or any subsequent holder of such Rule 144A Note, in each case demonstrated to the reasonable satisfaction of the Company (which may require delivery of legal opinions); or (B) with respect to any Regulation S Note, the date which is 40 days after the later of the commencement of the offering or the closing date (such period, the "distribution compliance period").

Unless a holder of a Rule 144A Note holds such Rule 144A Note for the entire applicable holding period, such holder may not be able to determine the Specified Date because such holder may not be able to determine the last date on which the Company or any affiliate thereof was the beneficial owner of such holder's Rule 144A Note. The Fiscal and Paying Agent will not be required to accept for registration or transfer any Rule 144A Notes, except upon presentation of satisfactory evidence (which may include legal opinions) that the restrictions on transfer have been complied with, all in accordance with such reasonable regulations as the Company may from time to time agree with such Fiscal and Paying Agent.

Prescription

Under New York's statute of limitations, any legal action upon the Notes in respect of interest or principal must be commenced within six years after the payment thereof is due. Thereafter any such legal action on the Notes will become generally unenforceable.

Notice

Notices to holders of Notes will be deemed to be validly given if sent by first-class mail postage prepaid to the last addresses of such holders as they appear in the Notes register. Such notices will be deemed to have been given on the date following such mailing.

So long as any global notes representing the applicable series of Notes are held in their entirety on behalf of a clearing system, or any of its participants, there may be substituted for the mailing described above the delivery of the relevant notices to the clearing system, and its participants, for communication by them to the entitled accountholders. Any such notice shall be deemed to have been given to the accountholders on the third day after the day on which the said notice was given to the clearing system and its participants.

Listing

Application has been made to list the Notes on the Official List of the United Kingdom Listing Authority and for the admission of the Notes to trading on the Regulated Market of the London Stock Exchange. The Company will agree in each Fiscal and Paying Agency Agreement to use its reasonable endeavours to maintain such listing and admission to trading of the relevant series of Notes for so long as any of the Notes of the relevant series remain outstanding. If it is unable to do so, the Company will agree in each Fiscal and Paying Agency Agreement to use all reasonable endeavours to obtain and maintain a quotation or listing of the relevant series of Notes on such other stock exchange or exchanges or securities market or markets as the Company may decide.

Consent to Service

The Company will initially designate CT Corporation Systems as its authorised agent for service of process in any legal suit, action or proceeding arising out of or relating to the performance of its obligations under the applicable Fiscal and Paying Agency Agreement and the Notes brought in any state or federal court in the Borough of Manhattan, the City of New York, and will irrevocably submit (but for those purposes only) to the non-exclusive jurisdiction of any such court in any such suit, action or proceeding.

Governing Law

The Notes and each Fiscal and Paying Agency Agreement shall be governed by and construed in accordance with the laws of the State of New York, without regard to principles of conflicts of laws thereof.

Regarding the Fiscal and Paying Agent

In acting under the Fiscal and Paying Agency Agreements and in connection with the Notes, the Fiscal and Paying Agent is acting solely as agent of the Company and does not assume any obligation towards or relationship of agency or trust for or with the owners or holders of the Notes, except that any funds held by the Fiscal and Paying Agent for payment of principal of or interest on the Notes or Additional Amounts with respect thereto shall be applied as set forth in the Notes, but need not be segregated from other funds held by it except as required by law. For a description of the duties and immunities and rights of the Fiscal and Paying Agent under the Fiscal and Paying Agency Agreements, reference is made to the Fiscal and Paying Agency Agreements, and the obligations of the Fiscal and Paying Agent are subject to such immunities and rights.

BOOK-ENTRY, DELIVERY AND FORM

The Notes that are initially offered and sold in the United States to QIBs (the "Rule 144A Notes") will be represented by beneficial interests in one or more Rule 144A global notes in registered form without interest coupons, which will be deposited on or about the closing date of the Offering of the Notes (the "Closing Date") with Citibank N.A., London Branch as custodian (the "Custodian") for DTC and registered in the name of Cede & Co. as nominee of DTC.

The Notes that are offered and sold in reliance on Regulation S (the "Regulation S Notes") will be represented by beneficial interests in one or more Regulation S global notes in registered form without interest coupons, which will be deposited on or about the Closing Date with the Custodian, and registered in the name of Cede & Co., as nominee of DTC. Investors may hold their interests in the global notes directly through DTC if they are participants in, or indirectly through organisations that are participants in, such systems. Euroclear and Clearstream, Luxembourg will hold interests in the Rule 144A Notes or Regulation S Notes on behalf of their participants through customers' securities accounts in their respective names on the books of their respective depositaries, which are participants in DTC.

So long as DTC or its nominee is the registered holder of a global note, DTC or such nominee, as the case may be, will be considered the sole owner or holder of the applicable Notes represented by the applicable global note for all purposes under the Fiscal and Paying Agency Agreements and the applicable Notes (except as the context otherwise requires in respect of Additional Amounts). The Notes (including beneficial interests in the global notes) will be subject to certain restrictions on transfer set forth therein and in the Fiscal and Paying Agency Agreements and will bear a legend regarding such restrictions as set forth under "Transfer Restrictions". Under certain circumstances, transfers may be made only upon receipt by the Fiscal and Paying Agent, in its capacity as transfer agent, as well as the Fiscal and Paying Agent and the Company, of a written certification (in the form set out in the Fiscal and Paying Agency Agreements).

Transfers within Global Notes

Subject to the procedures and limitations described herein, transfers of beneficial interests within a global note may be made without delivery to the Company or the Fiscal and Paying Agent of any written certifications or other documentation by the transferor or transferee.

Transfers between Global Notes

A beneficial interest in a Rule 144A Note may be transferred to a person who wishes to take delivery of such beneficial interest through the applicable Regulation S Note only upon receipt by the Fiscal and Paying Agent of a written certification (in the form set out in the Fiscal and Paying Agency Agreements) from the transferor to the effect that such transfer is being made in accordance with Rule 903 or 904 of Regulation S or, in the case of an exchange occurring following the Specified Date, Rule 144. A beneficial interest in a Regulation S Note may be transferred to a person who wishes to take delivery of such beneficial interest through the applicable Rule 144A Note only upon receipt by the Fiscal and Paying Agent of a written certification (in the form set out in the Fiscal and Paying Agency Agreements) from the transferor to the effect that such transfer is being made to a person whom the transferor reasonably believes is a QIB within the meaning of Rule 144A, in a transaction meeting the requirements of Rule 144A and in accordance with any applicable securities laws of any state of the United States and any other jurisdiction. Any beneficial interest in a Rule 144A Note or a Regulation S Note that is transferred to a person who takes delivery in the form of a beneficial interest in the other global note will, upon transfer, cease to be a beneficial interest in such global note and become a beneficial interest in the other global note and, accordingly, will thereafter be subject to all transfer restrictions and other procedures applicable to a beneficial interest in such other global note for so long as such person retains such an interest.

Transfers or Exchanges from Global Notes to Definitive Notes

No global note representing a Rule 144A Note or Regulation S Note may be exchanged in whole or in part for Notes in definitive registered form ("Definitive Notes" and each a "Definitive Note") unless:

- DTC notifies the Company that it is unwilling or unable to hold the applicable global note or DTC ceases to be a clearing agency registered under the Exchange Act, and in each case the Company does not appoint a successor depositary that is registered under the Exchange Act within 90 days; or
- a payment default has occurred and is continuing; or

- in the event of a bankruptcy default, the Company fails to make payment on the applicable Notes when due; or
- the Company shall have determined in its sole discretion that the Notes shall no longer be represented by the applicable global notes.

The holder of a Definitive Note may transfer such note by surrendering it at the specified office of the Fiscal and Paying Agent. Upon the transfer, exchange or replacement of a Rule 144A Definitive Note bearing the applicable legend set forth under "Transfer Restrictions" herein, or upon specific request for removal of such legend on a Definitive Note, the Company will deliver only Definitive Notes that bear such legend, or will refuse to remove such legend, as the case may be, unless there is delivered to the Company and the Fiscal and Paying Agent such satisfactory evidence, which may include an opinion of counsel, as may reasonably be required by the Company and the Fiscal and Paying Agent, respectively, that neither the legend nor the restrictions on transfer set forth therein are required to ensure compliance with the provisions of the Securities Act.

Each such Definitive Note will include terms substantially in the form of those set forth in the Fiscal and Paying Agency Agreements. Except as set forth herein, no global note may be exchanged in whole or in part for Definitive Notes.

Clearing and Settlement

The information set out below in connection with DTC is subject to any change in or reinterpretation of the rules, regulations and procedures of DTC currently in effect. The information about DTC set forth below has been obtained from sources that the Company believes to be reliable, including DTC, but none of the Company or any of the Initial Purchasers takes any responsibility for the accuracy of the information. None of the Company, the Fiscal and Paying Agent or any of the Initial Purchasers will have any responsibility or liability for any aspect of the records relating to, or payments made on account of interests in, Notes held through, the facilities of any clearing system, or for maintaining, supervising or reviewing any records relating to such beneficial ownership interests.

DTC has advised the Company as follows: DTC is a limited purpose trust company organised under the laws of the State of New York, a member of the Federal Reserve System, a "clearing corporation" within the meaning of the New York Uniform Commercial Code and a "clearing agency" registered pursuant to the provisions of Section 17A of the Exchange Act. DTC was created to hold securities for DTC participants and to facilitate the clearance and settlement of transactions between DTC participants through electronic book-entry changes in accounts of DTC participants, thereby eliminating the need for physical movement of certificates. DTC participants include certain of the Initial Purchasers, securities brokers and dealers, banks, trust companies, clearing corporations and may in the future include certain other organisations ("DTC participants"). Indirect access to the DTC system is also available to others such as banks, brokers, dealers and trust companies that clear through or maintain a custodial relationship with a DTC participant, either directly or indirectly ("indirect DTC participants").

Under the rules, regulations and procedures creating and affecting DTC and its operations (the "Rules"), DTC is required to make book-entry transfers of Notes among DTC participants on whose behalf it acts with respect to Notes accepted into DTC's book-entry settlement system as described below (the "DTC Notes") and to receive and transmit distributions of the nominal amount and interest on the DTC Notes. DTC participants and indirect DTC participants with which beneficial owners of DTC Notes ("Owners") have accounts with respect to the DTC Notes similarly are required to make book-entry transfers and receive and transmit such payments on behalf of their respective Owners. Accordingly, although Owners who hold DTC Notes through DTC participants or indirect DTC participants will not possess Notes, the Rules, by virtue of the requirements described above, provide a mechanism by which such Owners will receive payments and will be able to transfer their interests with respect to the Notes.

Transfers of ownership or other interests in the Notes in DTC may be made only through DTC participants. Indirect DTC participants are required to effect transfers through a DTC participant. DTC has no knowledge of the actual beneficial owners of the Notes. DTC's records reflect only the identity of the DTC participants to whose accounts the Notes are credited, which may not be the beneficial owners. DTC participants will remain responsible for keeping account of their holdings on behalf of their customers and for forwarding all notices concerning the Notes to their customers. So long as DTC, or its nominee, is the registered holder of a global note, payments on the applicable Notes will be made in immediately available funds to DTC. DTC's practice is to credit DTC participants' accounts on the applicable payment date in accordance with their respective holdings shown on its records, unless DTC has reason to believe that it will not receive payment on that date. Payments by DTC participants to beneficial owners will be governed by standing instructions and customary practices, and will be the responsibility of the DTC participants and not of DTC, or any other party, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment to DTC is the responsibility of the Fiscal and Paying Agent. Disbursement of payments for DTC participants will be DTC's responsibility, and disbursement of payments to the beneficial owners will be the responsibility of DTC participants and indirect DTC participants.

Because DTC can only act on behalf of DTC participants, who in turn act on behalf of indirect DTC participants, and because owners of beneficial interests in the Notes holding through DTC will hold interests in the Notes through DTC participants or indirect DTC participants, the ability of the owners of the beneficial interests to pledge Notes to persons or entities that do not participate in DTC, or otherwise take actions with respect to the Notes, may be limited. DTC will take any action permitted to be taken by an Owner only at the direction of one or more DTC participants to whose account with DTC such Owner's DTC Notes are credited. Additionally, DTC has advised the Company that it will take such actions with respect to any percentage of the beneficial interest of Owners who hold Notes through DTC participants or indirect participants only at the direction of and on behalf of DTC participants whose account holders include undivided interests that satisfy any such percentage.

To the extent permitted under applicable law and regulations, DTC may take conflicting actions with respect to other undivided interests to the extent that such actions are taken on behalf of DTC participants whose account holders include such undivided interests.

Ownership of interests in the Rule 144A Notes and the Regulation S Notes will be shown on, and the transfer of that ownership will be effected only through records maintained by, DTC, the DTC participants and the indirect DTC participants, including Euroclear and Clearstream, Luxembourg. Transfers between participants in DTC, as well as transfers between participants in Euroclear and Clearstream, Luxembourg will be effected in the ordinary way in accordance with DTC rules.

Subject to compliance with the transfer restrictions applicable to the Notes, cross-market transfers between DTC, on the one hand, and participants in Euroclear or Clearstream, Luxembourg on the other hand, will be effected in DTC in accordance with the Rules on behalf of Euroclear or Clearstream, Luxembourg, as the case may be. Such cross-market transactions, however, will require delivery of instructions to Euroclear or Clearstream, Luxembourg, as the case may be, by the counterparty in such system in accordance with its rules and procedures and within its established deadlines. Euroclear or Clearstream, Luxembourg, as the case may be, will, if the transaction meets its settlement requirements, deliver instructions to DTC to take action to effect final settlement on its behalf by delivering or receiving payment in accordance with DTC's Same Day Funds Settlement System.

According to DTC, the foregoing information with respect to DTC has been provided to the industry for informational purposes only and is not intended to serve as a representation, warranty or contract modification of any kind. Although DTC, Euroclear and Clearstream, Luxembourg have agreed to the foregoing procedures in order to facilitate transfers of interests in the global notes among participants of DTC, Euroclear and Clearstream, Luxembourg, they are under no obligation to perform or continue to perform such procedures, and such procedures may be discontinued at any time. None of the Company or the Fiscal and Paying Agent will have any responsibility for the performance by DTC, Euroclear or Clearstream, Luxembourg or their respective participants or indirect participants, of their respective obligations under the rules and procedures governing their operations.

Initial Settlement in relation to DTC Notes

Upon the issue of a DTC Note deposited with DTC or a custodian therefor, DTC or its custodian, as the case may be, will credit, on its internal system, the respective nominal amount of the individual beneficial interest represented by such relevant DTC Note or Notes to the accounts of persons who have accounts with DTC. Such accounts initially will be designated by or on behalf of the relevant Initial Purchasers. Ownership of beneficial interest in a DTC Note will be limited to DTC participants, including Euroclear and Clearstream, Luxembourg or indirect DTC participants. Ownership of beneficial interests in DTC Notes will be shown on, and the transfer of that ownership will be effected only through, records maintained by DTC or its nominee (with respect to interests of DTC participants) and the records of DTC participants (with respect to interests of indirect DTC participants). Investors that hold their interests in a

DTC Note will follow the settlement procedures applicable to global bond issues. Investors' securities custody accounts will be credited with their holdings against payment in same day funds on the Issue Date.

Secondary Market Trading in relation to DTC Notes

Since the purchaser determines the place of delivery, it is important to establish at the time of the trade where both the purchaser's and seller's accounts are located to ensure that settlement can be made on the desired value date. Although DTC has agreed to the following procedures in order to facilitate transfers of interests in global notes deposited with DTC or a custodian therefor among participants of DTC, DTC is under no obligation to perform or continue to perform such procedures, and such procedures may be discontinued at any time. Neither the Company nor any agent of the Company will have any responsibility for the performance by DTC or its participants or indirect participants of their respective obligations under the rules and procedures governing their operations.

Secondary market trading between DTC participants will be settled using the procedures applicable to global bond issues in same day funds.

Payments

The Company will maintain an office or agency (a) where the applicable Notes may be presented for payment, (b) where the applicable Notes may be presented for registration of transfer and for exchange and (c) where notices and demands to or upon the Company in respect of the applicable Notes or the Fiscal and Paying Agency Agreements may be served. The Company will give the Fiscal and Paying Agent written notice of the location of any such office or agency and of any change of location thereof. The Company will initially designate the Fiscal and Paying Agent for such purposes. The Company may also from time to time designate one or more other offices or agencies where the Notes may be presented or surrendered for any or all such purposes or where such notices or demands may be served and may from time to time rescind such designations; provided, however, that the Company will, to the extent possible as a matter of law, maintain a paying agent with a specified office in a member state of the EU that will not be obliged to withhold or deduct tax pursuant to EU Directive 2003/48/EC on the taxation of savings or any law implementing or complying with, or introduced in order to conform to, the Directive. The Company shall give written notice to the Fiscal and Paying Agent of any such designation or rescission and of any such change in the location of any other office or agency.

A holder of Notes may transfer or exchange Notes in accordance with their terms. The Fiscal and Paying Agent will not be required to accept for registration or transfer any Notes, except upon presentation of satisfactory evidence (which may include legal opinions) that the restrictions on transfer have been complied with, all in accordance with such reasonable regulations as the Company may from time to time agree with such Fiscal and Paying Agent.

Notwithstanding any statement herein, the Company reserves the right to impose or remove such transfer, certification, substitution or other requirements, and to require such restrictive legends on the Notes, as it may determine are necessary to ensure compliance with the securities laws of the United States and the states therein and any other applicable laws or as may be required by any stock exchange on which the Notes are listed. The Company may require payment of a sum sufficient to cover any tax or other governmental charge that may be imposed in connection with any exchange or registration of transfer of Notes and any other expenses (including the fees and expenses of the Fiscal and Paying Agent). No service charge will be made for any such transaction.

The Fiscal and Paying Agent will not be required to exchange or register a transfer of (a) any Notes for a period of 15 days ending on the due date for any payment of principal in respect of the Notes or the first mailing of any notice of redemption of Notes to be redeemed or (b) any Notes selected, called or being called for redemption.

The Notes will be issued in registered form without coupons and transferable in denominations of $200,000 and integral multiples of $1,000 in excess thereof.

The laws of some jurisdictions require that certain persons take physical delivery in definitive form of securities which they own. Consequently, the ability to transfer beneficial interests in the global notes is limited to such extent.

CERTAIN TAXATION CONSIDERATIONS

United Kingdom Taxation

The comments below are of a general nature based on current United Kingdom tax law as applied in England and Wales and HM Revenue & Customs practice (which may not be binding on HM Revenue & Customs) and are not intended to be exhaustive. They do not necessarily apply where the income is deemed for tax purposes to be the income of any other person. They relate only to the position of persons who are the absolute beneficial owners of their Notes. Certain classes of persons such as dealers, certain professional investors, or persons connected with the Company may be subject to special rules and this summary does not apply to such Noteholders.

Any Noteholders who are in doubt as to their own tax position or who may be subject to tax in a jurisdiction other than the United Kingdom should consult their professional advisers.

Interest on the Notes

Payments of interest on the Notes may be made without withholding or deduction for or on account of United Kingdom income tax as long as the Notes are and continue to be listed on a recognised stock exchange within the meaning of section 1005 of the Income Tax Act 2007. The London Stock Exchange is such a recognised stock exchange. Securities will be treated as listed on the London Stock Exchange if they are included in the Official List (within the meaning of and in accordance with the provisions of Part 6 of the Financial Services and Markets Act 2000) and admitted to trading on the London Stock Exchange. Provided, therefore, that the Notes remain so listed, interest may be paid on the Notes without withholding or deduction for or on account of United Kingdom income tax.

If the Notes cease to be listed, interest will generally be paid by the Company under deduction of income tax at the basic rate (currently 20 per cent.) unless: (i) another relief applies; or (ii) the Company has received a direction to the contrary from HM Revenue & Customs in respect of such relief as may be available pursuant to the provisions of any applicable double taxation treaty.

If interest were paid under deduction of United Kingdom income tax (e.g., if the Notes lost their listing), Noteholders who are not resident in the United Kingdom may be able to recover all or part of the tax deducted if there is an appropriate provision in an applicable double taxation treaty. In its current form, the tax treaty between the United Kingdom and the United States provides for a zero rate of withholding on interest for those holders that are eligible for the benefits of such treaty.

The interest has a United Kingdom source and accordingly may be chargeable to United Kingdom tax by direct assessment irrespective of the residence of the Noteholder. However, where the interest is paid without withholding or deduction on account of United Kingdom tax, the interest will not be assessed to United Kingdom tax in the hands of Noteholders (other than certain trustees) who are not resident in the United Kingdom, except where the Noteholder carries on a trade, profession or vocation through a branch or agency, or in the case of a corporate holder, carries on a trade through a permanent establishment in the United Kingdom, in connection with which the interest is received or to which the Notes are attributable, in which case (subject to exemptions for interest received by certain categories of agent) tax may be levied on the United Kingdom branch or agency, or permanent establishment.

Noteholders should be aware that the provisions relating to additional amounts referred to in "Description of the Notes—Payment of Additional Amounts" above would not apply as a consequence of HM Revenue & Customs seeking to assess directly the person entitled to the relevant interest to United Kingdom tax (which HM Revenue & Customs Revenue may not do to a holder not resident in the United Kingdom who does not carry on a trade, profession or vocation in the United Kingdom through a United Kingdom branch, agency or permanent establishment). However, exemption from, or reduction of, such United Kingdom tax liability might be available under an applicable double taxation treaty.

Information Reporting

HM Revenue & Customs has powers to obtain information relating to securities in certain circumstances. This may include details of the beneficial owners of the Notes (or the persons for whom the Notes are held), details of the persons to whom payments derived from the Notes are or may be paid and information and documents in connection with transactions relating to the Notes. Information may be required to be provided by, amongst others, the holders of the Notes, persons by (or via) whom payments derived from the Notes are made or who receive (or would be entitled to receive) such payments, persons who effect or are a party to transactions relating to the Notes on behalf of others and certain registrars or administrators. In certain circumstances, the information obtained by HM Revenue & Customs may be exchanged with tax authorities in other countries.

EU Directive on the Taxation of Savings Income

The EU Savings Directive requires EU Member States to provide to the tax authorities of other EU Member States details of payments of interest and other similar income paid by a person established within its jurisdiction to (or for the benefit of) an individual or certain other persons in that other EU Member State, except that Austria and Luxembourg will instead impose a withholding system for a transitional period (subject to a procedure whereby, on meeting certain conditions, the beneficial owner of the interest or other income may request that no tax be withheld) unless during such period they elect otherwise. The Luxembourg government has announced its intention to elect out of the withholding system in favour of an automatic exchange of information with effect from 1 January 2015.

The European Commission has proposed certain amendments to the EU Savings Directive, which may, if implemented, amend or broaden the scope of the requirements described above.

Taxation of Disposal (including Redemption) and Return

Noteholders Within the Charge to Corporation Tax

Noteholders within the charge to United Kingdom corporation tax (including non-resident Noteholders whose Notes are used, held or acquired for the purposes of a trade carried on in the United Kingdom through a permanent establishment) will be subject to tax as income on all profits and gains from the Notes broadly in accordance with their statutory accounting treatment. Such Noteholders will generally be charged in each accounting period by reference to interest and other amounts which, in accordance with generally accepted accounting practice, are recognised in determining the Noteholder's profit or loss for that period. Fluctuations in value relating to foreign exchange gains and losses in respect of the Notes will be brought into account as income.

Other United Kingdom Noteholders

Interest

Noteholders who are either individuals or trustees and are resident for tax purposes in the United Kingdom or who carry on a trade, profession or vocation in the United Kingdom through a branch or agency to which the Notes are attributable will generally be liable to United Kingdom tax on the amount of any interest received in respect of the Notes.

Transfer (including redemption)

A disposal of a Note by a Noteholder resident for tax purposes in the United Kingdom or who carries on a trade, profession or vocation in the United Kingdom through a branch or agency to which the Note is attributable may give rise to a chargeable gain or allowable loss for the purposes of taxation of capital gains. In calculating any gain or loss on disposal of a Note, pound sterling values are compared at acquisition and transfer. Accordingly, a taxable profit can arise even where the foreign currency amount received on a disposal is less than or the same as the amount paid for the Note.

A transfer of a Note by a Noteholder resident for tax purposes in the United Kingdom or who carries on a trade, profession or vocation in the United Kingdom through a branch or agency to which the Note is attributable may give rise to a charge to tax on income in respect of an amount representing interest on the Note which has accrued since the preceding interest payment date under the provisions of Chapter 2 of Part 12 of the Income Tax Act 2007 (Accrued Income Profits and Losses).

Non-United Kingdom Noteholders

A disposal of a Note by a Noteholder that, in the relevant period, is not resident for tax purposes in the United Kingdom and who does not carry on a trade, profession or vocation in the United Kingdom will not, in most circumstances (other than, for example, when the Noteholder is only temporarily resident outside the United Kingdom), give rise to a charge to United Kingdom tax.

CERTAIN UNITED STATES FEDERAL INCOME TAX CONSIDERATIONS

TO ENSURE COMPLIANCE WITH TREASURY DEPARTMENT CIRCULAR 230, HOLDERS ARE HEREBY NOTIFIED THAT: (A) ANY DISCUSSION OF UNITED STATES FEDERAL TAX ISSUES IN THIS OFFERING CIRCULAR IS NOT INTENDED OR WRITTEN TO BE RELIED UPON, AND CANNOT BE RELIED UPON, BY HOLDERS FOR THE PURPOSE OF AVOIDING PENALTIES THAT MAY BE IMPOSED ON HOLDERS UNDER THE INTERNAL REVENUE CODE; (B) SUCH DISCUSSION IS INCLUDED HEREIN BY THE COMPANY IN CONNECTION WITH THE PROMOTION OR MARKETING (WITHIN THE MEANING OF CIRCULAR 230) BY THE COMPANY OF THE TRANSACTIONS OR MATTERS ADDRESSED HEREIN; AND (C) HOLDERS SHOULD SEEK ADVICE BASED ON THEIR PARTICULAR CIRCUMSTANCES FROM AN INDEPENDENT TAX ADVISER.

* * * * *

The following is a summary of certain U.S. federal income tax consequences of the acquisition, ownership and disposition of Notes by a United States Holder (as defined below). This summary deals only with initial purchasers of Notes at the issue price that are United States Holders and that will hold the Notes as capital assets. The discussion does not cover all aspects of U.S. federal income taxation that may be relevant to, or the actual tax effect that any of the matters described herein will have on, the acquisition, ownership or disposition of Notes by particular investors, and does not address state, local, foreign or other tax laws. This summary also does not discuss all of the tax considerations that may be relevant to certain types of investors subject to special treatment under the U.S. federal income tax laws (such as financial institutions, insurance companies, investors liable for the alternative minimum tax or the net investment income tax, individual retirement accounts and other tax-deferred accounts, tax-exempt organisations, dealers in securities or currencies, investors that will hold the Notes as part of straddles, hedging transactions or conversion transactions for U.S. federal income tax purposes or investors whose functional currency is not the United States dollar).

As used herein, the term "United States Holder" means a beneficial owner of Notes that is, for U.S. federal income tax purposes, (i) an individual citizen or resident of the United States, (ii) a corporation created or organised under the laws of the United States or any State thereof, (iii) an estate the income of which is subject to U.S. federal income tax without regard to its source or (iv) a trust if a court within the United States is able to exercise primary supervision over the administration of the trust and one or more United States persons have the authority to control all substantial decisions of the trust, or the trust has validly elected to be treated as a domestic trust for U.S. federal income tax purposes.

The U.S. federal income tax treatment of a partner in an entity treated as a partnership for U.S. federal income tax purposes that holds Notes will depend on the status of the partner and the activities of the partnership. Prospective purchasers that are entities treated as partnerships for U.S. federal income tax purposes and their partners should consult their tax advisers concerning the U.S. federal income tax consequences of the acquisition, ownership and disposition of Notes by the partnership.

This summary is based on the tax laws of the United States, including the Internal Revenue Code of 1986, as amended, its legislative history, existing and proposed regulations thereunder, published rulings and court decisions, as well as on the income tax treaty between the United States and the United Kingdom (the "Treaty"), all as of the date hereof and all subject to change at any time, possibly with retroactive effect.

THE SUMMARY OF UNITED STATES FEDERAL INCOME TAX CONSEQUENCES SET OUT BELOW IS FOR GENERAL INFORMATION ONLY. ALL PROSPECTIVE PURCHASERS SHOULD CONSULT THEIR TAX ADVISERS AS TO THE PARTICULAR TAX CONSEQUENCES TO THEM OF OWNING THE NOTES, INCLUDING THEIR ELIGIBILITY FOR THE BENEFITS OF THE TREATY, THE APPLICABILITY AND EFFECT OF STATE, LOCAL, FOREIGN AND OTHER TAX LAWS AND POSSIBLE CHANGES IN TAX LAW.

Payments of Interest

General. Interest on a Note will be taxable to a United States Holder as ordinary income at the time it is received or accrued, depending on the holder's method of accounting for tax purposes. Interest paid by the Issuer on the Notes constitutes income from sources outside the United States. Prospective purchasers should consult their tax advisers concerning the applicability of the foreign tax credit and source of income rules to income attributable to the Notes.

Sale and Retirement of the Notes

A United States Holder will generally recognise gain or loss on the sale or retirement of a Note equal to the difference between the amount realised on the sale or retirement and the tax basis of the Note. A United States Holder's tax basis in a Note will generally be its United States dollar cost. The amount realised does not include the amount attributable to accrued but unpaid interest, which will be taxable as interest income to the extent not previously included in income.

Gain or loss realised by a United States Holder on the sale or retirement of a Note generally will be United States source.

Backup Withholding and Information Reporting

Payments of principal and interest on, and the proceeds of sale or other disposition of, Notes by a United States paying agent or other United States intermediary will be reported to the IRS and to the United States Holder as may be required under applicable regulations. Backup withholding may apply to these payments if the United States Holder fails to provide an accurate taxpayer identification number or certification of exempt status or fails to report all interest and dividends required to be shown on its U.S. federal income tax returns. Certain United States Holders are not subject to backup withholding. United States Holders should consult their tax advisers as to their qualification for exemption from backup withholding and the procedure for obtaining an exemption.

Foreign Financial Asset Reporting

Legislation enacted in 2010 imposes reporting requirements on the holding of certain foreign financial assets, including debt of foreign entities, if the aggregate value of all of these assets exceeds $50,000 at the end of the taxable year or $75,000 at any time during the taxable year. The thresholds are higher for individuals living outside of the United States and married couples filing jointly. The Notes will not to constitute foreign financial assets subject to these requirements if the Notes are held in an account at a financial institution (but the account may be reportable if maintained by a foreign financial institution). United States Holders should consult their tax advisers regarding the application of this legislation.

PLAN OF DISTRIBUTION

Pursuant to a Purchase Agreement dated 10 October 2013 (the "Purchase Agreement"), the Initial Purchasers have severally and not jointly agreed with the Company, subject to the satisfaction of certain conditions, to purchase $750,000,000 principal amount of the 2023 Notes and $600,000,000 principal amount of the 2043 Notes. The respective principal amount of Notes to be purchased by each of the Initial Purchasers from the Company is set forth opposite their respective names below:

Initial Purchaser	Principal Amount of 2023 Notes	Principal Amount of 2043 Notes
Barclays Capital Inc.	$ 93,750,000	$ 75,000,000
BNP Paribas Securities Corp.	$ 93,750,000	$ 75,000,000
Citigroup Global Markets Inc.	$ 93,750,000	$ 75,000,000
Deutsche Bank Securities Inc.	$ 93,750,000	$ 75,000,000
HSBC Securities (USA) Inc.	$ 93,750,000	$ 75,000,000
J.P. Morgan Securities LLC	$ 93,750,000	$ 75,000,000
RBS Securities Inc.	$ 93,750,000	$ 75,000,000
Société Générale	$ 93,750,000	$ 75,000,000
Total	**$750,000,000**	**$600,000,000**

The Purchase Agreement entitles the Initial Purchasers to terminate the purchase of the Notes under certain circumstances prior to payment to the Company. The Company has agreed to indemnify the Initial Purchasers against certain liabilities in connection with the offer and sale of the Notes, including liabilities under the Securities Act, and may be required to contribute to payments the Initial Purchasers may be required to make in respect thereof.

The Initial Purchasers, or certain of their respective affiliates as selling agents, initially propose to offer part or all of the Notes at the respective offering prices set forth on the cover page hereof. After the initial offering of the Notes, the offering prices and other selling terms may be varied from time to time by the Initial Purchasers.

The Company has agreed with the Initial Purchasers that neither they nor any person acting on their behalf will, without the prior written consent of the Initial Purchasers, for the period from and including the date of the Purchase Agreement through and including the issue date of the Notes, offer, sell, contract to sell or otherwise dispose of any debt securities of the Company substantially similar to the Notes or securities convertible into or exchangeable for such debt securities of the Company, or sell or grant options, rights or warrants with respect to such debt securities of the Company or securities convertible into or exchangeable for such debt securities of the Company.

The Notes are a new issue of securities with no established trading market. The Notes are expected to be admitted to trading on the Regulated Market of the London Stock Exchange.

The Initial Purchasers are not obliged to make a market in the Notes and, even if such activities are commenced, they may be discontinued at any time without notice. Accordingly, no assurance can be given as to the liquidity of, or any trading market for, the Notes. If the Notes are traded, they may trade at a discount from their initial offering price depending on prevailing interest rates, the market for similar securities, the operating performance and financial condition of the Group, general economic conditions and other factors.

In connection with the Offering of the Notes, Stabilisation Manager may over-allot or effect transactions with a view to supporting the market price of the Notes at a level higher than that which might otherwise prevail for a limited period after the date of issue of the Notes. However, there is no obligation on the part of the Stabilisation Manager to do this. Such stabilising, if commenced, may be discontinued at any time, and must be brought to an end after a limited period.

No action has been or will be taken in any jurisdiction that would permit a public offering of the Notes or the possession, circulation or distribution of any material relating to the Offering in any jurisdiction where action for such purpose is required. Accordingly, the Notes may not be offered or sold, directly or indirectly, nor may any offering material or advertisement in connection with the Notes (including this document and any amendment or supplement hereto) be distributed or published, in or from any country or jurisdiction, except under circumstances that will result in compliance with any applicable rules and regulations of any such country or jurisdiction.

Certain of the Initial Purchasers and their affiliates have performed and may continue to perform certain investment and commercial banking or financial advisory services for the Company and its affiliates from time to time, for which they have received customary fees and commissions, and they expect to provide these services to the Company and its affiliates in the future, for which they expect to receive customary fees and commissions.

In addition, in the ordinary course of their business activities, the Initial Purchasers and their affiliates may make or hold a broad array of investments and actively trade debt and equity securities (or related derivative securities) and financial instruments (including bank loans) for their own account and for the accounts of their customers. Such investments and securities activities may involve securities and/or instruments of the Company and its affiliates. Certain of the Initial Purchasers or their affiliates that have a lending relationship with the Company routinely hedge their resulting credit exposure consistent with their customary risk management policies. Typically, such Initial Purchasers and their affiliates would hedge such exposure by entering into transactions which consist of either the purchase of credit default swaps or the creation of short positions in our securities, including potentially the Notes offered hereby. Any such short positions could adversely affect future trading prices of the Notes offered hereby. The Initial Purchasers and their affiliates may also make investment recommendations and/or publish or express independent research views in respect of such securities or financial instruments and may hold, or recommend to clients that they acquire, long and/or short positions in such securities and instruments.

United States

The Notes have not been and will not be registered under the Securities Act and may not be offered, sold or delivered within the United States or to, or for the account or benefit of, US persons except in certain transactions exempt from the registration requirements of the Securities Act. Accordingly, the Notes are being offered and sold only (i) outside the United States in reliance on Regulation S and (ii) within the United States to QIBs in accordance with Rule 144A.

Each Initial Purchaser has represented and agreed with the Company that, except as permitted by the Purchase Agreement, it will not offer, sell or deliver the Notes, (i) as part of their distribution at any time or (ii) otherwise until and including the fortieth day after the later of the commencement of the Offering and the Closing Date for the sale of any Notes pursuant to the Purchase Agreement (the "distribution compliance period"), within the United States or to, or for the account or benefit of, US persons except in accordance with Rule 144A or Rule 903 of Regulation S. Each Initial Purchaser has also agreed that it, each of its affiliates and each person acting on its or their behalf has complied and will comply with the offering restriction requirements of Regulation S; and that at or prior to confirmation of a sale of Notes (other than a sale pursuant to Rule 144A, if permitted) it will have sent to each distributor, dealer or other person receiving a selling concession, fee or other remuneration to which it sells Notes during the distribution compliance period a confirmation or other notice setting forth the restrictions on offers and sales of the Notes within the United States or to, or for the account or benefit of, US persons. Each Initial Purchaser has also represented and agreed with the Company that no directed selling efforts (as defined in Regulation S) have been made or will be made in the United States by the Initial Purchasers, any of their affiliates or any person acting on behalf of any of the Initial Purchasers or their affiliates with respect to the Notes; and none of it, any of its affiliates, or anyone acting on its or their behalf has solicited offers for, offered or sold the Notes by any form of general solicitation or general advertising (as those terms are used in Regulation D under the Securities Act) in the United States in connection with the Offering of the Notes or otherwise in any manner involving a public offering within the meaning of Section 4(2) of the Securities Act.

Terms used in the preceding two paragraphs have the meanings ascribed to them by Rule 144A and Regulation S under the Securities Act, as applicable.

In addition, until 40 days after the commencement of the Offering of the Notes, an offer or sale of Notes within the United States by any dealer (whether or not participating in the Offering of the Notes) may violate the registration requirements of the Securities Act if such offer or sale is made otherwise than in accordance with Rule 144A under the Securities Act.

The Purchase Agreement also provides that the Initial Purchasers or their affiliates may arrange for the placing of a portion of the Notes to persons reasonably believed to be QIBs pursuant to Rule 144A.

United Kingdom

Each Initial Purchaser has represented and agreed with the Company that:

- it has communicated or caused to be communicated and will only communicate or cause to be communicated any invitation or inducement to engage in investment activity (within the meaning of section 21 of the Financial Services and Markets Act 2000 (the "FSMA")), received by it in connection with the issue or sale of any Notes in circumstances in which section 21(1) of the FSMA does not apply to the Company; and
- it has complied and will comply with all applicable provisions of the FSMA with respect to anything done by it in relation to the Notes in, from or otherwise involving the United Kingdom.

Japan

Each Initial Purchaser understands that the Notes have not been and will not be registered under the Securities and Exchange Law of Japan, and represents that it has not offered or sold, and agrees with the Company not to offer or sell, directly or indirectly, any Notes in Japan or for the account of any resident thereof except pursuant to any exemption from the registration requirements of the Securities and Exchange Law of Japan and otherwise in compliance with applicable provisions of Japanese law.

TRANSFER RESTRICTIONS

The following restrictions will apply to the Notes. Prospective holders of Notes are advised to consult legal counsel prior to making any offer, sale, resale, pledge, or transfer of the Notes offered hereby.

The Notes have not been and will not be registered under the Securities Act or any state securities laws and, unless so registered, may not be offered, sold or delivered except pursuant to an exemption from, or in a transaction not subject to, the registration requirements of the Securities Act and applicable state securities laws. Accordingly, the Notes offered hereby are being offered and sold only (i) within the United States to QIBs in reliance on Rule 144A under the Securities Act and (ii) outside the United States in reliance on Regulation S under the Securities Act.

Each purchaser of Notes, by its acceptance thereof, will be deemed to have acknowledged, represented to and agreed with the Company and the Initial Purchasers as follows:

(1) It understands and acknowledges that the Notes have not been and will not be registered under the Securities Act or any other applicable securities law, are being offered for resale in transactions not requiring registration under the Securities Act or any other securities law, including sales pursuant to Rule 144A under the Securities Act, and may not be offered, sold or otherwise transferred within the United States except in compliance with the registration requirements of the Securities Act or any other applicable securities law, pursuant to an exemption therefrom or in any transaction not subject thereto, and in each case in compliance with, the conditions for transfer set forth in paragraphs (4) and (5) below.

(2) It is not an "affiliate" (as defined in Rule 144 under the Securities Act) of the Company, nor acting on behalf of the Company and it is either:

- a QIB and is aware that any sale of Notes to it will be made in reliance on Rule 144A under the Securities Act, of which the purchase will be for its own account or for the account of another QIB; or
- purchasing the Notes outside the United States in accordance with Regulation S under the Securities Act.

(3) It acknowledges that none of the Company, its subsidiaries or the Initial Purchasers, nor any person representing the Company, its subsidiaries or the Initial Purchasers, has made any representation to it with respect to the Offering or sale of any Notes, other than the information contained in this Offering Circular, which has been delivered to it and upon which it is relying in making its investment decision with respect to the Notes. It has had access to such financial and other information concerning the Company and the Notes as it has deemed necessary in connection with its decision to purchase any of the Notes.

(4) It is purchasing the Notes for its own account, or for one or more investor accounts for which it is acting as a fiduciary or agent, in each case for investment, and not with a view to, or for offer or sale in connection with, any distribution thereof in violation of the Securities Act or any state securities laws, subject to any requirement of law that the disposition of its property or the property of such investor account or accounts be at all times within its or their control and subject to its or their ability to resell such Notes pursuant to Rule 144A, Regulation S or any other exemption from registration available under the Securities Act.

(5) If such a purchaser is a purchaser of Notes issued in reliance on Rule 144A ("Rule 144A Notes"), it agrees on its own behalf and on behalf of any investor account for which it is purchasing the Notes, and each subsequent holder of the Notes by its acceptance thereof will be deemed to agree not to offer, sell or otherwise transfer such Notes prior to the date following the expiration of the applicable required holding period determined pursuant to Rule 144, after which such Notes may be freely transferred pursuant to Rule 144 under the Securities Act, except (i) to the Company, (ii) pursuant to a registration statement that has been declared effective under the Securities Act, (iii) for so long as the Notes are eligible for resale pursuant to Rule 144A under the Securities Act, to a person it reasonably believes is a QIB that purchases for its own account or for the account of a QIB to whom notice is given that the transfer is being made in reliance on Rule 144A under the Securities Act, (iv) pursuant to offers and sales that occur outside the US in compliance with Regulation S under the Securities Act or (v) pursuant to any other available exemption from the registration requirements of the Securities Act, subject in each of the foregoing cases to any requirement of law that the disposition of its property or the property of such investor account or accounts be at all times within its or their

control and in compliance with any applicable state securities laws, and any applicable local laws and regulations, and further subject to the Company's and the Fiscal and Paying Agent's rights prior to any such offer, sale or transfer (A) pursuant to clause (v) above to require the delivery of an opinion of counsel, certification and/or other information satisfactory to each of them and (B) in each of the foregoing cases, to require that a transfer notice in the form attached as a schedule to the Fiscal and Paying Agency Agreements is completed and delivered by the transferor to the Fiscal and Paying Agent.

(6) It understands that the Notes being sold pursuant to Rule 144A will bear a legend to the following effect:

THIS NOTE IS A GLOBAL NOTE WITHIN THE MEANING OF THE FISCAL AND PAYING AGENCY AGREEMENTS HEREINAFTER REFERRED TO AND IS REGISTERED IN THE NAME OF A DEPOSITARY OR A NOMINEE OR A DEPOSITARY OR A SUCCESSOR DEPOSITARY. NEITHER THIS NOTE NOR ANY BENEFICIAL INTEREST HEREIN HAS BEEN REGISTERED UNDER THE US SECURITIES ACT OF 1933, AS AMENDED (THE "SECURITIES ACT") OR ANY STATE SECURITIES LAWS. NEITHER THIS NOTE NOR ANY INTEREST OR PARTICIPATION HEREIN MAY BE REOFFERED, SOLD, ASSIGNED, TRANSFERRED, PLEDGED, ENCUMBERED OR OTHERWISE DISPOSED OF IN THE UNITED STATES IN THE ABSENCE OF SUCH REGISTRATION OR UNLESS SUCH TRANSACTION IS EXEMPT FROM, OR NOT SUBJECT TO, THE REGISTRATION REQUIREMENTS OF THE SECURITIES ACT.

THE HOLDER OF THIS NOTE BY ITS ACCEPTANCE HEREOF AGREES TO OFFER, SELL OR OTHERWISE TRANSFER SUCH NOTE, PRIOR TO THE DATE (THE "SPECIFIED DATE") FOLLOWING THE EXPIRATION OF THE APPLICABLE REQUIRED HOLDING PERIOD DETERMINED PURSUANT TO RULE 144 UNDER THE SECURITIES ACT FROM THE LATER OF THE DATE OF ACQUISITION OF THIS NOTE FROM (I) THE ISSUER THEREOF OR (II) AN AFFILIATE OF SUCH ISSUER, AND ANY RESALE OF THIS NOTE IN RELIANCE ON RULE 144 UNDER THE SECURITIES ACT FOR THE ACCOUNT OF EITHER THE ACQUIRER OR ANY SUBSEQUENT HOLDER OF THIS NOTE (IN EACH CASE DEMONSTRATED TO THE REASONABLE SATISFACTION OF THE ISSUER OF THIS NOTE) ONLY (A) TO THE ISSUER AND ANY SUBSIDIARY OR ANY AFFILIATE THEREOF (B) PURSUANT TO A REGISTRATION STATEMENT WHICH HAS BEEN DECLARED EFFECTIVE UNDER THE SECURITIES ACT, (C) FOR SO LONG AS THE SECURITIES ARE ELIGIBLE FOR RESALE PURSUANT TO RULE 144A UNDER THE SECURITIES ACT ("RULE 144A"), TO A PERSON IT REASONABLY BELIEVES IS A "QUALIFIED INSTITUTIONAL BUYER" AS DEFINED IN RULE 144A THAT PURCHASES FOR ITS OWN ACCOUNT OR FOR THE ACCOUNT OF A QUALIFIED INSTITUTIONAL BUYER TO WHOM NOTICE IS GIVEN THAT THE TRANSFER IS BEING MADE IN RELIANCE ON RULE 144A, (D) PURSUANT TO OFFERS AND SALES THAT OCCUR OUTSIDE THE UNITED STATES IN COMPLIANCE WITH REGULATION S UNDER THE SECURITIES ACT OR (E) PURSUANT TO ANY OTHER AVAILABLE EXEMPTION FROM THE REGISTRATION REQUIREMENTS OF THE SECURITIES ACT, SUBJECT IN EACH OF THE FOREGOING CASES TO ANY REQUIREMENT OF LAW THAT THE DISPOSITION OF ITS PROPERTY OR THE PROPERTY OF SUCH INVESTOR ACCOUNT OR ACCOUNTS BE AT ALL TIMES WITHIN ITS OR THEIR CONTROL AND IN COMPLIANCE WITH ANY APPLICABLE STATE SECURITIES LAWS, AND ANY APPLICABLE LOCAL LAWS AND REGULATIONS AND FURTHER SUBJECT TO THE ISSUER'S AND THE FISCAL AND PAYING AGENT'S RIGHTS PRIOR TO ANY SUCH OFFER, SALE OR TRANSFER (I) PURSUANT TO CLAUSE (E) TO REQUIRE THE DELIVERY OF AN OPINION OF COUNSEL, CERTIFICATION AND/OR OTHER INFORMATION SATISFACTORY TO EACH OF THEM AND (II) IN EACH OF THE FOREGOING CASES, TO REQUIRE THAT A CERTIFICATE OF TRANSFER IN THE FORM ATTACHED AS A SCHEDULE TO THE FISCAL AND PAYING AGENCY AGREEMENTS IS COMPLETED AND DELIVERED BY THE TRANSFEROR TO THE FISCAL AND PAYING AGENT. THE FOREGOING RESTRICTIONS ON RESALE WILL NOT APPLY SUBSEQUENT TO THE SPECIFIED DATE. THE FISCAL AND PAYING AGENCY AGREEMENTS CONTAINS A PROVISION REQUIRING THE FISCAL AND PAYING AGENT TO REFUSE TO REGISTER ANY TRANSFER OF THIS NOTE IN VIOLATION OF THE FOREGOING RESTRICTIONS.

(7) It understands that the Notes being sold in reliance on Regulation S will bear a legend to the following effect:

THIS NOTE IS A GLOBAL NOTE WITHIN THE MEANING OF THE FISCAL AND PAYING AGENCY AGREEMENTS HEREINAFTER REFERRED TO AND IS REGISTERED IN THE NAME OF A DEPOSITARY OR A NOMINEE OR A DEPOSITARY OR A SUCCESSOR DEPOSITARY. NEITHER THIS NOTE NOR ANY BENEFICIAL INTEREST HEREIN HAS BEEN REGISTERED UNDER THE UNITED STATES SECURITIES ACT OF 1933, AS AMENDED (THE "SECURITIES ACT"), AND MAY NOT BE OFFERED, SOLD OR DELIVERED IN THE UNITED STATES OR TO, OR FOR THE ACCOUNT OR BENEFIT OF, ANY US PERSON, UNLESS SUCH NOTE IS REGISTERED UNDER THE SECURITIES ACT OR AN EXEMPTION FROM THE REGISTRATION REQUIREMENTS THEREOF IS AVAILABLE. THIS LEGEND WILL BE REMOVED AFTER THE EXPIRATION OF FORTY DAYS FROM THE LATER OF (I) THE DATE ON WHICH THESE NOTES ARE FIRST OFFERED AND (II) THE DATE OF ISSUE OF THESE NOTES.

(8) It agrees that it will give to each person to whom it transfers the Notes notice of any restrictions on transfer of such Notes.

(9) It acknowledges that until 40 days after the commencement of the Offering, any offer or sale of the Notes within the United States by a dealer (whether or not participating in the Offering) may violate the registration requirements of the Securities Act if such offer or sale is made otherwise than in accordance with Rule 144A under the Securities Act.

(10) It acknowledges that the Fiscal and Paying Agent will not be required to accept for registration of transfer any Notes except upon presentation of evidence satisfactory to the Company and the Fiscal and Paying Agent that the restrictions set forth therein have been complied with.

(11) It acknowledges that the Company, the Initial Purchasers and others will rely upon the truth and accuracy of the foregoing acknowledgements, representations, warranties and agreements and agrees that if any of the acknowledgements, representations, warranties and agreements deemed to have been made by its purchase of the Notes are no longer accurate, it shall promptly notify the Initial Purchasers. If it is acquiring any Notes as a fiduciary or agent for one or more investor accounts, it represents that it has sole investment discretion with respect to each such investor account and that it has full power to make the foregoing acknowledgements, representations and agreements on behalf of each such investor account.

LEGAL MATTERS

The validity of the Notes offered by this Offering Circular and certain matters governed by US federal, New York state and English law will be passed upon for the Issuer by Linklaters LLP. Certain matters governed by US federal and New York state law will be passed upon for the Initial Purchasers by Davis Polk & Wardwell London LLP.

INDEPENDENT AUDITORS

The Consolidated Financial Statements of the Group as of 31 December 2012, 2011 and 2010 and for each of the three years in the period ended 31 December 2012 included in this Offering Circular have been audited by PricewaterhouseCoopers LLP, independent accountants, as stated in its reports appearing herein.

GENERAL INFORMATION

Listing

The listing of the Notes on the Official List will be expressed as a percentage of their nominal amount (exclusive of accrued interest). It is expected that listing of the Notes on the Official List of the United Kingdom Listing Authority and admission of the Notes to trading on the Market will be granted on or before 17 October 2013, subject only to the issue of the Notes in global form. Prior to official listing and admission to trading, however, dealings will be permitted by the London Stock Exchange in accordance with its rules. Transactions will normally be effected for delivery on the third working day after the day of the transaction.

Clearing Reference Numbers

The Notes have been accepted for clearance through DTC's book-entry settlement system. DTC's address is 570 Washington Boulevard, Jersey City, NJ 07310. The CUSIP and ISIN numbers for the Notes are as follows:

	CUSIP Numbers	ISIN Numbers
Rule 144A		
2023 Notes	15639KAA0	US15639KAA07
2043 Notes	15639KAB8	US15639KAB89
Regulation S		
2023 Notes	G2071AAED	USG2071AAE04
2043 Notes	G2071AAF7	USG2071AAF78

Incorporation of the Issuer

The Company was registered and incorporated in England and Wales under registration number 03033654 and operates under the Companies Act 2006 as a public limited company. The Issuer was incorporated on 16 March 1995 and its shares were first traded on the London Stock Exchange on 17 February 1997. The Issuer's registered office is located at Millstream, Maidenhead Road, Windsor, Berkshire SL4 5GD, and the telephone number is +44 1753 494 000.

Corporate Authority

The Company has obtained all necessary consents, approvals and authorisations in connection with the issuance and performance of the Notes. The issue of the Notes was authorised by the Board of the Company in resolutions passed on 17 September 2013 and a committee of the Board of the Company in resolutions dated 27 September 2013.

Absence of Significant Changes

There has been no significant change in the financial or trading position of the Company and its subsidiaries taken as a whole since 30 June 2013, and there has been no material adverse change in the financial position or prospects of the Company and its subsidiaries taken as a whole since 31 December 2012.

Absence of Litigation

There are no governmental, legal or arbitration proceedings (including any such proceedings which are pending or threatened of which the Company is aware), nor have there been such proceedings in the 12 months preceding the date of this document, which may have or have in such period had a significant effect on the financial position or profitability of the Company and/or the Group as a whole.

Absence of Material Contracts

There are no material contracts entered into other than in the ordinary course of the Company's business, which could result in any member of the Group being under an obligation or entitlement that is material to the Issuer's ability to meet its obligations to holders of the Notes.

Yield

The yield of the 2023 Notes and the 2043 Notes is 4.087 per cent. and 5.427 per cent., respectively, on an annual basis. The yield in each case is calculated as of 10 October 2013, on the basis of the issue price set out on the cover of this Offering Circular. It is not an indication of future yield.

Documents on Display

For 12 months starting on the date of this Offering Circular, the following may be inspected during normal business hours (local time) on any weekday (Saturdays, Sundays and public holidays excluded) at the Company's office and the office of the Fiscal and Paying Agent, namely:

(a) this Offering Circular;

(b) the forms of Notes;

(c) the articles of association of the Company;

(d) the annual reports and financial information of Centrica, including the audited consolidated financial information for the periods ended 31 December 2012, 2011, and 2010;

(e) the Interim Financial Statements; and

(f) the Fiscal and Paying Agency Agreements.

This Offering Circular will be published on the website of the Regulatory News Service operated by the London Stock Exchange at http://www.londonstockexchange.com/exchange/prices-and-news/news/market-news/market-news-home.html.

GLOSSARY

The definitions set out below apply throughout this Offering Circular, unless the context requires otherwise.

2023 Notes	means the $750,000,000 4.000 per cent. senior Notes due 2023;
2043 Notes	means the $600,000,000 5.375 per cent. senior Notes due 2043;
2010 Financial Statements	means the consolidated financial statements as of and for the year ended 31 December 2010;
2011 Financial Statements	means the consolidated financial statements as of and for the year ended 31 December 2011;
2012 Financial Statements	means the consolidated financial statements as of and for the year ended 31 December 2012;
2P	means proven and probable;
bcfe	means billion cubic feet equivalent;
BGIL	means British Gas Insurance Limited;
Big Six	means EDF Energy, E.ON UK, npower, Scottish Power, SSE and British Gas;
CBI	means the Confederation of British Industry;
CCGT	means gas-fired combined cycle gas turbine;
Centrica Storage	means the Group's UK gas storage business;
CEP	means the Communications Energy and Paperworkers Union;
CERT	means the Carbon Emissions Reduction Target scheme;
CESP	means the Community Energy Savings Programme;
CGUs	means cash generating units;
Clearstream, Luxembourg	means Clearstream Banking, société anonyme;
Clockwork	means Clockwork Home Services Inc.;
COGEH	means the Canadian Oil and Gas Evaluation Handbook;
Commission	means the US Securities and Exchange Commission;
Company	means Centrica plc;
Consolidated Financial Statements	means, collectively, the 2010 Financial Statements, the 2011 Financial Statements, the 2012 Financial Statements and the Interim Financial Statements;
CRA Regulation	means Regulation (EC) No. 1060/2009 (as amended);
Custodian	means the custodian for DTC;
DECC	means the Department for Energy and Climate Change;
Direct Energy	means the Group's downstream businesses in North America;

DTC	means the Depositary Trust Company;
ECO	means the Energy Companies Obligation;
EMR	means Electricity Market Reform;
EMS	means environmental management systems;
EU Savings Directive	means the Directive 2003/48/EC on the taxation of savings income;
Euroclear	means Euroclear Bank S.A./N.V.;
Exchange Act	means the US Securities Exchange Act of 1934, as amended;
Fiscal and Paying Agency Agreements	means the fiscal and paying agency agreements governing the Notes;
Fiscal and Paying Agent	means Citibank, N.A., London Branch;
FSMA	means the Financial Services and Markets Act 2000;
GFRMC	means the Group Financial Risk Management Committee;
HSSE	means health, safety, security and environment;
IAS	means the International Accounting Standard;
IFRS	means the International Financial Reporting standards as adopted by the European Union;
Initial Purchasers	means the several initial purchasers listed in the first paragraph of "Plan of Distribution";
Interim Financial Statements	means the unaudited interim consolidated financial statements as of and for the six months ended 30 June 2013;
LNG	means liquefied natural gas;
London Stock Exchange	means the London Stock Exchange plc;
LTIFR	means lost-time injury frequency rate;
Markets in Financial Instruments Directive	means Directive 2004/39/EC;
Moody's	means Moody's Investors Service Ltd;
NBP	means the National Balancing Point;
Notes	has the meaning given to that term on the front page of this Offering Circular;
Offering	means the offer and sale of the Notes;
Offering Circular	means this offering circular;
Official List	means the official list of the UK Listing Authority;
Ofgem	means the Office of Gas and Electricity Markets;
PaR	means Profit at Risk;
Paying Agent	means Citibank, N.A., London Branch;
PP&E	means plant, property and equipment;
PRA	means Prudential Regulation Authority;
Prospectus Directive	means Directive 2003/71/EC, as amended;

PRT	means petroleum revenue tax;
Purchase Agreement	means the purchase agreement dated 10 October 2013;
PwC	means PricewaterhouseCoopers LLP;
QIBs	means “qualified institutional buyers”;
QPI	means Qatar Petroleum International;
Regulation S	means Regulation S under the Securities Act;
Regulation S Notes	means the notes offered and sold in reliance on Regulation S;
RMR	means Retail Market Review;
Rough	means the Rough gas storage facility;
Rough Field	means the partially depleted gas field at Rough;
RSA 421-B	means Chapter 421-B of the New Hampshire Revised Statutes Annotated, 1955, as amended;
Rule 144A	means Rule 144A under the Securities Act;
Rule 144A Notes	means the Notes that are initially offered and sold in the United States to QIBs in reliance on Rule 144A;
S&P	means Standard & Poor’s Credit Market Services Europe Limited;
SBU	means Standard Bundled Unit;
Securities Act	means the US Securities Act of 1933, as amended;
SNS	means the Southern North Sea;
Transfer Agent	means Citibank, N.A., London Branch;
Treaty	means the income tax treaty between the United States and the United Kingdom;
Trust Indenture Act	means the US Trust Indenture Act of 1939, as amended;
UK Listing Authority	means the UK Financial Conduct Authority;
VaR	means Value at Risk; and
Venture	means the 2009 acquisitions of Venture Production plc.

INDEX TO FINANCIAL STATEMENTS

INDEPENDENT REVIEW REPORT TO CENTRICA PLC

Introduction

We have been engaged by the company to review the condensed interim Financial Statements in the Interim Results for the six months ended 30 June 2013, which comprise the Group Income Statement, Group Statement of Comprehensive Income, Group Statement of Changes in Equity, Group Balance Sheet, Group Cash Flow Statement and related notes. We have read the other information contained in the Interim Results and considered whether it contains any apparent misstatements or material inconsistencies with the information in the condensed set of Financial Statements.

Directors' responsibilities

The Interim Results are the responsibility of, and have been approved by, the Directors. The Directors are responsible for preparing the Interim Results in accordance with the Disclosure and Transparency Rules of the United Kingdom's Financial Conduct Authority.

As disclosed in note 2, the annual Financial Statements of the Group are prepared in accordance with IFRSs as adopted by the European Union. The condensed set of Financial Statements included in the Interim Results has been prepared in accordance with International Accounting Standard 34, "Interim Financial Reporting", as adopted by the European Union.

Our responsibility

Our responsibility is to express to the company a conclusion on the condensed set of Financial Statements in the Interim Results based on our review. This report, including the conclusion, has been prepared for and only for the company for the purpose of the Disclosure and Transparency Rules of the Financial Conduct Authority and for no other purpose. We do not, in producing this report, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

Scope of review

We conducted our review in accordance with International Standard on Review Engagements (UK and Ireland) 2410, 'Review of Interim Financial Information Performed by the Independent Auditor of the Entity' issued by the Auditing Practices Board for use in the United Kingdom. A review of interim financial information consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing (UK and Ireland) and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the condensed set of Financial Statements in the Interim Results for the six months ended 30 June 2013 are not prepared, in all material respects, in accordance with International Accounting Standard 34 as adopted by the European Union and the Disclosure and Transparency Rules of the United Kingdom's Financial Conduct Authority.

PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
London
31 July 2013

Notes

(i) The maintenance and integrity of the Centrica plc website is the responsibility of the Directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the Financial Statements since they were initially presented on the website.
(ii) Legislation in the United Kingdom governing the preparation and dissemination of financial information may differ from legislation in other jurisdictions.

GROUP INCOME STATEMENT

Six months ended 30 June	Notes	2013 Business performance £m	2013 Exceptional items and certain re-measurements £m	2013 Results for the period £m	2012 (restated) (i) Business performance £m	2012 (restated) (i) Exceptional items and certain re-measurements £m	2012 (restated) (i) Results for the period £m
Group revenue	5(a)	**13,651**	**–**	**13,651**	11,977	–	11,977
Cost of sales before exceptional items and certain re-measurements (i)		**(10,886)**	**–**	**(10,886)**	(9,445)	–	(9,445)
Re-measurement of energy contracts	6(b)	**–**	**104**	**104**	–	513	513
Cost of sales		**(10,886)**	**104**	**(10,782)**	(9,445)	513	(8,932)
Gross profit		**2,765**	**104**	**2,869**	2,532	513	3,045
Operating costs before exceptional items (i)		**(1,332)**	**–**	**(1,332)**	(1,244)	–	(1,244)
Exceptional items	6(a)	**–**	**–**	**–**	–	(90)	(90)
Operating costs		**(1,332)**	**–**	**(1,332)**	(1,244)	(90)	(1,334)
Share of profits/(losses) in joint ventures and associates, net of interest and taxation	6(b), 13(a)	**52**	**1**	**53**	58	(2)	56
Group operating profit	5(b)	**1,485**	**105**	**1,590**	1,346	421	1,767
Investment income (i)	7	**26**	**–**	**26**	31	–	31
Financing costs (i)	7	**(129)**	**–**	**(129)**	(133)	–	(133)
Net finance cost		**(103)**	**–**	**(103)**	(102)	–	(102)
Profit before taxation		**1,382**	**105**	**1,487**	1,244	421	1,665
Taxation	8	**(649)**	**(19)**	**(668)**	(521)	(168)	(689)
Profit for the period		**733**	**86**	**819**	723	253	976
Earnings per ordinary share				Pence			Pence
Basic (i)	10			**15.8**			18.9
Diluted (i)	10			**15.7**			18.8
Interim dividend proposed/paid per ordinary share	9			**4.92**			4.62
Prior period final dividend paid per ordinary share	9			**11.78**			11.11

(i) See notes 3a) and 3b).

The notes on pages 27 to 43 form part of these condensed interim Financial Statements.

GROUP STATEMENT OF COMPREHENSIVE INCOME

Six months ended 30 June	2013 £m	2012 (restated) (i) £m
Profit for the period (i)	**819**	976
Other comprehensive (loss)/income		
Items that will be or have been recycled to the Group Income Statement:		
Gains on revaluation of available-for-sale securities	**–**	2
Taxation on revaluation of available-for-sale securities	**–**	4
	–	6
Gains/(losses) on cash flow hedges	**2**	(2)
Transferred to income and expense on cash flow hedges	**12**	42
Transferred to assets and liabilities on cash flow hedges	**(1)**	1
Exchange differences on cash flow hedges	**1**	6
Taxation on cash flow hedges	**(4)**	(12)
	10	35
Exchange differences on translation of foreign operations	**42**	(39)
Share of other comprehensive income/(loss) of joint ventures and associates, net of taxation	**12**	(7)
	64	(5)
Items that will not be recycled to the Group Income Statement:		
Net actuarial (losses)/gains on defined benefit pension schemes (i)	**(198)**	47
Taxation on net actuarial (losses)/gains on defined benefit pension schemes	**48**	(10)
	(150)	37
Share of other comprehensive loss of joint ventures and associates, net of taxation	**(15)**	(17)
Other comprehensive (loss)/income, net of taxation	**(101)**	15
Total comprehensive income for the period	**718**	991

(i) See notes 3a) and 3b).

The notes on pages 27 to 43 form part of these condensed interim Financial Statements.

GROUP STATEMENT OF CHANGES IN EQUITY

	Share capital £m	Share premium £m	Retained earnings £m	Accumulated other comprehensive income/(loss) £m	Other equity £m	**Total equity £m**
1 January 2013 (as previously reported)	321	929	4,511	(434)	600	5,927
Effect of adoption of IAS 19 (revised 2011) [i]	–	–	(325)	325	–	–
1 January 2013 (restated)	321	929	4,186	(109)	600	5,927
Total comprehensive income	–	–	819	(101)	–	**718**
Employee share schemes	–	2	(6)	–	35	**31**
Purchase of treasury shares	–	–	–	–	(213)	**(213)**
Dividends	–	–	(611)	–	–	**(611)**
Taxation	–	–	–	–	14	**14**
Exchange adjustments	–	–	–	–	(2)	**(2)**
30 June 2013	**321**	**931**	**4,388**	**(210)**	**434**	**5,864**

	Share capital £m	Share premium £m	Retained earnings £m	Accumulated other comprehensive income/(loss) £m	Other equity £m	**Total equity £m**
1 January 2012 (as previously reported)	319	874	4,043	(238)	602	5,600
Effect of adoption of IAS 19 (revised 2011) [i]	–	–	(297)	297	–	–
1 January 2012 (restated)	319	874	3,746	59	602	5,600
Total comprehensive income	–	–	976	15	–	991
Employee share schemes	1	44	13	–	(19)	39
Dividends	–	–	(576)	–	–	(576)
Taxation	–	–	–	–	5	5
Exchange adjustments	–	–	–	–	1	1
30 June 2012 (restated)	320	918	4,159	74	589	6,060

(i) See note 3a).

The notes on pages 27 to 43 form part of these condensed interim Financial Statements.

GROUP BALANCE SHEET

	Notes	30 June 2013 £m	31 December 2012 (restated) (i) £m
Non-current assets			
Goodwill		**2,603**	2,543
Other intangible assets		**1,723**	1,579
Property, plant and equipment		**7,934**	7,965
Interests in joint ventures and associates		**2,673**	2,721
Deferred tax assets		**212**	183
Trade and other receivables		**60**	55
Derivative financial instruments		**246**	313
Securities	11(a)	**200**	199
Retirement benefit assets	14(c)	**171**	254
		15,822	15,812
Current assets			
Inventories		**421**	545
Current tax assets		**56**	54
Trade and other receivables		**4,442**	4,335
Derivative financial instruments		**292**	268
Securities	11(a)	**11**	7
Cash and cash equivalents	11(a)	**800**	931
		6,022	6,140
Total assets		**21,844**	21,952
Current liabilities			
Trade and other payables		**(4,267)**	(4,545)
Current tax liabilities		**(605)**	(594)
Bank overdrafts, loans and other borrowings (i)	11	**(674)**	(566)
Derivative financial instruments		**(474)**	(615)
Provisions for other liabilities and charges		**(223)**	(266)
		(6,243)	(6,586)
Net current liabilities		**(221)**	(446)
Non-current liabilities			
Trade and other payables		**(127)**	(26)
Bank overdrafts, loans and other borrowings (i)	11	**(4,728)**	(4,762)
Derivative financial instruments		**(302)**	(327)
Deferred tax liabilities		**(1,882)**	(1,678)
Provisions for other liabilities and charges		**(2,456)**	(2,480)
Retirement benefit obligations	14(c)	**(242)**	(166)
		(9,737)	(9,439)
Net assets		**5,864**	5,927
Equity			
Share capital		**321**	321
Share premium		**931**	929
Retained earnings (i)		**4,388**	4,186
Accumulated other comprehensive loss (i)		**(210)**	(109)
Other equity		**434**	600
Total equity		**5,864**	5,927

(i) See notes 3a) and 3b).

The notes on pages 27 to 43 form part of these condensed interim Financial Statements.

GROUP CASH FLOW STATEMENT

Six months ended 30 June	Notes	2013 £m	2012 £m
Cash generated from operations	12	**1,944**	1,480
Income taxes paid		**(286)**	(181)
Petroleum revenue tax paid		**(115)**	(102)
Interest received		**–**	2
Payments relating to exceptional charges		**(132)**	(167)
Net cash flow from operating activities		**1,411**	1,032
Purchase of businesses net of cash and cash equivalents acquired		**(2)**	(74)
Sale of businesses net of cash and cash equivalents disposed of		**5**	27
Purchase of intangible assets	5(d)	**(174)**	(291)
Purchase of property, plant and equipment	5(d)	**(615)**	(1,109)
Disposal of property, plant and equipment and intangible assets		**6**	5
Investments in joint ventures and associates		**(34)**	(120)
Dividends received from joint ventures and associates		**103**	37
Repayments of loans to, and disposal of investments in, joint ventures and associates		**59**	36
Interest received		**11**	21
(Purchase)/sale of securities	11(a)	**(6)**	25
Net cash flow from investing activities		**(647)**	(1,443)
Issue of ordinary share capital		**2**	23
Purchase of treasury shares	10	**(203)**	–
Sale/(purchase) of own shares		**7**	(7)
Financing interest paid		**(116)**	(74)
Cash inflow from additional debt	11(a)	**72**	1,533
Cash outflow from payment of capital element of finance leases	11(a)	**(15)**	(14)
Cash outflow from repayment of other debt	11(a)	**(37)**	(15)
Net cash flow from increase in debt		**20**	1,504
Realised net foreign exchange gain on cash settlement of derivative contracts		**–**	13
Equity dividends paid		**(607)**	(571)
Net cash flow from financing activities		**(897)**	888
Net (decrease)/increase in cash and cash equivalents		**(133)**	477
Cash and cash equivalents at 1 January		**931**	479
Effect of foreign exchange rate changes		**2**	(2)
Cash and cash equivalents at 30 June		**800**	954
Included in the following lines of the Balance Sheet:			
Cash and cash equivalents	11(a)	**800**	995
Bank overdrafts, loans and other borrowings		**–**	(41)
		800	954

The notes on pages 27 to 43 form part of these condensed interim Financial Statements.

NOTES TO THE CONDENSED INTERIM FINANCIAL STATEMENTS

1. General information

Centrica plc is a Company domiciled and incorporated in the UK. The address of the registered office is Millstream, Maidenhead Road, Windsor, Berkshire, SL4 5GD. The Company has its listing on the London Stock Exchange.

These condensed interim Financial Statements for the six months ended 30 June 2013 were authorised for issue in accordance with a resolution of the Board of Directors on 31 July 2013. These condensed interim Financial Statements do not comprise statutory accounts within the meaning of Section 434 of the Companies Act 2006. Statutory accounts for the year ended 31 December 2012 were approved by the Board of Directors on 27 February 2013 and delivered to the Registrar of Companies. The report of the auditors on those accounts was unqualified, did not contain an emphasis of matter paragraph and did not contain any statement under Section 498 of the Companies Act 2006. The financial information contained in these condensed interim Financial Statements is unaudited. The Group Income Statement, Group Statement of Comprehensive Income, Group Statement of Changes in Equity and Group Cash Flow Statement for the interim period to 30 June 2013, and the Group Balance Sheet as at 30 June 2013 and related notes have been reviewed by the auditors and their report to the Company is set out on page 21.

2. Basis of preparation

These condensed interim Financial Statements for the six months ended 30 June 2013 have been prepared in accordance with the Disclosure and Transparency Rules of the Financial Conduct Authority and with IAS 34: 'Interim financial reporting', as adopted by the European Union. These condensed interim Financial Statements should be read in conjunction with the annual Financial Statements for the year ended 31 December 2012, which have been prepared in accordance with International Financial Reporting Standards as adopted by the European Union.

Preparation of interim statements requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expense. Actual amounts may differ from these estimates. In preparing these condensed interim Financial Statements, the significant judgements, estimates and assumptions made by management in applying the Group's accounting policies were the same as those applied in the annual Financial Statements for the year ended 31 December 2012.

After making enquiries, the Board has a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future. For this reason, the Board continues to adopt the going concern basis in preparing the condensed interim Financial Statements. Further details of the Group's liquidity position and going concern review are provided in note 4 of these condensed interim Financial Statements.

3. Accounting policies

The accounting policies applied in these condensed interim Financial Statements are consistent with those of the annual Financial Statements for the year ended 31 December 2012, as described in those annual Financial Statements, with the exception of standards, amendments and interpretations effective in 2013 and other presentational changes as detailed below. Taxes on income in the interim period are accrued using tax rates that would be applicable to expected total annual earnings for each relevant source of income.

(a) Standards, amendments and interpretations effective in 2013

(i) IAS 19 (revised)

IAS 19 (revised): 'Employee benefits' amends the accounting for employee benefits. The Group has applied the standard retrospectively in accordance with the transition provisions and the comparatives have been restated accordingly. The impact on the Group has been as follows:

- The standard replaces the interest cost on the defined benefit obligation and the expected return on plan assets with a net interest cost, based on the net defined benefit asset or liability and the discount rate, measured at the beginning of the year. This has increased the income statement charge with an equal and offsetting movement in other comprehensive income (actuarial gains and losses).
- Investment income has been reduced by £23 million for the six months ended 30 June 2013, reduced by £14 million for the six months ended 30 June 2012 and reduced by £26 million for the year ended 31 December 2012.
- Profit after tax has been reduced by £18 million for the six months ended 30 June 2013, reduced by £14 million for the six months ended 30 June 2012 and reduced by £28 million for the year ended 31 December 2012.
- As at 1 January 2012 and 1 January 2013, retained earnings have been reduced by £297million and £325 million respectively. The actuarial gains and losses reserve increased by the same amounts to reflect the retrospective application.
- Basic and diluted earnings per share ('EPS') have been reduced by 0.4 pence for the six months ended 30 June 2013 and by 0.2 pence for the six months ended 30 June 2012. For the year ended 31 December 2012 the effect was a reduction of 0.6 pence on basic and 0.5 pence on diluted EPS. The effect on adjusted basic and adjusted diluted EPS was to reduce EPS by 0.4 pence for the six months ended 30 June 2013 and by 0.2 pence for the six months ended 30 June 2012. For the year ended 31 December 2012 the effect was a reduction of 0.5 pence on adjusted basic and 0.6 pence on adjusted diluted EPS.

(ii) Amendment to IAS 1

'Amendment to IAS 1: Presentation of financial statements - Presentation of items of other comprehensive income'. The Group has applied this amendment retrospectively and the comparatives have been represented accordingly. Within the Group statement of comprehensive income, items are now separated into 'Items that will be or have been recycled to the Group Income Statement' and 'Items that will not be recycled to the Group Income Statement'.

NOTES TO THE CONDENSED INTERIM FINANCIAL STATEMENTS CONTINUED

3. Accounting policies continued

(iii) IFRS 10, 11 and 12

IFRS 10: 'Consolidated financial statements', IFRS 11: 'Joint arrangements', IFRS 12: 'Disclosures of interests in other entities', and subsequent revisions to IAS 27: 'Separate financial statements' and IAS 28: 'Investments in associates and joint ventures' are new and revised standards that are mandatory for adoption in 2014 for EU endorsed IFRS reporters. The Group has not yet adopted these standards in these interim statements but is continuing to assess the impact and whether it will early adopt in the full year financial statements for 2013.

(iv) IFRS 13

IFRS 13: 'Fair value measurement' has measurement and disclosure requirements that are applicable for the December 2013 year-end onwards. The Group has included the IFRS 13 (and IFRS 7) disclosures required by IAS 34 para 16a(j) in note 4.

There are no other IFRSs or IFRIC interpretations that are effective for the first time for the current financial period that have had a material impact on the Group.

(b) Other presentational changes

(i) Presentation of sales commissions and prepayment customer vending fees

Where there is a specific link to revenue generation, the Group has reclassified sales commissions paid to brokers or agents (or similar arrangements) and prepayment customer vending fees, from operating costs to cost of sales.

The effect has been to reduce operating costs and increase cost of sales by £87 million for the six months ended 30 June 2013, by £82 million for the six months ended 30 June 2012 and by £164 million for the 12 months ended 31 December 2012. The prior period comparatives have been restated accordingly.

(ii) Current/non-current classification of interest accruals

The Group has reclassified the interest accruals on bank overdrafts, loans and other borrowings from non-current liabilities to current liabilities because the amounts are due for payment within 12 months.

The effect has been to increase current liabilities and reduce non-current liabilities by £139 million as at 30 June 2013 and by £94 million as at 31 December 2012. The prior period comparatives have been restated accordingly.

(iii) Presentation of gains and losses on revaluations in financing costs

The Group has represented fair value gains and losses on its derivatives and hedges on a net basis within financing costs because it aids comparability with prior periods. Historically such gains and losses were recognised gross within financing costs and investment income.

The effect has been to reduce financing costs and reduce investment income by £190 million for the six months ended 30 June 2013, by £89 million for the six months ended 30 June 2012 and by £166 million for the 12 months ended 31 December 2012. The prior period comparatives have been restated accordingly.

(c) Centrica specific accounting measures

Use of adjusted profit measures

The Directors believe that reporting adjusted profit and adjusted earnings per share measures provides additional useful information on business performance and underlying trends. These measures are used for internal performance purposes. The adjusted measures in this report are not defined terms under IFRS and may not be comparable with similarly titled measures reported by other companies.

The measure of operating profit used by management to evaluate segment performance is adjusted operating profit. Adjusted operating profit is defined as operating profit before:

- exceptional items;
- certain re-measurements;
- depreciation resulting from fair value uplifts to property, plant and equipment (PP&E) on the acquisition of Strategic Investments;

but including:

- the Group's share of the results of joint ventures and associates before interest and taxation.

Note 5(b) contains an analysis of adjusted operating profit by segment and a reconciliation of adjusted operating profit to operating profit after exceptional items and certain re-measurements.

Adjusted earnings is defined as earnings before:

- exceptional items, net of taxation;
- certain re-measurements, net of taxation; and
- depreciation of fair value uplifts to PP&E on the acquisition of Strategic Investments, net of taxation.

A reconciliation of earnings is provided in note 10.

The Directors have determined that for Strategic Investments it is important to separately identify the earnings impact of increased depreciation arising from the acquisition-date fair value uplifts made to PP&E over their useful economic lives. As a result of the nature of fair value assessments in the energy industry the value attributed to strategic assets is a subjective judgement based on a wide range of complex variables at a point in time. The subsequent depreciation of the fair value uplifts bears little relationship to current market conditions, operational performance or underlying cash generation. Management therefore reports and monitors the operational performance of Strategic

NOTES TO THE CONDENSED INTERIM FINANCIAL STATEMENTS CONTINUED

3. Accounting policies continued

Investments before the impact of depreciation on fair value uplifts to PP&E and the segmental results are presented on a consistent basis. The Group has two Strategic Investments for which reported profits have been adjusted due to the impact of fair value uplifts. These Strategic Investments relate to the 2009 acquisitions of Venture Production plc ('Venture'), the operating results of which are included within the 'Centrica Energy – Gas' segment and of the 20% interest in Lake Acquisitions Limited ('British Energy'), which owned the British Energy Group, the results of which are included within the 'Centrica Energy – Power' segment.

(i) Venture

Significant adjustments have been made to the acquired PP&E to report the acquired oil and gas field interests at their acquisition-date fair values which are subsequently depreciated through the Group Income Statement over their respective useful economic lives using the unit of production method.

Whilst the impact of unwinding the PP&E at their acquisition-date fair values is included in overall reported profit for the period, the Directors have reversed the earnings impact of the increased depreciation and related taxation resulting from fair value uplifts to the acquired oil and gas interests in order to arrive at adjusted profit from operations after taxation.

(ii) British Energy

The 20% interest in British Energy is accounted for as an investment in an associate using the equity method. The Group reports its share of the associate's profit or loss, which is net of interest and taxation, within the Group Income Statement.

The most significant fair value adjustments arising on the acquisition of the 20% investment in British Energy relate to the fair value uplifts made to the British Energy nuclear power stations to report the PP&E at their acquisition-date fair values and fair value uplifts made to British Energy's energy procurement contracts and energy sales contracts to report these at their acquisition-date fair values.

Whilst the impact of increased depreciation and related taxation through unwinding the fair value uplifts to the nuclear power stations is included in the share of associate's post-acquisition result within the overall reported Group profit for the period, the Directors have reversed these impacts in arriving at adjusted profit from operations for the period. The impact of unwinding the acquisition-date fair values attributable to the acquired energy procurement and energy sales contracts is included within certain re-measurements.

Exceptional items and certain re-measurements

The Group reflects its underlying financial results in the 'business performance' column of the Group Income Statement. To be able to provide readers with this clear and consistent presentation, the effects of 'certain re-measurements' of financial instruments, and 'exceptional items', are reported separately in a different column in the Group Income Statement and are separately identified in segmental note 5(b).

The Group is an integrated energy business. This means that it utilises its knowledge and experience across the gas and power (and related commodity) value chains to make profits across the core markets in which it operates. As part of this strategy, the Group enters into a number of forward energy trades to protect and optimise the value of its underlying production, generation, storage and transportation assets (and similar capacity or off-take contracts), as well as to meet the future needs of our customers (downstream demand). These trades are designed to reduce the risk of holding such assets, contracts or downstream demand and are subject to strict risk limits and controls.

Primarily because some of these trades include terms that permit net settlement (i.e. they are prohibited from being designated as 'own use'), the rules within IAS 39: 'Financial instruments' require them to be individually fair valued. Fair value movements on these commodity derivative trades do not reflect the underlying performance of the business because they are economically related to our upstream assets, capacity/off-take contracts or downstream demand, which are typically not fair valued. Therefore, these certain re-measurements are reported separately and are subsequently reflected in business performance when the underlying transaction or asset impacts profit or loss.

The arrangements discussed above and reflected as certain re-measurements are all managed separately from proprietary energy trading activities where trades are entered into speculatively for the purpose of making profits in their own right. These proprietary trades are included in the business performance column (i.e. in the results before certain re-measurements).

Exceptional items are those items which are of a non-recurring nature and, in the judgement of the Directors, need to be disclosed separately by virtue of their nature, size or incidence. Again, to ensure the business performance column reflects the underlying results of the Group, these exceptional items are also reported in a separate column in the Group Income Statement. Items which may be considered exceptional in nature include disposals of businesses, business restructurings, significant onerous contract charges and asset write-downs.

Disposals of equity stakes in wind farm developments

The Group's wind farm strategy is to realise value, share risk and reduce our capital requirements as individual projects develop, which may include bringing in partners at an appropriate stage. Profits and losses arising on disposal of equity stakes in these developments are reported within the 'business performance' column as part of the 'Centrica Energy – Power' segment.

(d) Update to critical accounting judgements in applying the Group's accounting policies

Energy Company Obligation

The Energy Company Obligation ('ECO') order requires UK-licensed energy suppliers to improve the energy efficiency of domestic households from 1 January 2013. Targets are set in proportion to the size of historic customer bases and must be delivered by 31 March 2015. The Group continues to judge that it is not legally obligated by this order until 31 March 2015. Accordingly, the costs of delivery are recognised as incurred, when cash is spent or unilateral commitments made resulting in obligations that cannot be avoided. During the period, the Group has entered into a number of contractual arrangements and commitments, and issued a public statement to underline its commitment, to deliver a specific proportion of the ECO requirements. Consequently, the Group's result includes the costs of these contractual arrangement and commitment obligations.

NOTES TO THE CONDENSED INTERIM FINANCIAL STATEMENTS CONTINUED

4. Risk management and financial instruments

(a) Risk management

During the period financial risk management was overseen by the Group Financial Risk Management Committee (GFRMC) according to objectives, targets and policies set by the Board. Commodity price risk management is carried out in accordance with individual business unit Financial Risk Management Committees and their respective financial risk management policies, as approved by the GFRMC under delegated authority of the Board. The Financing & Treasury policy, which includes management of currency risk, interest rate risk, equity price risk and liquidity risk, is approved by the Board. The wholesale credit risks associated with commodity trading and treasury positions are managed in accordance with the Group's credit risk policy. Downstream credit risk management is carried out in accordance with individual business unit credit policies.

(i) Commodity price risk management

During the six months ended 30 June 2013, the Group continued to be exposed to commodity price risk in its upstream assets, energy procurement contracts, downstream and proprietary energy trading activities. Specific limits are used to manage the exposure to commodity prices associated with the Group's activities to an acceptable level. Volumetric limits are supported by Profit at Risk (PaR) and Value at Risk (VaR) metrics in the UK and in North America to measure the Group's exposure to commodity price risk. Limits are also set on PaR and VaR measurements as a further control over exposure to market prices.

The Group measures and manages the commodity price risk associated with the Group's entire energy procurement, upstream and downstream portfolio. Only certain of the Group's energy procurement, upstream and downstream contracts constitute financial instruments under IAS 39.

The net gain of £105 million from operations during the six months ended 30 June 2013 (six months ended 30 June 2012: £511 million) on the re-measurement of energy contracts included within Group operating profit largely represents the unwinding of mark-to-market positions created by gas and power purchase contracts which were priced above the current wholesale market value of energy at the start of the period, partially offset by the impact of wholesale market price movements during the period. These balance sheet mark-to-market positions are calculated with reference to forward energy prices and therefore the extent of the economic gain or loss arising over the life of these contracts is uncertain, and entirely dependent upon the level of future wholesale energy prices. Generally, subject to short-term balancing, the ultimate net charge to cost of sales will be consistent with the price of energy agreed in these contracts and the fair value adjustments will reverse as the energy is supplied over the life of the contract.

(ii) Credit risk management

During the six months ended 30 June 2013, counterparty credit exposure issues remained a focal point within Centrica and the Group continues to be vigilant in managing counterparty risks in accordance with its approved financial risk management policies. The economic environment continues to impact the markets in which the Group is active, however the Group has not altered its rating thresholds for counterparty credit limits and continues to operate within its limits. In the US and UK, there is a continuing emphasis on understanding the impact of regulatory changes which may result in an increase in trading over exchanges or via zero threshold margined contracts. This helps to reduce counterparty credit risk, but carries increased liquidity requirements.

(iii) Liquidity risk management and going concern

The Group has a number of treasury and risk policies to monitor and manage liquidity risk. Cash forecasts identifying the Group's liquidity requirements are produced regularly and are stress-tested for different scenarios, including, but not limited to, reasonably possible increases or decreases in commodity prices and the potential cash implications of a credit rating downgrade. The Group seeks to ensure that sufficient financial headroom exists for at least a 12-month period to safeguard the Group's ability to continue as a going concern. It is the Group's policy to maintain committed facilities and/or available surplus cash resources of at least £1,200 million, to raise at least 75% of its net debt (excluding non-recourse debt) in the long-term debt market and to maintain an average term to maturity in the recourse long-term debt portfolio greater than five years.

At 30 June 2013, the Group held £800 million (31 December 2012: £931 million) of cash and cash equivalents and had undrawn committed credit facilities of £3,444 million (31 December 2012: £3,029 million). 123% (31 December 2012: 130%) of the Group's net debt has been raised in the long-term debt market and the average term to maturity of the long-term debt portfolio was 12.3 years (31 December 2012: 12.6 years). The Group's high level of available cash resources and undrawn committed bank borrowing facilities has enabled the Directors to conclude that the Group has sufficient headroom to continue as a going concern.

The Group holds cash as collateral against counterparty balances and also pledges cash as collateral, principally under margin calls, to cover exposure to mark-to-market positions on certain wholesale commodity contracts. Generally, cash paid or received as collateral is interest-bearing and is free from any restriction over its use by the holder.

The table below summarises the cash collateral balances and associated movements for the Group's businesses:

	2013 £m	2012 £m
Cash pledged as collateral at 1 January	**(102)**	(219)
Net cash (outflow)/inflow	**(2)**	132
Foreign exchange movements	**(6)**	3
Cash pledged as collateral at 30 June	**(110)**	(84)

Also during the period, the Group pledged £29 million of non-current securities as collateral against an index-linked swap maturing on 16 April 2020.

NOTES TO THE CONDENSED INTERIM FINANCIAL STATEMENTS CONTINUED

4. Risk Management and financial instruments continued

(b) Financial instruments

(i) Fair value of financial assets and liabilities held at fair value

Financial assets and financial liabilities measured and held at fair value are classified into one of three categories, known as hierarchy levels, which are defined according to the inputs used to measure fair value as follows:

- Level 1: Fair value is determined using observable inputs that reflect unadjusted quoted market prices for identical assets and liabilities.
- Level 2: Fair value is determined using significant inputs that may be directly observable inputs or unobservable inputs that are corroborated by market data.
- Level 3: Fair value is determined using significant unobservable inputs that are not corroborated by market data and may be used with internally developed methodologies that result in management's best estimate of fair value.

30 June 2013	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Financial assets				
Derivative financial instruments:				
Energy derivatives	37	231	48	316
Interest rate derivatives	–	167	–	167
Foreign exchange derivatives	–	55	–	55
Treasury gilts designated at fair value through profit or loss	128	–	–	128
Debt instruments	62	–	2	64
Equity instruments	13	–	6	19
Total financial assets	**240**	**453**	**56**	**749**
Financial liabilities				
Derivative financial instruments:				
Energy derivatives	(42)	(469)	(114)	(625)
Interest rate derivatives	–	(34)	–	(34)
Foreign exchange derivatives	–	(117)	–	(117)
Total financial liabilities	**(42)**	**(620)**	**(114)**	**(776)**

There were no significant transfers between Level 1 and Level 2 during the period. The reconciliation of the Level 3 fair value measurements during the period is as follows:

	Financial assets £m	2013 Financial liabilities £m
Level 3 financial instruments		
1 January	**147**	**(157)**
Total realised and unrealised (losses)/gains recognised in Income Statement	**(65)**	**37**
Transfers from Level 3 to Level 2	**(26)**	**6**
30 June	**56**	**(114)**
Total (losses)/gains for the period recognised within certain re-measurements for Level 3 financial instruments held at the end of the reporting period [(i)]	**(55)**	**37**

(i) No gains or losses were recognised in other comprehensive income during the period.

The Group's policy is to recognise transfers in and transfers out of fair value hierarchy levels as of the date of the event or change in circumstances that caused the transfer. The transfers from Level 3 to Level 2 occur when the commodity market prices used in the valuation move from being internally derived to being quoted in an active market.

(ii) Valuation techniques used to derive Level 2 and 3 fair values and Group valuation processes

Level 2 interest rate derivatives and foreign exchange derivatives comprise interest rate swaps and forward foreign exchange contracts. Interest rate swaps are fair valued using forward interest rates extracted from observable yield curves. Forward foreign exchange contracts are fair valued using forward exchange rates that are quoted in an active market.

Level 2 energy derivatives are fair valued by comparing and discounting the difference between the expected contractual cashflows for the relevant commodities and the quoted prices for those commodities in an active market.

For Level 3 energy derivatives, the main input used by the Group pertains to deriving expected future commodity prices in markets that are not active as far into the future as some of our contractual terms. Fair values are then calculated by comparing and discounting the difference between the expected contractual cash flows and these derived future prices.

NOTES TO THE CONDENSED INTERIM FINANCIAL STATEMENTS CONTINUED

4. Risk Management and financial instruments continued

Because the Level 3 energy derivative valuations involve the prediction of future commodity market prices, sometimes a long way into the future, reasonably possible alternative assumptions for gas, power, coal, emissions or oil prices may result in a higher or lower fair value for Level 3 financial instruments. Given the relative size of these fair values, it is unlikely that the impact of these reasonably possible changes would be significant when judged in relation to the Group's profit and loss or total asset value.

It should be noted that the fair values disclosed in the tables above only concern those contracts entered into which are within the scope of IAS 39. The Group has numerous other commodity contracts which are outside of the scope of IAS 39 and are not fair valued. The Group's actual exposure to market rates is constantly changing as the Group's portfolio of energy contracts changes.

The Group's valuation process includes specific teams of individuals that perform valuations of the Group's derivatives for financial reporting purposes, including Level 3 valuations. The Group has an independent team that derives future commodity price curves based on available external data and these prices feed in to the energy derivative valuations. The price curves are subject to review and approval by the Group's Investment Sub-Committee and valuations of all derivatives, together with other contracts that are not within the scope of IAS 39, are also reviewed regularly as part of the overall risk management process.

(iii) Fair value of financial assets and liabilities held at amortised cost

The carrying value of the Group's financial assets and liabilities measured at amortised cost are approximately equal to their fair value except as listed below:

	30 June 2013 Carrying value £m	30 June 2013 Fair value £m	31 December 2012 (restated) (i) Carrying value £m	31 December 2012 (restated) (i) Fair value £m
Bank overdrafts and loans	**(358)**	**(390)**	(367)	(388)
Bonds	**(4,463)**	**(4,930)**	(4,483)	(5,119)
Obligations under finance leases	**(284)**	**(315)**	(299)	(337)

(i) See note 3b).

5. Segmental analysis

(a) Revenue

Six months ended 30 June	2013 Gross segment revenue £m	2013 Less inter-segment revenue £m	2013 Group revenue £m	2012 (restated) (i) Gross segment revenue £m	2012 (restated) (i) Less inter-segment revenue £m	2012 (restated) (i) Group revenue £m
International Downstream						
Residential energy supply	**5,486**	**–**	**5,486**	4,807	–	4,807
Residential services	**805**	**(68)**	**737**	811	(56)	755
Business energy supply and services	**1,621**	**(2)**	**1,619**	1,589	(5)	1,584
British Gas	**7,912**	**(70)**	**7,842**	7,207	(61)	7,146
Residential energy supply	**1,308**	**–**	**1,308**	1,210	–	1,210
Business energy supply (i)	**1,609**	**(22)**	**1,587**	1,300	(16)	1,284
Residential and business services	**274**	**–**	**274**	253	–	253
Direct Energy	**3,191**	**(22)**	**3,169**	2,763	(16)	2,747
International Upstream						
Gas (i)	**2,448**	**(411)**	**2,037**	1,825	(286)	1,539
Power	**666**	**(151)**	**515**	640	(171)	469
Centrica Energy	**3,114**	**(562)**	**2,552**	2,465	(457)	2,008
Centrica Storage	**107**	**(19)**	**88**	91	(15)	76
	14,324	**(673)**	**13,651**	12,526	(549)	11,977

(i) On 27 February 2013 the Group announced a new organisational structure. To reflect this structure and to align with management reporting, the North American Upstream Gas business has been reallocated from the 'Direct Energy - Upstream and wholesale energy' segment to the 'Centrica Energy – Gas' segment and the North American Power and Midstream & Trading businesses have been reallocated from the 'Direct Energy - Upstream and wholesale energy' segment to the 'Direct Energy – Business energy supply' segment. Prior period comparatives have been restated accordingly.

NOTES TO THE CONDENSED INTERIM FINANCIAL STATEMENTS CONTINUED

5. Segmental analysis continued

(b) Operating profit

Six months ended 30 June	2013 £m	2012 (restated) (i) £m
International Downstream		
Residential energy supply	**356**	345
Residential services	**135**	125
Business energy supply and services	**78**	93
British Gas	**569**	563
Residential energy supply	**99**	101
Business energy supply (i)	**53**	43
Residential and business services	**13**	11
Direct Energy	**165**	155
International Upstream		
Gas (i) (ii)	**683**	519
Power (ii)	**119**	174
Centrica Energy	**802**	693
Centrica Storage	**47**	36
Adjusted operating profit – segment operating profit before exceptional items, certain re-measurements and impact of fair value uplifts from Strategic Investments (iii)	**1,583**	1,447
Share of joint ventures/associates' interest and taxation	**(47)**	(49)
Depreciation of fair value uplifts to property, plant and equipment – Venture (ii)	**(27)**	(37)
Depreciation of fair value uplifts to property, plant and equipment, net of taxation – associates – British Energy (ii)	**(24)**	(15)
	1,485	1,346
Exceptional items (note 6a)	**–**	(90)
Certain re-measurements included within gross profit (note 6b)	**104**	513
Certain re-measurements of associates' energy contracts, net of taxation (note 6b)	**1**	(2)
Operating profit after exceptional items and certain re-measurements	**1,590**	1,767

(i) On 27 February 2013 the Group announced a new organisational structure. To reflect this structure and to align with management reporting, the North American Upstream Gas business has been reallocated from the 'Direct Energy - Upstream and wholesale energy' segment to the 'Centrica Energy – Gas' segment and the North American Power and Midstream & Trading businesses have been reallocated from the 'Direct Energy - Upstream and wholesale energy' segment to the 'Direct Energy – Business energy supply' segment. Prior period comparatives have been restated accordingly.
(ii) See note 3 and note 10 for an explanation of the depreciation on fair value uplifts to PP&E on acquiring Strategic Investments.
(iii) Includes results of equity-accounted interests before interest and taxation.

NOTES TO THE CONDENSED INTERIM FINANCIAL STATEMENTS CONTINUED

5. Segmental analysis continued

(c) Included within adjusted operating profit

Six months ended 30 June	Share of results of joint ventures and associates before interest and taxation 2013 £m	2012 £m	Depreciation and impairments of property, plant and equipment 2013 £m	2012 £m	Amortisation, write-downs and impairments of intangibles 2013 £m	2012 £m
International Downstream						
Residential energy supply	**–**	–	**8**	4	**25**	14
Residential services	**–**	–	**11**	8	**4**	3
Business energy supply and services	**–**	–	**1**	1	**3**	4
British Gas	**–**	–	**20**	13	**32**	21
Residential energy supply	**–**	–	**–**	1	**12**	11
Business energy supply	**–**	–	**10**	9	**7**	4
Residential and business services	**–**	–	**1**	1	**3**	3
Direct Energy	**–**	–	**11**	11	**22**	18
International Upstream						
Gas (ii) (iii)	**–**	–	**446**	281	**38**	12
Power (i) (iii)	**123**	122	**48**	55	**1**	1
Centrica Energy	**123**	122	**494**	336	**39**	13
Centrica Storage	**–**	–	**15**	15	**–**	–
Other (iv)	**–**	–	**9**	11	**10**	10
	123	122	**549**	386	**103**	62

(i) The share of results of joint ventures and associates is before interest, certain re-measurements, depreciation of fair value uplifts to PP&E on Strategic Investments and taxation.
(ii) During the period, £30 million (2012: £7 million) of write downs relating to exploration and evaluation assets were incurred.
(iii) Depreciation of PP&E is stated before depreciation of fair value uplifts for Strategic Investments.
(iv) Other comprises Corporate Centre assets which are charged out to other Group segments.

NOTES TO THE CONDENSED INTERIM FINANCIAL STATEMENTS CONTINUED

5. Segmental analysis continued

(d) Capital expenditure

Six months ended 30 June	Capital expenditure on property, plant and equipment 2013 £m	Capital expenditure on property, plant and equipment 2012 (restated) (i) £m	Capital expenditure on intangible assets other than goodwill 2013 £m	Capital expenditure on intangible assets other than goodwill 2012 (restated) (i) £m
International Downstream				
Residential energy supply	**10**	4	**159**	101
Residential services	**18**	9	**5**	4
Business energy supply and services	**–**	2	**10**	6
British Gas	**28**	15	**174**	111
Residential energy supply	**1**	–	**3**	2
Business energy supply (i)	**9**	4	**24**	13
Residential and business services	**1**	1	**–**	1
Direct Energy	**11**	5	**27**	16
International Upstream				
Gas (i) (ii)	**434**	1,196	**69**	210
Power	**8**	52	**2**	1
Centrica Energy	**442**	1,248	**71**	211
Centrica Storage	**17**	35	**2**	–
Other	**5**	3	**21**	23
Capital expenditure	**503**	1,306	**295**	361
Increase/(decrease) in prepayments related to capital expenditure	**7**	(4)	**–**	–
Capitalised borrowing costs	**(23)**	(26)	**(4)**	–
Decrease/(increase) in payables related to capital expenditure	**128**	(167)	**29**	3
Purchases of emissions allowances and renewable obligations certificates (iii)	**–**	–	**(146)**	(73)
Net cash outflow	**615**	1,109	**174**	291

(i) On 27 February 2013 the Group announced a new organisational structure. To reflect this structure and to align with management reporting, the North American Upstream Gas business has been reallocated from the 'Direct Energy - Upstream and wholesale energy' segment to the 'Centrica Energy – Gas' segment and the North American Power and Midstream & Trading businesses have been reallocated from the 'Direct Energy - Upstream and wholesale energy' segment to the 'Direct Energy – Business energy supply' segment. Prior period comparatives have been restated accordingly.
(ii) During the six months ended 30 June 2012, £1,048 million of assets were acquired from Statoil, ConocoPhillips and Total.
(iii) These purchases are included within operating cash flows.

NOTES TO THE CONDENSED INTERIM FINANCIAL STATEMENTS CONTINUED

6. Exceptional items and certain re-measurements

(a) Exceptional items

Six months ended 30 June	2013 £m	2012 £m
Restructuring charges	–	(90)
Exceptional items included within operating profit	–	(90)
Taxation on exceptional items	–	24
Net exceptional items after taxation	–	(66)

(b) Certain re-measurements

Six months ended 30 June	2013 £m	2012 £m
Certain re-measurements recognised in relation to energy contracts (note 3):		
Net gains arising on delivery of contracts	**291**	491
Net (losses)/gains arising on market price movements and new contracts	**(187)**	22
Net re-measurements included within gross profit	**104**	513
Net gains/(losses) arising on re-measurement of associates' energy contracts, net of taxation	**1**	(2)
Net re-measurements included within operating profit	**105**	511
Taxation on certain re-measurements	**(19)**	(192)
Net re-measurements after taxation	**86**	319

7. Net finance cost

Six months ended 30 June	2013 Financing costs £m	2013 Investment income £m	2013 Total £m	2012 (restated) (i) Financing costs £m	2012 (restated) (i) Investment income £m	2012 (restated) (i) Total £m
Cost of servicing net debt						
Interest income	**–**	**20**	**20**	–	19	19
Interest cost on bonds, bank loans and overdrafts	**(119)**	**–**	**(119)**	(114)	–	(114)
Interest cost on finance leases	**(9)**	**–**	**(9)**	(9)	–	(9)
	(128)	**20**	**(108)**	(123)	19	(104)
Net gains/(losses) on revaluation (ii)	**4**	**–**	**4**	(6)	–	(6)
Notional interest arising from discounting and other interest	**(32)**	**6**	**(26)**	(30)	12	(18)
	(156)	**26**	**(130)**	(159)	31	(128)
Capitalised borrowing costs (iii)	**27**	**–**	**27**	26	–	26
(Cost)/income	**(129)**	**26**	**(103)**	(133)	31	(102)

(i) See notes 3a) and 3b).
(ii) Includes (a) gains and losses on fair value hedges, (b) movements in fair value of other derivatives primarily used to hedge foreign exchange exposure associated with inter-company loans and (c) foreign currency gains and losses arising primarily from retranslating those inter-company loans.
(iii) Borrowing costs have been capitalised using an average rate of 4.65% (2012: 4.72%).

NOTES TO THE CONDENSED INTERIM FINANCIAL STATEMENTS CONTINUED

8. Taxation

Analysis of tax charge

Six months ended 30 June	Business performance £m	Exceptional items and certain re-measurements £m	2013 Results for the period £m	Business performance £m	Exceptional items and certain re-measurements £m	2012 Results for the period £m
The tax charge comprises:						
UK corporation tax (i)	**(278)**	**(23)**	**(301)**	(287)	(122)	(409)
UK petroleum revenue tax	**(96)**	**–**	**(96)**	(97)	–	(97)
Foreign tax (i)	**(275)**	**4**	**(271)**	(137)	(46)	(183)
Total tax on profit (ii)	**(649)**	**(19)**	**(668)**	(521)	(168)	(689)

(i) Including adjustments in respect of prior periods.
(ii) Taxation on profit excludes taxation on the Group's share of results of joint ventures and associates.

The Group's effective tax rate before exceptional items and certain re-measurements was 47% for the six months to 30 June 2013 (2012: 42%).

9. Dividends

	£m	Pence per share	2013 Date of payment	£m	Pence per share	2012 Date of payment
Prior year final dividend	**611**	**11.78**	**12 June 2013**	576	11.11	13 Jun 2012

An interim dividend of 4.92 pence (2012: 4.62 pence) per ordinary share, totalling £256 million (2012: £240 million), will be paid on 13 November 2013 (14 November 2012) to shareholders on the register on 27 September 2013.

10. Earnings per ordinary share

Basic earnings per ordinary share has been calculated by dividing the earnings attributable to equity holders of the Company for the period of £819 million (2012: £976 million) by the weighted average number of ordinary shares in issue during the period of 5,181 million (2012: 5,174 million). The number of shares excludes 19 million ordinary shares (2012: 6 million), being the weighted average number of the Company's own shares held in the employee share trust or purchased by the Group as part of the share repurchase programme. The Directors believe that the presentation of adjusted basic earnings per ordinary share, being the basic earnings per ordinary share adjusted for certain re-measurements, exceptional items and the impact of depreciation relating to fair value uplifts attributed to Strategic Investments on acquisition, assists with understanding the underlying performance of the Group, as explained in note 3.

During the period, the Group purchased 57.5 million ordinary shares of $6^{14}/_{81}$ pence each, representing 1% of the called up share capital as at 30 June 2013 at an average price of £3.68 per share for a total consideration including expenses of £213 million (of which £10 million was unpaid at 30 June 2013). The shares were purchased as part of the £500 million share repurchase programme announced on 4 February 2013 to return surplus capital to shareholders, following the decision not to proceed with nuclear new build investment. These shares are held as treasury shares once purchased.

The reconciliation of basic to adjusted basic earnings per ordinary share is as follows:

Six months ended 30 June	2013 £m	2013 Pence per ordinary share	2012 (restated) (i) £m	2012 (restated) (i) Pence per ordinary share
Earnings – basic (i)	**819**	**15.8**	976	18.9
Net exceptional items after taxation (notes 3 and 6a)	**–**	**–**	66	1.3
Certain re-measurement gains after taxation (notes 3 and 6b)	**(86)**	**(1.7)**	(319)	(6.2)
Depreciation of fair value uplifts to property, plant and equipment from Strategic Investments, after taxation	**34**	**0.7**	30	0.6
Earnings – adjusted basic (i)	**767**	**14.8**	753	14.6
Earnings – diluted (i)	**819**	**15.7**	976	18.8
Earnings – adjusted diluted (i)	**767**	**14.7**	753	14.5

(i) See note 3a).

Certain re-measurements included within operating profit comprise re-measurements arising on energy trading activities described in note 3. All other re-measurements are included within results before exceptional items and certain re-measurements.

NOTES TO THE CONDENSED INTERIM FINANCIAL STATEMENTS CONTINUED

10. Earnings per ordinary share continued

Strategic Investments

During 2009, the Group acquired a 20% interest in British Energy and the entire share capital of Venture. As explained in note 3c), the depreciation relating to fair value uplifts of the acquired Venture property, plant and equipment and associated taxation is excluded in arriving at adjusted earnings for the period, which amounted to £27 million (six months ended 30 June 2012: £37 million) depreciation and a taxation credit of £17 million (six months ended 30 June 2012: £22 million) in the period. Additionally, the impact of depreciation arising on fair value uplifts attributed to the British Energy nuclear power stations and related taxation included within the Group's share of the post-tax results of the associate is excluded in arriving at adjusted earnings for the period, which amounted to £24 million (six months ended 30 June 2012: £15 million) net of taxation.

11. Sources of finance

At 30 June 2013, the Group's long-term credit rating was A3 stable outlook for Moody's Investors Service Limited (31 December 2012: A3 stable outlook) and A- stable outlook for Standard & Poor's Credit Market Services Europe Limited (31 December 2012: A- stable outlook).

The Group monitors its current and projected capital position on a regular basis, considering a medium-term view of three to five years, and different stress case scenarios, including the impact of changes in the Group's credit ratings and significant movements in commodity prices. A number of financial ratios are monitored, including those used by the credit rating agencies, such as debt to cash flow ratios and EBITDA to gross interest expense. The Group's capital structure is managed against these ratios as required to maintain strong credit ratings.

British Gas Insurance Limited (BGIL) is required under PRA (Prudential Regulation Authority) regulations to hold a minimum capital amount and has complied with this requirement in 2013 (and 2012). For the Group as a whole, the level of debt that can be raised is restricted by the Company's Articles of Association. As at 30 June 2013, net debt is limited to the greater of £5.0 billion and a gearing ratio of three times adjusted capital and reserves. This restriction can be amended or removed by the shareholders of the Company passing a special resolution.

(a) Net debt summary

	Cash and cash equivalents (ii) £m	Current and non-current Securities £m	Current and non-current borrowings £m	Derivatives £m	**Net debt £m**
1 January 2013	931	206	(5,328)	144	**(4,047)**
Cash outflow from purchase of securities	(6)	6	–	–	**–**
Cash inflow from additional debt	72	–	(72)	–	**–**
Cash outflow from payment of capital element of finance leases	(15)	–	15	–	**–**
Cash outflow from repayment of other debt	(37)	–	37	–	**–**
Net cash outflow increasing net debt	(147)	–	–	–	**(147)**
Revaluation	–	(2)	42	(41)	**(1)**
(Increase)/decrease in interest payable	–	–	(44)	37	**(7)**
Exchange adjustments	2	1	(52)	–	**(49)**
30 June 2013	800	211	(5,402)	140	**(4,251)**

	Cash and cash equivalents (ii) £m	Current and non-current Securities £m	Current and non-current borrowings £m	Derivatives £m	Net debt (restated) (i) £m
1 January 2012	518	218	(4,171)	143	(3,292)
Cash inflow from net sale of securities	25	(25)	–	–	–
Cash inflow from additional debt	1,533	–	(1,533)	–	–
Cash outflow from payment of capital element of finance leases	(14)	–	14	–	–
Cash outflow from repayment of other debt	(15)	–	15	–	–
Net cash outflow increasing net debt	(1,052)	–	–	–	(1,052)
Revaluation	–	3	(2)	5	6
(Decrease)/increase in interest payable	–	–	(73)	44	(29)
Acquisitions	–	5	–	–	5
Exchange adjustments	(2)	1	15	–	14
Other non-cash movements	2	–	5	–	7
30 June 2012	995	202	(5,730)	192	(4,341)

(i) To align with management reporting, net debt has been restated to include mark-to-market values on derivative financial instruments used to hedge offsetting changes in borrowings.

(ii) Cash and cash equivalents includes £220 million (31 December 2012: £201 million) cash at bank, in transit and in hand and £580 million (31 December 2012: £730 million) short-term deposits.

NOTES TO THE CONDENSED INTERIM FINANCIAL STATEMENTS CONTINUED

11. Sources of finance continued

(b) Borrowings summary

	Coupon rate %	Principal m	30 June 2013 Current £m	30 June 2013 Non-current £m	30 June 2013 Total £m	31 December 2012 (restated) (i) Current £m	31 December 2012 (restated) (i) Non-current £m	31 December 2012 (restated) (i) Total £m
Bank overdrafts and loans			**30**	**328**	**358**	31	336	367
Bonds (by maturity date):								
27 February 2013	1.045	¥3,000	**–**	**–**	**–**	22	–	22
9 December 2013	7.125	€367	**317**	**–**	**317**	304	–	304
4 November 2014	Floating	$100	**–**	**66**	**66**	–	61	61
10 December 2014	5.125	£315	**–**	**327**	**327**	–	331	331
31 March 2015	Floating	$70	**–**	**46**	**46**	–	43	43
24 October 2016	5.500	£300	**–**	**328**	**328**	–	334	334
19 September 2018	7.000	£400	**–**	**456**	**456**	–	471	471
1 February 2019	3.213	€100	**–**	**85**	**85**	–	81	81
22 February 2022	3.680	HK$450	**–**	**38**	**38**	–	36	36
10 March 2022	6.375	£500	**–**	**500**	**500**	–	501	501
4 September 2026	6.400	£200	**–**	**216**	**216**	–	224	224
16 April 2027	5.900	$70	**–**	**46**	**46**	–	43	43
13 March 2029	4.375	£750	**–**	**740**	**740**	–	740	740
5 January 2032 (ii)	Zero	€50	**–**	**47**	**47**	–	41	41
19 September 2033	7.000	£770	**–**	**762**	**762**	–	762	762
12 September 2044	4.250	£500	**–**	**489**	**489**	–	489	489
			317	**4,146**	**4,463**	326	4,157	4,483
Commercial paper			**156**	**–**	**156**	82	–	82
Obligations under finance leases			**30**	**254**	**284**	30	269	299
Interest accruals (i)			**141**	**–**	**141**	97	–	97
			674	**4,728**	**5,402**	566	4,762	5,328

(i) See note 3b).
(ii) €50 million of zero coupon notes have an accrual yield of 4.200%, which will result in a €114 million repayment on maturity.

12. Note to the Group Cash Flow Statement

Reconciliation of Group operating profit to cash generated from operations

Six months ended 30 June	2013 £m	2012 £m
Group operating profit including share of result of joint ventures and associates	**1,590**	1,767
Less share of profit of joint ventures and associates	**(53)**	(56)
Group operating profit before share of results of joint ventures and associates	**1,537**	1,711
Add back/(deduct):		
Amortisation, write-down and impairment of intangible assets	**103**	64
Depreciation, write-down and impairment of property, plant and equipment	**576**	423
Profit on sale of businesses, property, plant and equipment and other intangible assets	**(30)**	(43)
(Decrease)/increase in provisions	**(27)**	48
Defined benefit pension service cost	**58**	45
Defined benefit pension contributions	**(61)**	(52)
Employee share scheme costs	**23**	23
Re-measurement of energy contracts (i)	**(121)**	(538)
Operating cash flows before movements in working capital	**2,058**	1,681
Decrease/(increase) in inventories	**149**	(57)
(Increase)/decrease in trade and other receivables (ii)	**(36)**	127
Decrease in trade and other payables (ii)	**(227)**	(271)
Cash generated from operations	**1,944**	1,480

(i) Adds back unrealised gains arising from re-measurement of energy contracts.
(ii) Includes net outflow of £2 million of cash collateral in 2013 (2012: £132 million inflow).

NOTES TO THE CONDENSED INTERIM FINANCIAL STATEMENTS CONTINUED

13. Interests in joint ventures and associates

The Group's share of results of joint ventures and associates for the six months ended 30 June 2013 principally arises from its interests in the following entities (all reported in the 'Centrica Energy – Power' segment):

- Wind farms – Braes of Doune Wind Farm (Scotland) Limited (see note 16), Barrow Offshore Wind Limited, GLID Wind Farms TopCo Limited, Lincs Wind Farm Limited and Celtic Array Limited ('Round 3'); and
- Nuclear – Lake Acquisitions Limited ('British Energy').

(a) Share of results of joint ventures and associates

Six months ended 30 June	Joint ventures Wind farms £m	Associates Nuclear £m	2013 Total £m	2012 Total £m
Income	26	304	**330**	309
Expenses excluding certain re-measurements (i)	(25)	(213)	**(238)**	(221)
Certain re-measurements	–	1	**1**	(2)
Interest expense	(12)	(11)	**(23)**	(24)
Taxation excluding certain re-measurements (i)	–	(17)	**(17)**	(6)
Share of post-taxation results of joint ventures and associates (i)	(11)	64	**53**	56

(i) Includes £31 million (2012: £34 million) relating to depreciation of fair value uplifts to property, plant and equipment on acquiring the British Energy investment. The associated tax impact is £7 million credit (2012: £19 million credit).

British Energy

The Group's share of profit arising from its investment in British Energy for the period, as set out in the table above includes the effect of unwinding the fair value adjustments. As explained in note 3 the depreciation, net of taxation, arising on fair value uplifts attributed to the nuclear power stations is reversed in arriving at adjusted profit for the period as shown in the reconciliation table below and as set out in notes 5(b) and 10.

(b) Reconciliation of share of results of joint ventures and associates to share of adjusted results of joint ventures and associates

Six months ended 30 June	Joint ventures Wind farms £m	Associates Nuclear £m	2013 Total £m	2012 Total £m
Share of post-taxation results of joint ventures and associates	(11)	64	**53**	56
Certain re-measurements, net of taxation	–	(1)	**(1)**	2
Depreciation – British Energy, net of taxation (i)	–	24	**24**	15
Interest expense	12	11	**23**	24
Taxation (excluding certain re-measurements and British Energy depreciation)	–	24	**24**	25
Share of adjusted results of joint ventures and associates	1	122	**123**	122

(i) Relates to depreciation of fair value uplifts to PP&E on acquiring the British Energy investments.

14. Pensions

(a) Summary of main defined benefit schemes

Name of scheme	Section	Status	Funding/tax status	Country
Centrica Engineers Pension Scheme	Final salary section	Closed to new members	Funded/tax-registered	UK
	Career average section	Open to new members	Funded/tax-registered	UK
Centrica Pension Plan	Management section	Closed to new members	Funded/tax-registered	UK
	2008 section	Closed to new members	Funded/tax-registered	UK
Centrica Pension Scheme	Final salary section	Closed to new members	Funded/tax-registered	UK
	Career average section	Closed to new members	Funded/tax-registered	UK
Direct Energy Marketing Limited Pension Plan		Closed to new members	Funded/tax-registered	Canada

The Centrica Pension Scheme also has a defined contribution section which is open to new members. The Centrica Engineers Pension Scheme, Centrica Pension Plan and Centrica Pension Scheme form the majority of the Group's defined benefit obligation and are referred to below as the 'Registered Pension Schemes'.

The latest full actuarial valuations have been updated to 30 June 2013 for the purposes of meeting the requirements of IAS 19. The Group has applied IAS 19 (revised): 'Employee benefits' retrospectively in accordance with the transition provisions of that standard. See note 3.

Based on the latest triennial valuation at 31 March 2012, the Group and the trustees of the Registered Pension Schemes agreed to fund the scheduled deficit payments using asset-backed contribution arrangements. Under the arrangements, certain loans to UK Group companies were transferred to Scottish Limited Partnerships established by the Group. During the period the Group made special contributions to the Registered Pension Schemes of £360 million (31 December 2012: £84 million); the schemes immediately used these contributions to

NOTES TO THE CONDENSED INTERIM FINANCIAL STATEMENTS CONTINUED

14. Pensions continued

acquire interests in the partnerships for their fair value of £360 million (31 December 2012: £84 million). The schemes' total partnership interests now entitle them to distributions from the income of the partnerships over a period of between 4 and 15 years. Over the next 4 years this income will amount to £77 million per annum but will reduce thereafter. The partnerships are controlled by Centrica and their results are consolidated by the Group. As the trustees' interests in the partnerships do not meet the definition of a plan asset under IAS 19, they are not reflected in the Balance Sheet. Distributions from the partnerships to the schemes will be recognised as scheme assets in the future as they occur. A continuing charge over the Humber power station provides additional security for the trustees.

Deficit payments are also being made in respect of the Direct Energy Marketing Limited Pension Plan in Canada. £7 million per annum is to be paid from 2013 to 2016 and £3 million in 2017.

(b) Accounting assumptions

The accounting assumptions for the Registered Pension Schemes have been given below.

Major assumptions used for the actuarial valuation

	30 June 2013 %	31 December 2012 %
Rate of increase in employee earnings:		
Subject to cap	**1.7**	1.7
Other	**3.6**	3.2
Rate of increase in pensions in payment	**3.6**	3.2
Rate of increase in deferred pensions:		
In line with CPI capped at 2.5%	**2.5**	2.5
In line with RPI	**3.6**	3.2
Discount rate	**4.9**	4.8

Longevity assumptions remain unchanged from 31 December 2012.

(c) Amounts included in the Balance Sheet

	30 June 2013 £m	31 December 2012 £m
Fair value of plan assets	**5,412**	5,133
Present value of defined benefit obligation	**(5,483)**	(5,045)
Net (liability)/asset recognised in the Balance Sheet	**(71)**	88
Pension (liability)/asset presented in the Balance Sheet as:		
Retirement benefit assets	**171**	254
Retirement benefit liabilities	**(242)**	(166)
Net pension (liability)/asset	**(71)**	88

Included within the Balance Sheet within non-current securities are £64 million (31 December 2012: £61 million) of investments, held in trust on behalf of the Group, as security in respect of the Centrica Unfunded Pension Scheme. Included within the pension scheme liabilities above are £41 million (31 December 2012: £37 million) relating to this scheme.

15. Business combinations and asset purchases

Business combinations

Business combinations completed by the Group during the period are immaterial both individually and in aggregate to the Group's condensed interim Financial Statements.

Canadian upstream

On 15 April 2013, the Group announced that it had agreed to form a partnership with Qatar Petroleum International and jointly acquire a package of producing conventional natural gas and crude oil assets and associated infrastructure located in the Western Canadian Sedimentary Basin from Suncor Energy for approximately C$1 billion (£650 million). The Group will own a 60% share in the partnership and operate the assets. The transaction is expected to complete in the third quarter of 2013.

2012 Business Combinations – fair value updates

During the period, there have been no updates to the fair value entries posted in relation to acquisitions which occurred in 2012.

Asset purchases

UK shale gas

On 13 June 2013, the Group acquired a 25% interest in the Bowland exploration licence in Lancashire from Cuadrilla Resources Ltd and AJ Lucas Group Ltd for £44 million in cash. The Group will also potentially pay exploration and appraisal costs of up to £56 million, including a carry arrangement. Following the exploration and appraisal phase, if the Group elects to continue into the development phase, a further contingent consideration of £60 million will become payable.

NOTES TO THE CONDENSED INTERIM FINANCIAL STATEMENTS CONTINUED

16. Disposals

On 18 March 2013, the Group legally disposed of its 20% investment in NNB Holding Company Limited ('Nuclear New Build').

On 7 June 2013, the Group disposed of its 50% interest in the Braes of Doune wind farm, which resulted in a profit on disposal of £29 million.

17. Commitments and contingencies

(a) Commitments

The Group has commitments relating primarily to the acquisition of property, plant and equipment and intangible assets, commodity purchase contracts, LNG capacity and transportation capacity. There have been no significant changes to these commitments during the period.

On 25 March 2013, the Group announced that it had entered into a 20 year agreement with Cheniere to purchase 89bcf per annum of LNG volumes for export from the Sabine Pass liquefaction plant in Louisiana in the United States, subject to a number of project milestones and regulatory approvals being achieved. Under the terms of the agreement and subject to these approvals, the Group will make commodity purchases and capacity payments of up to £10 billion based on current gas prices. The target date for first commercial delivery is September 2018.

(b) Contingent liabilities

There are no material contingent liabilities.

18. Related party transactions

During the period, the Group entered into the following arms length transactions with related parties who are not members of the Group and had the following associated balances:

Six months ended 30 June			2013			2012
	Sale of goods and services £m	**Purchase of goods and services £m**	**Other transactions (i) £m**	Sale of goods and services £m	Purchase of goods and services £m	Other transactions (i) £m
Joint ventures:						
Wind farms (as defined in note 13)	**13**	**(42)**	**(3)**	12	(34)	(63)
Associates:						
Nuclear (as defined in note 13)	**27**	**(301)**	**103**	94	(281)	30
Other	**1**	**(3)**	**–**	14	(1)	1
	41	**(346)**	**100**	120	(316)	(32)

(i) Other transactions relate to investment and funding transactions with joint ventures and associates. In 2013 a dividend of £103 million was received from Lake Acquisitions Limited (2012: £35 million).

		30 June 2013		31 December 2012
	Amounts owed from £m	**Amounts owed to £m**	Amounts owed from £m	Amounts owed to £m
Joint ventures:				
Wind farms (as defined in note 13)	**468**	**42**	459	47
Associates:				
Nuclear (as defined in note 13)	**–**	**43**	8	73
Other	**18**	**–**	18	–
	486	**85**	485	120

During the period, there were no material changes to commitments in relation to joint ventures and associates. No provision for bad or doubtful debts relating to amounts owed from related parties was required in any of the periods disclosed above.

19. Seasonality of operations

Certain activities of the Group are affected by weather and temperature conditions. As a result of this, amounts reported for the six months ended 30 June 2013 may not be indicative of the amounts that would be reported for a full year due to the impact of weather on, and seasonal fluctuations in, customer demand for gas, electricity and services, market changes in commodity prices and changes in retail tariffs. Customer demand for gas in the UK and North America is driven primarily by heating load and is generally higher in the winter than in the summer, and higher from January to June than from July to December. Customer demand for electricity in the UK generally follows a similar pattern to gas, but the variation is less pronounced. Customer demand for electricity in North America is also more stable than gas but is driven by heating load in the winter and cooling load in the summer. Generally demand for electricity in North America is higher in the winter and summer than it is in the spring and autumn, and higher from July to December than it is from January to June.

Customer demand for home services in the UK is generally higher in the winter than it is in the summer, and higher in the earlier part of the winter reflecting greater heating system break downs, so that customer demand from July to December is higher than from January to June. Customer demand for home services in North America follows a similar pattern, but is also higher in the summer as a result of residential new construction in the US and the servicing of cooling systems.

Gas production volumes in the UK are generally higher in the winter when gas prices are higher. Gas production volumes are generally higher from January to June than they are from July to December as outages are generally planned for the summer months when gas demand and prices are lower. Gas production volumes in North America are generally not seasonal.

NOTES TO THE CONDENSED INTERIM FINANCIAL STATEMENTS CONTINUED

19. Seasonality of operations continued

Power generation volumes are dependent on spark spread prices, which is the difference between the price of electricity and the price of gas multiplied by a conversion rate and, as a result, are not as seasonal as gas production volumes in the UK, as wholesale prices for both gas and electricity are generally higher in the winter than they are in the summer. Power generation volumes in North America are generally higher in the summer than in the winter and can be higher or lower from January to June compared to July to December. The impact of seasonality on customer demand and wholesale prices has a direct effect on the Group's financial performance and cash flows.

20. Events after the balance sheet date

Dividends

An interim dividend of 4.92 pence (2012: 4.62 pence) per ordinary share, totalling £256 million, will be paid on 13 November 2013 to shareholders on the register on 27 September 2013.

Acquisitions

Bounce

On 12 July 2013 the Group announced that it had acquired the privately-owned Texas-based electricity retailer Bounce Energy ('Bounce') for $46 million (£30 million) in cash plus additional working capital.

Hess' Energy Marketing business

On 30 July 2013, the Group announced that it had agreed to acquire the New Jersey-based energy marketing business of Hess Corporation for $731 million (£478 million) in cash plus net working capital, estimated at approximately $300 million. The transaction is subject to regulatory approval and is expected to close later in 2013.

The Finance Act 2013

On 2 July 2013, the UK government substantively enacted The Finance Act 2013 which included reductions in the main UK corporation tax rate to 20% by 1 April 2015. The impact of the rate changes to taxation balances as at 30 June 2013 is estimated to be a reduction to net deferred taxation liabilities of £57 million.

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF CENTRICA PLC

We have audited the Group Financial Statements of Centrica plc for the year ended 31 December 2012 which comprise the Group Income Statement, the Group Statement of Comprehensive Income, the Group Statement of Changes in Equity, the Group Balance Sheet, the Group Cash Flow Statement and the related notes and supplementary information. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRS) as adopted by the European Union (EU).

Respective responsibilities of Directors and Auditors

As explained more fully in the Directors' Responsibility Statement set out on page 60, the Directors are responsible for the preparation of the Group Financial Statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the Group Financial Statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the Company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

Scope of the audit of the Financial Statements

An audit involves obtaining evidence about the amounts and disclosures in the Financial Statements sufficient to give reasonable assurance that the Financial Statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Group's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Directors; and the overall presentation of the Financial Statements. In addition, we read all the financial and non-financial information in the Annual Report and Accounts to identify material inconsistencies with the audited Financial Statements. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Opinion on Financial Statements

In our opinion the Group Financial Statements:

- give a true and fair view of the state of the Group's affairs as at 31 December 2012 and of its profit and cash flows for the year then ended;
- have been properly prepared in accordance with IFRS as adopted by the EU; and
- have been prepared in accordance with the requirements of the Companies Act 2006 and Article 4 of the IAS Regulations.

Opinion on the other matter prescribed by the Companies Act 2006

In our opinion the information given in the Directors' Report for the financial year for which the Group Financial Statements are prepared is consistent with the Group Financial Statements.

Matters on which we are required to report by exception

We have nothing to report in respect of the following:

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- certain disclosures of Directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

Under the Listing Rules we are required to review:

- the Directors' statement, set out on page 60 in relation to going concern;
- the part of the Corporate Governance Statement relating to the Company's compliance with the nine provisions of the UK Corporate Governance Code specified for our review; and
- certain elements of the report to shareholders by the Board on Directors' remuneration.

Other matter

We have reported separately on the parent Company Financial Statements of Centrica plc for the year ended 31 December 2012 and on the information in the Remuneration Report that is described as having been audited.

Charles Bowman

Charles Bowman
Senior Statutory Auditor
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
London
27 February 2013

Financial Statements

GROUP INCOME STATEMENT

Year ended 31 December	Notes	2012 Business performance £m	2012 Exceptional items and certain re-measurements £m	2012 Results for the year £m	2011 Business performance £m	2011 Exceptional items and certain re-measurements £m	2011 Results for the year £m
Group revenue	4(a)	**23,942**	**–**	**23,942**	22,824	–	22,824
Cost of sales before exceptional items and certain re-measurements	5	**(18,676)**	**–**	**(18,676)**	(17,959)	–	(17,959)
Exceptional items	7	**–**	**(89)**	**(89)**	–	(221)	(221)
Re-measurement of energy contracts	7	**–**	**603**	**603**	–	(437)	(437)
Cost of sales	5	**(18,676)**	**514**	**(18,162)**	(17,959)	(658)	(18,617)
Gross profit		**5,266**	**514**	**5,780**	4,865	(658)	4,207
Operating costs before exceptional items	5	**(2,844)**	**–**	**(2,844)**	(2,750)	–	(2,750)
Exceptional items	7	**–**	**(445)**	**(445)**	–	(110)	(110)
Operating costs	5	**(2,844)**	**(445)**	**(3,289)**	(2,750)	(110)	(2,860)
Share of profits/(losses) in joint ventures and associates, net of interest and taxation	7, 16	**140**	**(6)**	**134**	93	(26)	67
Group operating profit	4(b)	**2,562**	**63**	**2,625**	2,208	(794)	1,414
Interest income	8	**254**	**–**	**254**	212	–	212
Interest expense	8	**(437)**	**–**	**(437)**	(358)	–	(358)
Net interest expense		**(183)**	**–**	**(183)**	(146)	–	(146)
Profit from continuing operations before taxation		**2,379**	**63**	**2,442**	2,062	(794)	1,268
Taxation on profit from continuing operations	9	**(1,029)**	**(140)**	**(1,169)**	(810)	(16)	(826)
Profit from continuing operations after taxation		**1,350**	**(77)**	**1,273**	1,252	(810)	442
Profit from discontinued operations	7	**–**	**–**	**–**	13	22	35
Loss on disposal of discontinued operations	7, 31	**–**	**–**	**–**	–	(56)	(56)
Discontinued operations		**–**	**–**	**–**	13	(34)	(21)
Profit for the year		**1,350**	**(77)**	**1,273**	1,265	(844)	421

Earnings per ordinary share	Notes	2012 Pence	2011 Pence
From continuing and discontinued operations:			
Basic	11	**24.6**	8.2
Diluted	11	**24.4**	8.1
From continuing operations:			
Basic	11	**24.6**	8.6
Diluted	11	**24.4**	8.5
Interim dividend paid per ordinary share	10	**4.62**	4.29
Final dividend proposed per ordinary share	10	**11.78**	11.11

The notes on pages 82 to 134 form part of these Financial Statements.

GROUP STATEMENT OF COMPREHENSIVE INCOME

Year ended 31 December	Notes	2012 £m	2011 £m
Profit for the year		**1,273**	421
Other comprehensive (loss)/income:			
Transfer of available-for-sale reserve to Income Statement	27	**–**	23
Gains/(losses) on revaluation of available-for-sale securities	27	**7**	(4)
Taxation on revaluation of available-for-sale securities	27	**(2)**	(2)
		5	17
Net losses on cash flow hedges	27	**(27)**	(99)
Transferred to income and expense on cash flow hedges	27	**108**	42
Transferred to assets and liabilities on cash flow hedges	27	**(1)**	2
Exchange differences on translation of cash flow hedges in foreign operations	27	**1**	(3)
Taxation on cash flow hedges	27	**(20)**	23
		61	(35)
Exchange differences on translation of foreign operations	27	**(44)**	(12)
Recycling of foreign exchange loss on disposal of business	27	**–**	(3)
		(44)	(15)
Net actuarial (losses)/gains on defined benefit pension schemes	27	**(319)**	198
Taxation on net actuarial (losses)/gains on defined benefit pension schemes	27	**69**	(59)
		(250)	139
Share of other comprehensive income of joint ventures and associates, net of taxation	27	**32**	(25)
Other comprehensive (loss)/income net of taxation		**(196)**	81
Total comprehensive income for the year		**1,077**	502

GROUP STATEMENT OF CHANGES IN EQUITY

	Share capital (note 26) £m	Share premium £m	Retained earnings £m	Accumulated other comprehensive (loss)/income (note 27) £m	Other equity (note 28) £m	**Total equity £m**
1 January 2011	318	833	4,386	(319)	601	5,819
Total comprehensive income	–	–	421	81	–	502
Employee share schemes	1	41	5	–	10	57
Dividends	–	–	(762)	–	–	(762)
Purchase of non-controlling interest	–	–	(7)	–	–	(7)
Taxation	–	–	–	–	(8)	(8)
Exchange adjustments	–	–	–	–	(1)	(1)
31 December 2011	319	874	4,043	(238)	602	5,600
Total comprehensive income	–	–	1,273	(196)	–	**1,077**
Employee share schemes	2	55	11	–	(2)	**66**
Dividends	–	–	(816)	–	–	**(816)**
Taxation	–	–	–	–	(1)	**(1)**
Exchange adjustments	–	–	–	–	1	**1**
31 December 2012	**321**	**929**	**4,511**	**(434)**	**600**	**5,927**

The notes on pages 82 to 134 form part of these Financial Statements.

Financial Statements

GROUP BALANCE SHEET

31 December	Notes	2012 £m	2011 £m
Non-current assets			
Goodwill	14	**2,543**	2,518
Other intangible assets	14	**1,579**	1,221
Property, plant and equipment	15	**7,965**	6,412
Interests in joint ventures and associates	16	**2,721**	2,620
Deferred tax assets	22	**183**	235
Trade and other receivables	18	**55**	74
Derivative financial instruments	19	**313**	290
Securities	12	**199**	190
Retirement benefit assets	29	**254**	413
		15,812	13,973
Current assets			
Inventories	17	**545**	442
Current tax assets		**54**	81
Trade and other receivables	18	**4,335**	4,212
Derivative financial instruments	19	**268**	315
Securities	12	**7**	28
Cash and cash equivalents	12	**931**	518
		6,140	5,596
Total assets		**21,952**	19,569
Current liabilities			
Trade and other payables	21	**(4,545)**	(4,094)
Current tax liabilities		**(594)**	(226)
Bank overdrafts, loans and other borrowings	12	**(472)**	(502)
Derivative financial instruments	19	**(615)**	(1,140)
Provisions for other liabilities and charges	23	**(266)**	(308)
		(6,492)	(6,270)
Net current liabilities		**(352)**	(674)
Non-current liabilities			
Trade and other payables	21	**(26)**	(33)
Bank overdrafts, loans and other borrowings	12	**(4,856)**	(3,669)
Derivative financial instruments	19	**(327)**	(505)
Deferred tax liabilities	22	**(1,678)**	(1,506)
Provisions for other liabilities and charges	23	**(2,480)**	(1,903)
Retirement benefit obligations	29	**(166)**	(83)
		(9,533)	(7,699)
Net assets		**5,927**	5,600
Equity			
Share capital	26	**321**	319
Share premium		**929**	874
Retained earnings		**4,511**	4,043
Accumulated other comprehensive loss	27	**(434)**	(238)
Other equity	28	**600**	602
Total equity		**5,927**	5,600

The Financial Statements on pages 78 to 134 were approved and authorised for issue by the Board of Directors on 27 February 2013 and were signed below on its behalf by:

Sam Laidlaw
Chief Executive

Nick Luff
Group Finance Director

The notes on pages 82 to 134 form part of these Financial Statements.

GROUP CASH FLOW STATEMENT

Year ended 31 December	Notes	2012 £m	2011 £m
Cash generated from continuing operations	13(a)	**3,605**	3,229
Income taxes paid	13(d)	**(332)**	(430)
Petroleum revenue tax paid	13(d)	**(192)**	(262)
Interest received		**6**	20
Interest paid		**(1)**	(3)
Payments relating to exceptional charges		**(266)**	(194)
Net cash flow from continuing operating activities		**2,820**	2,360
Net cash flow from discontinued operating activities		**–**	(23)
Net cash flow from operating activities		**2,820**	2,337
Purchase of businesses net of cash and cash equivalents acquired		**(155)**	(394)
Sale of businesses net of cash and cash equivalents disposed of		**30**	78
Purchase of intangible assets	4(e),13(c)	**(572)**	(299)
Purchase of property, plant and equipment	4(e)	**(1,795)**	(765)
Disposal of property, plant and equipment and intangible assets		**14**	6
Investments in joint ventures and associates		**(291)**	(236)
Dividends received from joint ventures and associates	16(a)	**110**	147
Repayments of loans to, and disposal of investments in, joint ventures and associates	16(a)	**42**	10
Interest received		**33**	6
Sale of securities	13(b)	**26**	48
Net cash flow from continuing investing activities		**(2,558)**	(1,399)
Net cash flow from discontinued investing activities		**–**	(1)
Net cash flow from investing activities		**(2,558)**	(1,400)
Issue of ordinary share capital	26	**33**	23
Purchase of own shares		**(9)**	(6)
Financing interest received		**46**	9
Financing interest paid		**(256)**	(202)
Cash inflow from additional debt		**1,712**	114
Cash outflow from payment of capital element of finance leases		**(31)**	(25)
Cash outflow from repayment of other debt		**(471)**	(30)
Cash outflow from settlement of derivative contracts related to borrowings		**(14)**	–
Net cash flow from increase in debt	13(b)	**1,196**	59
Realised net foreign exchange loss on cash settlement of derivative contracts		**(5)**	(28)
Equity dividends paid		**(815)**	(762)
Net cash flow from continuing financing activities		**190**	(907)
Net increase in cash and cash equivalents		**452**	30
Cash and cash equivalents at 1 January		**479**	451
Effect of foreign exchange rate changes		**–**	(2)
Cash and cash equivalents at 31 December		**931**	479
Included in the following lines of the Balance Sheet:			
Cash and cash equivalents	12(b)	**931**	518
Bank overdrafts, loans and other borrowings		**–**	(39)
		931	479

The notes on pages 82 to 134 form part of these Financial Statements.

NOTES TO THE FINANCIAL STATEMENTS

1. Summary of significant new accounting policies and reporting changes

The principal accounting policies applied in the preparation of these consolidated Financial Statements are set out below and in the Supplementary Information (note S2). These policies have been consistently applied to the years presented.

Basis of preparation

The consolidated Financial Statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union (EU) and therefore comply with Article 4 of the EU IAS Regulation and the Companies Act 2006.

The consolidated Financial Statements have been prepared on the historical cost basis, except for derivative financial instruments, available-for-sale financial assets, financial instruments designated as at fair value through profit or loss on initial recognition, and the assets of the Group's pension schemes that have been measured at fair value; and the liabilities of the Group's pension schemes that are measured using the projected unit credit valuation method. The carrying values of recognised assets and liabilities that are hedged items in fair value hedges, and are otherwise carried at cost, are adjusted to record changes in the fair values attributable to the risks that are being hedged.

The preparation of Financial Statements in conformity with IFRS as adopted by the EU requires the use of certain critical accounting estimates. It requires management to exercise its judgement in the processes of applying the Group's accounting policies. The areas involving a higher degree of judgement, complexity or areas where assumptions and estimates are significant to the consolidated Financial Statements are described in notes 2 and 3.

(a) Standards, amendments and interpretations effective in 2012

There are no IFRSs or IFRIC interpretations that are effective for the first time for the current financial year that have had a material impact on the Group.

(b) Standards, amendments and interpretations that are issued but not yet applied by the Group

The standards and amendments to standards that are issued but not yet applied which could have an impact on the Group's future Financial Statements are: IFRS 9, 10, 11, 12, 13 and amendments to IAS 19. These standards and amendments to standards have an effective date after the date of these Financial Statements and the Group has not early adopted them. IAS 19 (revised 2011) will apply for the year ended 31 December 2013 and will change the way interest is calculated on pension scheme assets and liabilities. If this standard had been applied to the year ended 31 December 2012, it is estimated that interest income would have been reduced by approximately £26 million. The Group is continuing to assess the impact that the other standards and amendments to standards may have.

2. Centrica specific accounting measures

Use of adjusted profit measures

The Directors believe that reporting adjusted profit and adjusted earnings per share measures provides additional useful information on business performance and underlying trends. These measures are used for internal performance purposes. The adjusted measures in this report are not defined terms under IFRS and may not be comparable with similarly titled measures reported by other companies.

The measure of operating profit used by management to evaluate segment performance is adjusted operating profit. Adjusted operating profit is defined as operating profit before:

- exceptional items;
- certain re-measurements;
- depreciation resulting from fair value uplifts to property, plant and equipment (PP&E) on the acquisition of Strategic Investments;

but including:

- the Group's share of the results from joint ventures and associates before interest and taxation.

Note 4 contains an analysis of adjusted operating profit by segment and a reconciliation of adjusted operating profit to operating profit after exceptional items and certain re-measurements.

Adjusted earnings is defined as earnings before:

- exceptional items net of taxation;
- certain re-measurements net of taxation; and
- depreciation of fair value uplifts to PP&E on the acquisition of Strategic Investments, net of taxation.

A reconciliation of earnings is provided in note 11.

The Directors have determined that for Strategic Investments it is important to separately identify the earnings impact of increased depreciation arising from the acquisition-date fair value uplifts made to PP&E over their useful economic lives. As a result of the nature of fair value assessments in the energy industry the value attributed to strategic assets is a subjective judgement based on a wide range of complex variables at a point in time. The subsequent depreciation of the fair value uplifts bears little relationship to current market conditions, operational performance or underlying cash generation. Management therefore reports and monitors the operational performance of Strategic Investments before the impact of depreciation on fair value uplifts to PP&E and the segmental results are presented on a consistent basis.

The Group has two Strategic Investments for which reported profits have been adjusted due to the impact of fair value uplifts. These Strategic Investments relate to the 2009 acquisitions of Venture Production plc ('Venture') the operating results of which are included within the Centrica Energy – Gas segment and the acquisition of the 20% interest in Lake Acquisitions Limited ('British Energy'), which owned the British Energy Group, the results of which are included within the Centrica Energy – Power segment.

(i) Venture

Significant adjustments have been made to the acquired PP&E to report the acquired oil and gas field interests at their acquisition-date fair values which are subsequently depreciated through the Group Income Statement over their respective useful economic lives using the unit of production method.

Whilst the impact of unwinding the PP&E at their acquisition-date fair values is included in overall reported profit for the year, the Directors have reversed the earnings impact of the increased depreciation and related taxation resulting from fair value uplifts to the acquired oil and gas interests in order to arrive at adjusted profit from continuing operations after taxation.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

2. Centrica specific accounting measures continued

(ii) British Energy

The 20% interest in British Energy is accounted for as an investment in an associate using the equity method. The Group reports its share of the associate's profit or loss, which is net of interest and taxation, within the Group Income Statement.

The most significant fair value adjustments arising on the acquisition of the 20% investment in British Energy relate to the fair value uplifts made to the British Energy nuclear power stations to report the PP&E at their acquisition-date fair values and fair value uplifts made to British Energy's energy procurement contracts and energy sales contracts to report these at their acquisition-date fair values.

Whilst the impact of increased depreciation and related taxation through unwinding the fair value uplifts to the nuclear power stations is included in the share of associate's post-acquisition result included in overall reported Group profit for the year, the Directors have reversed these impacts in arriving at adjusted profit from continuing operations for the year. The impact of unwinding the acquisition-date fair values attributable to the acquired energy procurement and energy sales contracts is included within certain re-measurements.

Exceptional items and certain re-measurements

The Group reflects its underlying financial results in the 'business performance' column of the Group Income Statement. To be able to provide readers with this clear and consistent presentation, the effects of 'certain re-measurements' of financial instruments, and 'exceptional items', are reported separately in a different column in the Group Income Statement.

In our business we enter into a portfolio of forward energy contracts which include buying substantial quantities of commodity to meet the future needs of our customers. Primarily because these contracts include terms that permit net settlement, the rules within IAS 39 require the contracts to be individually fair valued. In addition, the Group also enters into a range of commodity contracts designed to secure the value of its underlying production, generation, storage and transportation assets, consistent with an integrated energy business in the UK and North America. Fair value movements on these commodity derivative contracts do not reflect the underlying performance of the business because the contracts are economically related to our upstream assets or downstream demand in our chosen markets, which are typically not fair valued. Therefore, these certain re-measurements are reported separately and are subsequently reflected in business performance when the underlying transaction or asset impacts profit or loss.

Exceptional items are those items which are of a non-recurring nature and, in the judgement of the Directors, need to be disclosed separately by virtue of their nature, size or incidence. Again, to ensure the business performance column reflects the underlying results of the Group, these exceptional items are also reported in a separate column in the Group Income Statement. Items which may be considered exceptional in nature include disposals of businesses, business restructurings, significant onerous contract charges and asset write-downs. See note S2 for a more detailed explanation of the accounting treatment for exceptional items and certain re-measurements.

3. Critical accounting judgements and key sources of estimation uncertainty

(a) Critical judgements in applying the Group's accounting policies

The Group's accounting policies as set out in note S2 and Notes to the Financial Statements include descriptions of judgements management has made in applying the Group's accounting policies. Areas of judgement that have the most significant effect on the amounts recognised in the Financial Statements (apart from those involving estimations which are dealt with below) include the following:

- the presentation of selected items as exceptional, see notes 2, 7 and S2;
- the use of adjusted profit and adjusted earnings per share measures, see notes 2, 4 and 11; and
- the classification of energy procurement contracts as derivative financial instruments and presentation as certain re-measurements, see notes 2, 7 and 19.

In addition, management has made the following key judgements in applying the Group's accounting policies that have the most significant effect on the Group's Financial Statements:

Wind farm partial disposals

In recent years, the Group has disposed of 50% of the equity voting capital (and 50% of the shareholder loans where relevant) in wind farm companies, for example, GLID Wind Farms TopCo Limited, Lincs Wind Farm Limited and Celtic Array Limited ('Round 3').

Associated with certain of these disposals, the Group contracted to purchase a large percentage of the output produced by the wind farms under arm's length, 15-year, offtake agreements. The Group also contracted to provide management, operational and transitional support services to these companies as directed by their boards (and shareholders). Shareholders' agreements were put in place which included a number of reserved matters and provide for joint management of the major decisions of the companies.

Accordingly, the Directors have judged that the disposal of equity voting share capital (and shareholder loans) was a loss of control over the financial and operating policies of the companies. Therefore, the remaining investments are equity accounted as investments in joint ventures (see note 16). The Directors have also judged that the 15-year offtake agreements are not leasing arrangements. This is because the Group is not purchasing substantially all of the economic output of the wind farms. These contracts are considered to be outside the scope of IAS 39 apart from the embedded derivatives arising from the pricing terms which are marked to market separately.

For the Celtic Array Limited ('Round 3') disposal which occurred during the year, profits arising on disposal of the equity interest are recognised within the 'business performance' column, in line with the Group's established business model of bringing in partners as wind farm projects develop in order to realise value, share risk and reduce our capital requirements.

Leases – third-party power station tolling arrangements

The Group has two long-term power station tolling contracts: (i) Spalding in the UK and (ii) Rijnmond in the Netherlands. The arrangements provide Centrica with the right to nominate 100% of the plant output for the duration of the contracts in return for a mix of capacity payments and operating payments based on plant availability.

The Spalding contract runs until 2021 and Centrica holds an option to extend the tolling arrangement for a further eight years, exercisable by 30 September 2020. If extended, Centrica is granted an option to purchase the station at the end of this further period. The Directors have judged that the arrangement should be accounted for as a finance lease as the lease term is judged to be substantially all of the economic life of the power station and the present value

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

3. Critical accounting judgements and key sources of estimation uncertainty continued

of the minimum lease payments at inception date of the arrangement amounted to substantially all of the fair value of the power station at that time.

Details of the interest charges, finance lease payable and finance lease asset are included in notes 8, 12 and 15 respectively.

The Rijnmond contract runs until 2030 and Centrica does not have the right to extend the agreement or any option to purchase the plant. The Directors have judged that the arrangement should be accounted for as an operating lease as the lease term is not judged to be substantially all of the economic life of the power station and the present value of the minimum lease payments at the inception date of the arrangement did not amount to substantially all of the fair value of the power station at that time. Details of the operating lease disclosures are included in note 33.

Business combinations and asset acquisitions

Business combinations and acquisitions of associates and joint ventures require a fair value exercise to be undertaken to allocate the purchase price (cost) to the fair value of the acquired identifiable assets, liabilities and contingent liabilities.

As a result of the nature of fair value assessments in the energy industry this purchase price allocation exercise requires subjective judgements based on a wide range of complex variables at a point in time. Management uses all available information to make the fair value determinations.

During the year the Group has acquired a number of producing and development oil and gas assets. The Group has determined that these acquisitions take the form of asset purchases rather than business combinations as they constitute the purchase of jointly controlled assets governed by joint operating agreements and as such do not give the Group control of the businesses. Business combinations and asset acquisitions are set out in note 30.

Energy Company Obligation

The Energy Company Obligation ('ECO') order came into force on 5 December 2012. The order requires UK-licensed energy suppliers to improve the energy efficiency of domestic households from 1 January 2013. Targets are set in proportion to the size of historic customer bases and must be delivered by 31 March 2015. The Group judges that although targets are based on historic share of supply, it is not obligated by ECO in 2012. Accordingly, no provision has been recognised in the current year.

Metering contracts

The Department of Energy and Climate Change ('DECC') has modified the UK gas and electricity supply licences requiring all domestic premises to be fitted with compliant smart meters for measuring energy consumption by 31 December 2019. The Group has a number of existing rental contracts for non-compliant meters that include penalty charges if these meters are removed from use before the end of their deemed useful lives. The Group considers that these contracts are not onerous until the meters have been physically removed from use and therefore only recognises a provision at this point.

(b) Key sources of estimation uncertainty

The key assumptions concerning the future, and other key sources of estimation uncertainty at the balance sheet date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year, are discussed below.

Revenue recognition – unread gas and electricity meters

Revenue for energy supply activities includes an assessment of energy supplied to customers between the date of the last meter reading and the year end (unread). Unread gas and electricity comprises both billed and unbilled revenue. It is estimated through the billing systems, using historical consumption patterns, on a customer by customer basis, taking into account weather patterns, load forecasts and the differences between actual meter reads being returned and system estimates. Actual meter reads continue to be compared to system estimates between the balance sheet date and the finalisation of the accounts. An assessment is also made of any factors that are likely to materially affect the ultimate economic benefits which will flow to the Group, including bill cancellation and re-bill rates. To the extent that the economic benefits are not expected to flow to the Group, the value of that revenue is not recognised. The judgements applied, and the assumptions underpinning these judgements, are considered to be appropriate. However, a change in these assumptions would have an impact on the amount of revenue recognised.

Industry reconciliation process – cost of sales

Industry reconciliation procedures are required as differences arise between the estimated quantity of gas and electricity the Group deems to have supplied and billed customers, and the estimated quantity industry system operators deem the individual suppliers, including the Group, to have supplied to customers. Difference in deemed supply is referred to as imbalance. The reconciliation procedures can result in either a higher or lower value of industry deemed supply than has been estimated as being supplied to customers by the Group, but in practice tends to result in a higher value of deemed supply. The Group then reviews the difference to ascertain whether there is evidence that its estimate of amounts supplied to customers is inaccurate or whether the difference arises from other causes. The Group's share of the resulting imbalance is included within commodity costs charged to cost of sales. Management estimates the level of recovery of imbalance which will be achieved either through subsequent customer billing or through developing industry settlement procedures.

Decommissioning costs

The estimated cost of decommissioning at the end of the producing lives of fields (including storage assets) is reviewed periodically and is based on reserves, price levels and technology at the balance sheet date. Provision is made for the estimated cost of decommissioning at the balance sheet date. The payment dates of total expected future decommissioning costs are uncertain and dependent on the lives of the facilities, but are currently anticipated to be incurred until 2055, with the majority of the costs expected to be paid between 2020 and 2030.

Significant judgements and estimates are also made about the costs of decommissioning British Energy's nuclear power stations and the costs of waste management and spent fuel. These estimates impact the carrying value of our investment. Various arrangements and indemnities are in place with the Secretary of State with respect to these costs, as explained in note S2.

Gas and liquids reserves

The volume of proven and probable ('2P') gas and liquids reserves is an estimate that affects the unit of production method of depreciating producing gas and liquids PP&E as well as being a significant estimate affecting decommissioning and impairment calculations. The factors impacting gas and liquids estimates, the process for estimating reserve quantities and reserve recognition are described on page 143.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

3. Critical accounting judgements and key sources of estimation uncertainty continued

The impact of a change in estimated 2P reserves is dealt with prospectively by depreciating the remaining book value of producing assets over the expected future production. If 2P reserves estimates are revised downwards, earnings could be affected by higher depreciation expense or an immediate write-down (impairment) of the asset's book value.

Determination of fair values – energy derivatives

Fair values of energy derivatives are estimated by reference in part to published price quotations in active markets and in part by using valuation techniques. More detail on the assumptions used in determining fair valuations is provided in note 24.

Impairment of long-lived assets

The Group has several material long-lived assets that are assessed or tested for impairment at each reporting date in accordance with the Group's accounting policy as described in note S2. The Group makes judgements and estimates in considering whether the carrying amounts of these assets or cash generating units (CGUs) are recoverable. The key assets that are subjected to impairment tests are upstream gas and oil assets, power generation assets, storage facility assets, nuclear investment (investment in associate) and goodwill.

Upstream gas and oil assets

The recoverable amount of the Group's gas and oil assets is determined by discounting the post-tax cash flows expected to be generated by the assets over their lives. The cash flows are derived from projected production profiles of each field, based predominantly on expected 2P reserves and take into account forward prices for gas and liquids over the relevant period. Where forward market prices are not available, prices are determined based on internal model inputs. The recoverable amount also takes into account assumptions market participants would use in estimating fair value.

Power generation assets

The recoverable amount of the Group's power generation assets is calculated by discounting the pre-tax cash flows expected to be generated by the assets and is dependent on views of forecast power generation and forecast power, gas, carbon and capacity prices (where applicable) and the timing and extent of capital expenditure. Where forward market prices are not available, prices are determined based on internal model inputs. The prior year impairment charge in relation to UK gas-fired power stations assumed overcapacity in the UK power generation market post 2018 will diminish and normal returns will be achievable on our most efficient assets.

Storage facility assets

The recoverable amount of our planned storage facilities is calculated by discounting the post-tax cash flows expected to be generated by the assets based on predictions of seasonal gas price differentials and shorter term price volatilities less any related capital and operating expenditure. Should the business cases not support the planned investments, this risks a loss of pre-development costs incurred to date.

Nuclear investment

The recoverable amount of the nuclear investment is based on the value of the existing British Energy nuclear fleet. The existing fleet value is calculated by discounting post-tax cash flows derived from the stations based on forecast power generation and power prices, whilst taking account of planned outages and the possibility of life extensions.

Goodwill

Goodwill does not generate independent cash flows and accordingly is allocated at inception to specific CGUs or groups of CGUs for impairment testing purposes. The recoverable amounts of these CGUs are derived from estimates of future cash flows (as described in the asset classes above). The goodwill impairment tests are also subject to these key estimates.

Further detail on impairments arising and the assumptions used in determining the recoverable amounts is provided in notes 14 and 15.

Credit provisions for trade and other receivables

The methodology for determining provisions for credit losses on trade and other receivables and the level of such provisions is set out in note 18. Although the provisions recognised are considered appropriate, the use of different assumptions or changes in economic conditions could lead to changes in the provisions and therefore impact profit or loss.

Pensions and other post–employment benefits

The cost of providing benefits under defined benefit schemes is determined separately for each of the Group's schemes under the projected unit credit actuarial valuation method. Actuarial gains and losses are recognised in full in the period in which they occur. The key assumptions used for the actuarial valuation are based on the Group's best estimate of the variables that will determine the ultimate cost of providing post-employment benefits, on which further detail is provided in notes 29 and S6.

Provisions for onerous contracts

The Group has entered into a number of commodity procurement and capacity contracts related to specific assets in the ordinary course of its business. Where the unavoidable costs of meeting the obligations under these contracts exceed the associated, expected future net benefits, an onerous contract provision is recognised. The calculation of these provisions will involve the use of estimates. The key onerous provisions are as follows:

Rijnmond power station operating lease

The onerous provision is calculated using net revenue estimates related to power, gas, and carbon forward prices less the tolling costs. The contract runs until 2030 and there is currently no liquid market for these commodities for much of this period.

European gas transportation capacity contracts

The onerous provision is calculated using capacity costs incurred under the contracts, less any predicted income. The provision assumes that all contracts are onerous for the period to 2018 but that post-2018 the remaining capacities could still be necessary to secure supplies of gas into the UK. Therefore no provision has been recognised relating to this latter period.

Direct Energy wind farm power purchase agreements

The onerous nature of the power purchase agreements is measured using estimates relating to wind forecasts, forward curves for energy prices, balancing costs and renewable energy certificates for which there is not a liquid market for the full term of all the contracts.

Financial Statements

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

4. Segmental analysis

The Group's results are discussed in the Business Review (pages 5 to 50). For a description of the products and services from which each reportable segment derives its revenues, see note S4.

During the year the Group renamed its external segments. Downstream UK has been renamed as British Gas, Upstream UK as Centrica Energy, Storage UK as Centrica Storage, and North America as Direct Energy.

The Group's segmental results are as follows:

(a) Revenue

Year ended 31 December	2012 Gross segment revenue £m	2012 Less inter-segment revenue (i) £m	2012 Group revenue £m	2011 (restated) (ii) Gross segment revenue £m	2011 (restated) (ii) Less inter-segment revenue (i) £m	2011 (restated) (ii) Group revenue £m
Continuing operations:						
Residential energy supply (ii)	**9,121**	**–**	**9,121**	7,930	–	7,930
Residential services (ii)	**1,674**	**(131)**	**1,543**	1,644	(81)	1,563
Business energy supply and services (ii)	**3,062**	**(10)**	**3,052**	2,829	(7)	2,822
British Gas	**13,857**	**(141)**	**13,716**	12,403	(88)	12,315
Gas	**3,712**	**(353)**	**3,359**	3,571	(521)	3,050
Power	**1,237**	**(275)**	**962**	1,588	(179)	1,409
Centrica Energy	**4,949**	**(628)**	**4,321**	5,159	(700)	4,459
Centrica Storage	**202**	**(38)**	**164**	184	(20)	164
Residential energy supply	**2,357**	**–**	**2,357**	2,416	–	2,416
Business energy supply	**2,690**	**–**	**2,690**	2,748	–	2,748
Residential and business services	**532**	**–**	**532**	520	–	520
Upstream and wholesale energy	**436**	**(274)**	**162**	433	(231)	202
Direct Energy	**6,015**	**(274)**	**5,741**	6,117	(231)	5,886
	25,023	**(1,081)**	**23,942**	23,863	(1,039)	22,824
Discontinued operations:						
European Energy	**–**	**–**	**–**	167	–	167

(i) Inter-segment revenue is subject to year-on-year fluctuations principally due to the change in the mix of internal and external energy sales.
(ii) To align with management responsibilities and reporting, the British Gas Community Energy and British Gas New Energy businesses have been reallocated from the Residential energy supply segment to the Business energy supply and services and Residential services segments respectively. The 2011 comparatives have been restated accordingly.

The Group operates in the following geographical areas:

Revenue (based on location of customer)

Year ended 31 December	2012 £m	2011 £m
Continuing operations:		
UK	**16,991**	15,760
North America	**5,741**	5,886
Rest of the world	**1,210**	1,178
	23,942	22,824

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NOTES TO THE FINANCIAL STATEMENTS CONTINUED

4. Segmental analysis continued

(b) Operating profit

Year ended 31 December	2012 £m	2011 (restated) (i) £m
Continuing operations:		
Residential energy supply (i)	**606**	544
Residential services (i)	**312**	269
Business energy supply and services (i)	**175**	192
British Gas	**1,093**	1,005
Gas (ii)	**919**	769
Power (ii)	**311**	254
Centrica Energy	**1,230**	1,023
Centrica Storage	**89**	75
Residential energy supply	**156**	161
Business energy supply	**129**	110
Residential and business services	**33**	28
Upstream and wholesale energy	**13**	13
Direct Energy	**331**	312
Adjusted operating profit – segment operating profit before exceptional items, certain re-measurements and impact of fair value uplifts from Strategic Investments (iii)	**2,743**	2,415
Share of joint ventures/associates' interest and taxation	**(85)**	(102)
Depreciation of fair value uplifts to property, plant and equipment – Venture (ii)	**(67)**	(64)
Depreciation of fair value uplifts to property, plant and equipment (net of taxation) – associates – British Energy (ii)	**(29)**	(41)
	2,562	2,208
Exceptional items (note 7)	**(534)**	(331)
Certain re-measurements included within gross profit (note 7)	**603**	(437)
Certain re-measurements of associates' energy contracts (net of taxation) (note 7)	**(6)**	(26)
Operating profit after exceptional items and certain re-measurements	**2,625**	1,414
Discontinued operations:		
European Energy (iv)	**–**	13

(i) To align with management responsibilities and reporting, the British Gas Community Energy and British Gas New Energy businesses have been reallocated from the Residential energy supply segment to the Business energy supply and services and Residential services segments respectively. The 2011 comparatives have been restated accordingly.
(ii) See note 2 and note 11 for an explanation of the depreciation on fair value uplifts to PP&E on acquiring Strategic Investments.
(iii) Includes results of equity-accounted interests before interest and taxation.
(iv) Represents profit after taxation and before exceptional items and certain re-measurements of Oxxio B.V. up to the date of disposal. This is the measure of results of discontinued operations that is reported regularly to the Group's Executive Committee.

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NOTES TO THE FINANCIAL STATEMENTS CONTINUED

4. Segmental analysis continued

(c) Included within adjusted operating profit

Year ended 31 December	Share of results of joint ventures and associates before interest and taxation (i) 2012 £m	2011 £m	Depreciation and impairments of property, plant and equipment (iii) 2012 £m	2011 £m	Amortisation, write-downs and impairments of intangibles 2012 £m	2011 £m
Continuing operations:						
Residential energy supply	**–**	–	**8**	8	**34**	23
Residential services	**–**	–	**20**	18	**8**	6
Business energy supply and services	**–**	–	**2**	2	**6**	7
British Gas	**–**	–	**30**	28	**48**	36
Gas (i) (ii) (iii)	**–**	(1)	**637**	503	**131**	52
Power (i) (iii)	**254**	237	**106**	112	**5**	4
Centrica Energy	**254**	236	**743**	615	**136**	56
Centrica Storage	**–**	–	**30**	30	**–**	–
Residential energy supply	**–**	–	**2**	1	**22**	9
Business energy supply	**–**	–	**2**	1	**7**	4
Residential and business services	**–**	–	**3**	3	**7**	6
Upstream and wholesale energy (ii)	**–**	–	**84**	89	**6**	4
Direct Energy	**–**	–	**91**	94	**42**	23
Other (iv)	**–**	–	**22**	19	**19**	25
	254	236	**916**	786	**245**	140

(i) Share of results of joint ventures and associates is before interest, certain re-measurements, depreciation of fair value uplifts to PP&E on Strategic Investments and taxation.
(ii) During 2012, £118 million of write downs relating to exploration and evaluation assets were incurred in Centrica Energy – Gas (2011: £44 million) and £4 million were incurred in Direct Energy – Upstream and wholesale energy (2011: £2 million).
(iii) Depreciation of PP&E is stated before depreciation of fair value uplifts for Strategic Investments.
(iv) Other comprises Corporate Centre assets which are charged out to other Group segments.

(d) Assets and liabilities

The Group operates in the following geographical areas:

Non-current assets (based on location of assets) (i)

31 December	2012 £m	2011 £m
UK	**9,788**	9,146
North America	**2,458**	2,413
Norway	**2,113**	745
Rest of the world	**449**	467
	14,808	12,771

(i) Non-current assets include goodwill, other intangible assets, PP&E and interest in joint ventures and associates.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

4. Segmental analysis continued

(d) Assets and liabilities continued

31 December	Net segment assets/(liabilities) 2012 £m	Net segment assets/(liabilities) 2011 (restated) (i) £m	Average capital employed Year ended 31 December 2012 £m	Average capital employed Year ended 31 December 2011 (restated) (i) (ii) £m
Residential energy supply (i) (ii)	**(118)**	28	**212**	325
Residential services (i) (ii)	**349**	264	**289**	247
Business energy supply and services (i) (ii)	**645**	645	**714**	645
British Gas	**876**	937	**1,215**	1,217
Gas	**3,447**	2,427	**1,868**	1,500
Power	**3,671**	3,534	**2,995**	3,335
Centrica Energy	**7,118**	5,961	**4,863**	4,835
Centrica Storage	**510**	517	**301**	221
Residential energy supply (ii)	**800**	925	**840**	716
Business energy supply (ii)	**534**	459	**413**	316
Residential and business services (ii)	**393**	377	**371**	367
Upstream and wholesale energy (ii)	**720**	733	**743**	736
Direct Energy	**2,447**	2,494	**2,367**	2,135
	10,951	9,909	**8,746**	8,408
Unallocated current and deferred tax balances	**(7)**	186		
Certain derivative financial instruments (iii)	**(553)**	(1,214)		
Bank overdrafts and loans, securities and treasury derivatives	**(5,054)**	(3,868)		
Net retirement benefit asset	**88**	330		
Corporate Centre assets and discontinued operations	**502**	257		
Non-operating liabilities	**(5,024)**	(4,309)		
Net assets	**5,927**	5,600		

(i) To align with management responsibilities and reporting, the British Gas Community Energy and British Gas New Energy businesses have been reallocated from the Residential energy supply segment to the Business energy supply and services and Residential services segments respectively. The 2011 comparatives have been restated accordingly.
(ii) To align with management reporting, capital employed in British Gas and Direct Energy has been adjusted to include assets under construction. The 2011 comparatives have been restated accordingly.
(iii) Includes balances held by joint ventures/associates.

Capital employed represents the investment required to operate each of the Group's segments. Capital employed is used by the Group to calculate the return on capital employed for each of the Group's segments as part of the Group's 'managing for value' concept. Additional value is created when the return on capital employed exceeds the cost of capital. Net segment assets of the Group can be reconciled to the Group's capital employed as follows:

Year ended 31 December	2012 £m	2011 £m
Net segment assets at 31 December	**10,951**	9,909
Effect of averaging net segment assets	**177**	475
Deduct:		
Average intra-group balances	**55**	49
Average pre-productive assets	**(1,987)**	(1,592)
Average margin call debtor	**(114)**	(73)
Average cash at bank, in transit and in hand excluding certain restricted cash	**(336)**	(360)
Average capital employed	**8,746**	8,408

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

4. Segmental analysis continued

(e) Capital expenditure

Year ended 31 December	Capital expenditure on property, plant and equipment (note 15) 2012 £m	2011 (restated) (i) £m	Capital expenditure on intangible assets other than goodwill (note 14) 2012 £m	2011 £m
Continuing operations:				
Residential energy supply (i)	**7**	28	**230**	240
Residential services (i)	**44**	26	**9**	22
Business energy supply and services (i)	**9**	3	**91**	75
British Gas	**60**	57	**330**	337
Gas (ii)	**1,733**	488	**380**	97
Power	**76**	89	**8**	6
Centrica Energy	**1,809**	577	**388**	103
Centrica Storage	**42**	59	**1**	–
Residential energy supply	**–**	–	**3**	4
Business energy supply	**–**	1	**27**	18
Residential and business services	**3**	2	**2**	1
Upstream and wholesale energy	**79**	36	**14**	8
Direct Energy	**82**	39	**46**	31
Other	**17**	26	**64**	49
Capital expenditure on continuing operations	**2,010**	758	**829**	520
Decrease in prepayments related to capital expenditure	**(4)**	(15)	**–**	–
Capitalised borrowing costs	**(53)**	(46)	**(7)**	–
(Increase)/decrease in payables related to capital expenditure	**(158)**	68	**–**	(5)
Purchases of emissions allowances and renewable obligations certificates	**–**	–	**(250)**	(216)
Net cash outflow	**1,795**	765	**572**	299

(i) To align with management responsibilities and reporting, the British Gas Community Energy and British Gas New Energy businesses have been reallocated from the Residential energy supply segment to the Business energy supply and services and Residential services segments respectively. The 2011 comparatives have been restated accordingly.
(ii) During the period, £1,175 million of assets were acquired from Statoil, ConocoPhillips and Total. See note 30.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

5. Costs of continuing operations

Analysis of costs by nature

Year ended 31 December	2012 £m	2011 £m
Transportation, distribution and metering costs	**(3,835)**	(3,718)
Commodity costs	**(10,750)**	(10,918)
Depreciation, amortisation and write-downs	**(843)**	(757)
Employee costs	**(713)**	(672)
Other direct costs relating to the upstream businesses	**(694)**	(389)
Other direct costs relating to the downstream businesses	**(1,841)**	(1,505)
Total cost of sales before exceptional items and certain re-measurements	**(18,676)**	(17,959)
Exceptional items and certain re-measurements (note 7)	**514**	(658)
Total cost of sales	**(18,162)**	(18,617)
Depreciation, amortisation and write-downs	**(385)**	(233)
Employee costs	**(1,149)**	(1,188)
Impairment of trade receivables (note 18)	**(206)**	(222)
Other costs associated with upstream businesses	**(140)**	(211)
Other costs associated with downstream businesses	**(964)**	(896)
Total operating costs before exceptional items and certain re-measurements	**(2,844)**	(2,750)
Exceptional items and certain re-measurements (note 7)	**(445)**	(110)
Total operating costs	**(3,289)**	(2,860)

6. Directors and employees

(a) Employee costs [i]

Year ended 31 December	2012 £m	2011 £m
Wages and salaries	**(1,611)**	(1,562)
Social security costs	**(140)**	(137)
Pension and other post-employment benefits costs	**(97)**	(129)
Share scheme costs	**(43)**	(40)
	(1,891)	(1,868)
Capitalised employee costs	**29**	8
Employee costs recognised in the Income Statement	**(1,862)**	(1,860)

(i) Details of Directors' remuneration, share-based payments and pension entitlements in the Remuneration Report on pages 61 to 75 form part of these Financial Statements. Details of the remuneration of key management personnel are given in note 34.

(b) Average number of employees during the year

	2012 Number	2011 Number
British Gas	**30,305**	31,278
Centrica Energy	**1,788**	1,658
Centrica Storage	**306**	290
Direct Energy	**6,243**	6,206
	38,642	39,432

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NOTES TO THE FINANCIAL STATEMENTS CONTINUED

7. Exceptional items and certain re-measurements

(a) Exceptional items

Year ended 31 December	2012 £m	2011 £m
Continuing operations:		
Provision for Direct Energy wind power purchase agreements (i)	**(89)**	–
Provision for European onerous capacity contracts	**–**	(221)
Exceptional items from continuing operations included within gross profit	**(89)**	(221)
Impairment of UK generation assets	**–**	(226)
British Gas contract migration	**–**	(63)
Restructuring charges (ii)	**(214)**	(154)
Pension curtailment (note 29)	**–**	333
Impairment of investment in nuclear new build (notes 16 and 36)	**(231)**	–
	(445)	(110)
Exceptional items from continuing operations included within Group operating profit	**(534)**	(331)
Taxation on exceptional items (note 9)	**93**	69
Effect of change in upstream UK tax rates (note 9)	**(40)**	(204)
Net exceptional items from continuing operations after taxation	**(481)**	(466)
Discontinued operations:		
Loss on disposal of Oxxio B.V. after taxation (note 31)	**–**	(56)
Total exceptional items after taxation	**(481)**	(522)

(b) Certain re-measurements

Year ended 31 December	2012 £m	2011 £m
Continuing operations:		
Certain re-measurements recognised in relation to energy contracts:		
Net gains arising on delivery of contracts (iii)	**745**	200
Net losses arising on market price movements and new contracts (iv)	**(135)**	(632)
Net losses arising on positions in relation to cross-border transportation or capacity contracts	**(7)**	(5)
Net re-measurements from continuing operations included within gross profit	**603**	(437)
Net losses arising on re-measurement of associates' energy contracts (net of taxation) (v)	**(6)**	(26)
Net re-measurements included within Group operating profit	**597**	(463)
Taxation on certain re-measurements (note 9)	**(193)**	119
Net re-measurements from continuing operations after taxation	**404**	(344)
Discontinued operations:		
Net re-measurements on energy contracts of discontinued operations after taxation	**–**	22
Total re-measurements after taxation	**404**	(322)

(i) An exceptional charge has been recognised in relation to wind power purchase agreements in Direct Energy to reflect the fair value of the obligation to purchase power above its net realisable value.

(ii) As a result of a Group-wide cost reduction programme, restructuring charges have been recorded including staff redundancies, onerous lease charges and £48 million of asset impairments. See Business Review for more details.

(iii) As energy is delivered or consumed from previously contracted positions the related fair value recognised in the opening Balance Sheet (representing the discounted difference between forward energy prices at the opening Balance Sheet date and the contract price of energy to be delivered) is charged or credited to the Income Statement.

(iv) Represents fair value losses arising from the change in fair value of future contracted sales and purchase contracts as a result of changes in forward energy prices between reporting dates (or date of inception and the reporting date, where later).

(v) Includes fair value unwinds relating to the recognition of energy procurement contracts and energy sales contracts at their acquisition-date fair values.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

8. Net interest

Year ended 31 December	Interest expense £m	Interest income £m	2012 Total £m	Interest expense £m	Interest income £m	2011 Total £m
Continuing operations:						
Cost of servicing net debt:						
Interest income	**–**	**39**	**39**	–	37	37
Interest expense on bonds, bank loans and overdrafts (i)	**(232)**	**–**	**(232)**	(176)	–	(176)
Interest expense on finance leases	**(18)**	**–**	**(18)**	(19)	–	(19)
	(250)	**39**	**(211)**	(195)	37	(158)
(Losses)/gains on revaluation:						
(Losses)/gains on fair value hedges	**(22)**	**31**	**9**	(83)	72	(11)
Fair value (losses)/gains on other derivatives (ii)	**(155)**	**132**	**(23)**	(71)	35	(36)
Fair value gains on other securities measured at fair value	**–**	**3**	**3**	–	14	14
Net foreign exchange translation of monetary assets and liabilities (iii)	**(10)**	**–**	**(10)**	–	19	19
	(187)	**166**	**(21)**	(154)	140	(14)
Notional interest arising from discounting and other interest (iv)	**(60)**	**49**	**(11)**	(55)	35	(20)
	(497)	**254**	**(243)**	(404)	212	(192)
Capitalised borrowing costs (v)	**60**	**–**	**60**	46	–	46
Interest (expense)/income	**(437)**	**254**	**(183)**	(358)	212	(146)

(i) During 2012 the Group increased its outstanding bond debt principal by £1,250 million, €150 million and HK$450 million, and decreased it by £284 million. See note 12(c).
(ii) Primarily reflects changes in the fair value of derivatives used to hedge the foreign exchange exposure associated with inter-company loans denominated in foreign currencies.
(iii) Primarily reflects foreign exchange (losses)/gains on loans denominated in foreign currencies.
(iv) Other includes interest received for cash collateral balances, supplier early payment arrangements and a net £45 million (2011: £27 million) relating to pension schemes.
(v) Borrowing costs have been capitalised using an average rate of 4.70% (2011: 4.94%).

9. Taxation

(a) Analysis of tax charge

Year ended 31 December	Business performance £m	Exceptional items and certain re-measurements £m	2012 Results for the year £m	Business performance £m	Exceptional items and certain re-measurements £m	2011 Results for the year £m
Current tax						
UK corporation tax	**(376)**	**14**	**(362)**	(529)	69	(460)
UK petroleum revenue tax	**(208)**	**–**	**(208)**	(220)	–	(220)
Foreign tax	**(285)**	**(7)**	**(292)**	(107)	10	(97)
Adjustments in respect of prior years	**(53)**	**–**	**(53)**	23	–	23
Total current tax	**(922)**	**7**	**(915)**	(833)	79	(754)
Deferred tax						
Current year	**(143)**	**(86)**	**(229)**	(40)	90	50
UK petroleum revenue tax	**13**	**–**	**13**	46	–	46
Foreign deferred tax	**(70)**	**(11)**	**(81)**	(24)	17	(7)
Change in tax rates	**40**	**(50)**	**(10)**	30	(201)	(171)
Adjustments in respect of prior years	**53**	**–**	**53**	11	(1)	10
Total deferred tax	**(107)**	**(147)**	**(254)**	23	(95)	(72)
Total tax on profit from continuing operations (i)	**(1,029)**	**(140)**	**(1,169)**	(810)	(16)	(826)

(i) Total tax on profit from operations excludes taxation on the Group's share of profits in joint ventures and associates.

Tax on items taken directly to equity is disclosed in notes 27 and 28. The Group earns its profits primarily in the UK, therefore the tax rate used for tax on profit from ordinary activities is the standard rate for UK corporation tax, which from 1 April 2012 was 24% (2011: 26%), with the exception of upstream profits, which were taxed at a UK corporation tax rate of 30% (2011: 30%) plus a supplementary charge of 32% (2011: 32%). On 3 July 2012, the UK Government substantively enacted the restriction on the rate of tax relief on oil and gas decommissioning costs from the current 62% to 50%. A one-off exceptional charge of £40 million has been recognised from revaluing the related deferred tax provisions.

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NOTES TO THE FINANCIAL STATEMENTS CONTINUED

9. Taxation continued

Certain upstream assets also bear petroleum revenue tax at 50% (2011: 50%). Norwegian upstream profits are taxed at the standard rate of 28% (2011: 28%) plus a special tax of 50% (2011: 50%) resulting in an aggregate tax rate of 78%. Taxation for other jurisdictions is calculated at the rates prevailing in those respective jurisdictions.

The UK Government has announced its intention to propose that Parliament reduce the main rate of UK corporation tax to 21% by 1 April 2014. At 31 December 2012 a reduction in the rate to 23% had been substantively enacted so the relevant UK deferred tax assets and liabilities included in these Financial Statements have been based on that rate. The effect of the additional proposed reduction in the UK corporation tax rate by 2014 would be to decrease the net deferred tax liability by £18 million.

(b) Factors affecting the tax charge

The differences between the total tax shown above and the amount calculated by applying the standard rate of UK corporation tax to the profit before tax are as follows:

Year ended 31 December			2012			2011
	Business performance £m	Exceptional items and certain re-measurements £m	Results for the year £m	Business performance £m	Exceptional items and certain re-measurements £m	Results for the year £m
Profit from continuing operations before tax	**2,379**	**63**	**2,442**	2,062	(794)	1,268
Less: share of profits in joint ventures and associates, net of interest and taxation	**(140)**	**6**	**(134)**	(93)	26	(67)
Group profit from continuing operations before tax	**2,239**	**69**	**2,308**	1,969	(768)	1,201
Tax on profit from continuing operations at standard UK corporation tax rate of 24.5% (2011: 26.5%)	**(549)**	**(17)**	**(566)**	(522)	204	(318)
Effects of:						
Net expenses not deductible for tax purposes	**(77)**	**(56)**	**(133)**	(20)	–	(20)
Movement in unrecognised deferred tax assets	**(20)**	**–**	**(20)**	(28)	(31)	(59)
UK petroleum revenue tax rates	**(149)**	**–**	**(149)**	(128)	–	(128)
Overseas tax rates	**(39)**	**(6)**	**(45)**	(24)	15	(9)
Additional charges applicable to upstream profits	**(235)**	**(11)**	**(246)**	(152)	(2)	(154)
Changes to tax rates	**40**	**(50)**	**(10)**	30	(201)	(171)
Adjustments in respect of prior years	**–**	**–**	**–**	34	(1)	33
Taxation on profit from continuing operations	**(1,029)**	**(140)**	**(1,169)**	(810)	(16)	(826)

(c) Factors that may affect future tax charges

Production of gas and oil within the UK continental shelf is subject to several taxes: corporation tax at 30% (2011: 30%) on profits of gas and oil production; a supplementary charge at 32% (2011: 32%) on profits of gas and oil production (adjusted for financing costs) and petroleum revenue tax (PRT) at 50% (2011: 50%) on income generated from certain gas and oil production (net of certain costs).

PRT is a deductible expense for the purposes of corporation tax and the supplementary charge. The rate of tax suffered on profits of UK gas production therefore falls between 62% and 81% (2011: 62% and 81%). To the extent that the Group's profits are earned from UK gas and oil production, its effective tax rate will remain above the current UK statutory rate of 24% (2011: 26%).

Income earned in territories outside the UK, notably in the USA and Norway, is generally subject to higher effective rates of tax than the current UK statutory rate. In the medium term, the Group's effective tax rate is expected to remain above the UK statutory rate.

10. Dividends

			2012			2011
	£m	Pence per share	Date of payment	£m	Pence per share	Date of payment
Prior year final dividend	**576**	**11.11**	**13 Jun 2012**	540	10.46	15 Jun 2011
Interim dividend	**240**	**4.62**	**14 Nov 2012**	222	4.29	16 Nov 2011
	816			762		

The Directors propose a final dividend of 11.78 pence per ordinary share (totalling £602 million) for the year ended 31 December 2012. The dividend will be submitted for formal approval at the Annual General Meeting to be held on 13 May 2013 and, subject to approval, will be paid on 12 June 2013 to those shareholders registered on 26 April 2013.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

11. Earnings per ordinary share

Basic earnings per ordinary share has been calculated by dividing the earnings attributable to equity holders of the Company for the year of £1,273 million (2011: £421 million) by the weighted average number of ordinary shares in issue during the year of 5,183 million (2011: 5,159 million). The number of shares excludes six million ordinary shares (2011: seven million), being the weighted average number of the Company's own shares held in the employee share trust. The Directors believe that the presentation of adjusted basic earnings per ordinary share, being the basic earnings per ordinary share adjusted for certain re-measurements, exceptional items and the impact of Strategic Investments, assists with understanding the underlying performance of the Group, as explained in note 2.

The reconciliation of basic to adjusted basic earnings per ordinary share is as follows:

(a) Continuing and discontinued operations

Year ended 31 December	2012 £m	2012 Pence per ordinary share	2011 £m	2011 Pence per ordinary share
Earnings – basic	**1,273**	**24.6**	421	8.2
Net exceptional items after taxation (notes 2 and 7)	**481**	**9.2**	522	10.1
Certain re-measurement (gains)/losses after taxation (notes 2 and 7)	**(404)**	**(7.8)**	322	6.2
Depreciation of fair value uplifts to property, plant and equipment from Strategic Investments, after taxation	**56**	**1.1**	68	1.3
Earnings – adjusted basic	**1,406**	**27.1**	1,333	25.8
Earnings – diluted	**1,273**	**24.4**	421	8.1
Earnings – adjusted diluted	**1,406**	**27.0**	1,333	25.6

Strategic Investments

During 2009, the Group acquired a 20% interest in British Energy and the entire share capital of Venture. As explained in note 2, the depreciation relating to fair value uplifts of the acquired Venture PP&E and associated taxation is excluded in arriving at adjusted earnings for the year, which amounted to £67 million (2011: £64 million) depreciation and a taxation credit of £40 million (2011: £37 million) in the period. Additionally, the impact of depreciation arising on fair value uplifts attributed to the British Energy nuclear power stations and related taxation included within the Group's share of the post-taxation results of the associate is excluded in arriving at adjusted earnings for the period, which amounted to £29 million (2011: £41 million) net of taxation.

(b) Continuing operations

Year ended 31 December	2012 £m	2012 Pence per ordinary share	2011 £m	2011 Pence per ordinary share
Earnings – basic	**1,273**	**24.6**	442	8.6
Net exceptional items after taxation (notes 2 and 7)	**481**	**9.2**	466	9.0
Certain re-measurement (gains)/losses after taxation (notes 2 and 7)	**(404)**	**(7.8)**	344	6.7
Depreciation of fair value uplifts to property, plant and equipment from Strategic Investments, after taxation	**56**	**1.1**	68	1.3
Earnings – adjusted basic	**1,406**	**27.1**	1,320	25.6
Earnings – diluted	**1,273**	**24.4**	442	8.5
Earnings – adjusted diluted	**1,406**	**27.0**	1,320	25.4

(c) Discontinued operations

Year ended 31 December	2012 £m	2012 Pence per ordinary share	2011 £m	2011 Pence per ordinary share
Loss – basic and diluted	**–**	**–**	(21)	(0.4)

Certain re-measurements (notes 2 and 7) included within operating profit and discontinued operations comprise certain re-measurements arising on energy procurement activities and re-measurements of proprietary trades in relation to cross-border transportation or capacity contracts. All other re-measurements are included within results before exceptional items and certain re-measurements.

In addition to basic and adjusted basic earnings per ordinary share, information is presented for diluted and adjusted diluted earnings per ordinary share. Under this presentation, no adjustments are made to the reported earnings for either 2012 or 2011, however the weighted average number of shares used as the denominator is adjusted for potentially dilutive ordinary shares.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

11. Earnings per ordinary share continued

(d) Weighted average number of shares

	2012 Million shares	2011 Million shares
Weighted average number of shares used in the calculation of basic earnings per ordinary share	**5,183**	5,159
Dilutive impact of share-based payment schemes	**33**	44
Weighted average number of shares used in the calculation of diluted earnings per ordinary share	**5,216**	5,203

12. Sources of finance

The Group funds its business using a combination of debt and equity.

(a) Group funding

31 December	2012 £m	2011 (restated) (i) £m
Net debt	**4,047**	3,292
Equity	**5,927**	5,600
Capital	**9,974**	8,892

(i) To align with management reporting, net debt has been restated to include mark-to-market values on derivative financial instruments used to hedge offsetting changes in borrowings. See note 12(b).

The Group seeks to maintain an efficient capital structure with a balance of debt and equity. Debt levels are restricted to limit the risk of financial distress and, in particular, to maintain strong credit ratings. The Group's credit ratings are important for several reasons, to:

- maintain a low cost of debt;
- limit collateral requirements in energy trading, hedging and decommissioning security arrangements; and
- ensure the Group is an attractive counterparty to energy producers and long term customers.

At 31 December 2012, the Group's long-term credit rating was A3 stable outlook for Moody's Investors Service Limited and A- stable outlook for Standard & Poor's Credit Market Services Europe Limited. These ratings did not change during 2012.

The Group monitors its current and projected capital position on a regular basis, considering a medium-term view of three to five years, and different stress case scenarios, including the impact of changes in the Group's credit ratings and significant movements in commodity prices. A number of financial ratios are monitored, including those used by the credit rating agencies, such as debt to cash flow ratios and adjusted EBITDA to gross interest expense. At 31 December 2012, the ratio of the Group's net debt to adjusted EBITDA was 1.1 (2011: 1.1). Adjusted EBITDA to gross interest expense for the year ended 31 December 2012 was 8.4 (2011: 8.7).

British Gas Insurance Limited (BGIL) is required under FSA regulations to hold a minimum capital amount and has complied with this requirement in 2012 (and 2011). For the remainder of the Group, the level of debt that can be raised is restricted by the Company's Articles of Association. Net debt is limited to the greater of £5.0 billion and a gearing ratio of three times adjusted capital and reserves. Based on adjusted capital and reserves as at 31 December 2012 of £5.9 billion, the limit for net debt was £17.8 billion. The Group funds its debt principally through issuing bonds. In addition the Group also maintains substantial committed facilities from banks (see note 25), but generally uses these to provide backup liquidity and does not typically draw on them.

(b) Net debt summary

31 December	2012 £m	2011 (restated) (i) £m
Cash at bank, in transit and in hand	**201**	94
Short-term deposits	**730**	424
Cash and cash equivalents (ii)	**931**	518
Securities – current (iii)	**7**	28
Securities – non-current (iii) (iv)	**199**	190
Current and non-current borrowings	**(5,328)**	(4,171)
Derivatives	**144**	143
Net debt	**(4,047)**	(3,292)

(i) To align with management reporting, net debt has been restated to include mark-to-market values on derivative financial instruments used to hedge offsetting changes in borrowings.
(ii) Cash and cash equivalents includes £241 million (2011: £262 million) of restricted cash mostly held by the Group's insurance undertakings that is not readily available to be used for other purposes within the Group.
(iii) Securities balances include £76 million of available-for-sale financial assets (2011: £90 million).
(iv) Non-current securities include £130 million (2011: £128 million) of index-linked gilts which management use for short term liquidity management purposes.

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NOTES TO THE FINANCIAL STATEMENTS CONTINUED

12. Sources of finance continued

(c) Borrowings summary

31 December	Coupon rate %	Principal m	2012 Current £m	2012 Non-current £m	2012 Total £m	2011 Current £m	2011 Non-current £m	2011 Total £m
Bank overdrafts and loans (i)			**33**	**336**	**369**	69	198	267
Bonds (by maturity date):								
2 November 2012	5.875	£284	**–**	**–**	**–**	291	–	291
27 February 2013	1.045	¥3,000	**22**	**–**	**22**	–	26	26
9 December 2013	7.125	€367	**305**	**–**	**305**	–	317	317
4 November 2014	Floating	$100	**–**	**62**	**62**	–	64	64
10 December 2014	5.125	£315	**–**	**332**	**332**	–	335	335
31 March 2015	Floating	$70	**–**	**44**	**44**	–	45	45
24 October 2016	5.500	£300	**–**	**338**	**338**	–	336	336
19 September 2018	7.000	£400	**–**	**479**	**479**	–	473	473
1 February 2019	3.213	€100	**–**	**83**	**83**	–	–	–
22 February 2022	3.680	HK$450	**–**	**36**	**36**	–	–	–
10 March 2022	6.375	£500	**–**	**527**	**527**	–	527	527
4 September 2026	6.400	£200	**–**	**228**	**228**	–	224	224
16 April 2027	5.900	$70	**–**	**43**	**43**	–	45	45
13 March 2029	4.375	£750	**–**	**766**	**766**	–	–	–
5 January 2032 (ii)	Zero	€50	**–**	**41**	**41**	–	–	–
19 September 2033	7.000	£770	**–**	**777**	**777**	–	777	777
12 September 2044	4.250	£500	**–**	**495**	**495**	–	–	–
			327	**4,251**	**4,578**	291	3,169	3,460
Commercial paper			**82**	**–**	**82**	114	–	114
Obligations under finance leases			**30**	**269**	**299**	28	302	330
			472	**4,856**	**5,328**	502	3,669	4,171

(i) At 31 December the maturity analysis for non-current bank loans was: 1-2 years £15 million, 2-5 years nil and >5 years £321 million (2011: 1-2 years £34 million, 2-5 years £18 million and >5 years £146 million).
(ii) During the period, the Group issued €50 million of zero coupon notes with an accrual yield of 4.200%, which will result in a €114 million repayment on maturity.

13. Notes to the Group Cash Flow Statement

(a) Reconciliation of Group operating profit to cash generated from continuing operations

Year ended 31 December	2012 £m	2011 £m
Group operating profit including share of results of joint ventures and associates	**2,625**	1,414
Less share of profit of joint ventures and associates	**(134)**	(67)
Group operating profit before share of results of joint ventures and associates	**2,491**	1,347
Add back/(deduct):		
Amortisation, write-down and impairment of intangible assets	**289**	140
Depreciation, write-down and impairment of property, plant and equipment	**987**	1,055
Impairment of associate	**231**	–
Recycling of write-down of available-for-sale financial assets	**–**	23
(Profit)/loss on sale of businesses, property, plant and equipment and other intangible assets	**(38)**	5
Increase in provisions	**201**	395
Defined benefit pension curtailment gain	**(3)**	(332)
Defined benefit pension service cost	**87**	118
Defined benefit pension contributions	**(136)**	(130)
Employee share scheme costs	**43**	40
Re-measurement of energy contracts (i)	**(610)**	404
Operating cash flows before movements in working capital	**3,542**	3,065
Increase in inventories	**(88)**	(79)
(Increase)/decrease in trade and other receivables (ii)	**(210)**	201
Increase in trade and other payables (ii)	**361**	42
Cash generated from continuing operations	**3,605**	3,229

(i) Adds back unrealised (gains)/losses arising from re-measurement of energy contracts.
(ii) Includes net inflow of £114 million of cash collateral in 2012 (2011: net outflow of £26 million). See note 25.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

13. Notes to the Group Cash Flow Statement continued

(b) Reconciliation of net increase in cash and cash equivalents to movement in net debt

	2012 £m	2011 restated (i) £m
Net increase in cash and cash equivalents	**452**	30
Add back/(deduct):		
Net sale of securities	**(26)**	(48)
Cash inflow from additional debt	**(1,712)**	(114)
Cash outflow from payment of capital element of finance leases	**31**	25
Cash outflow from repayment of other debt	**471**	30
Cash outflow from settlement of derivative contracts related to borrowings	**14**	–
	(770)	(77)
Revaluation of:		
Securities	**10**	10
Loans and other borrowings	**2**	(59)
Derivative contracts related to borrowings	**(12)**	26
	(770)	(100)
Increase in interest payable on loans and other borrowings	**(41)**	(2)
Acquisitions	**5**	(3)
Exchange adjustments	**46**	8
Other non-cash movements	**5**	–
Movement in net debt	**(755)**	(97)
Net debt at 1 January	**(3,292)**	(3,195)
Net debt at 31 December	**(4,047)**	(3,292)

(i) To align with management reporting, net debt has been restated to include mark-to-market values on derivative financial instruments used to hedge offsetting changes in borrowings. See note 12(b).

(c) Exploration and evaluation cash flows

Included within the £572 million (2011: £299 million) purchase of intangible assets in investing activities is £370 million (2011: £85 million) relating to exploration and evaluation of oil and gas assets.

(d) Relationship between current tax charge and taxes paid

Year ended 31 December	UK £m	Non-UK £m	2012 £m	UK £m	Non-UK £m	2011 £m
Current tax charge:						
Corporation tax	433	274	**707**	438	96	534
Petroleum revenue tax	208	–	**208**	220	–	220
	641	**274**	**915**	658	96	754
Taxes paid:						
Corporation tax	139	193	**332**	389	41	430
Petroleum revenue tax	192	–	**192**	262	–	262
	331	**193**	**524**	651	41	692

Differences between current tax charged and taxes paid arose principally due to the following factors:

- Corporation tax is generally paid, based on estimated profits, partly during the year and partly in the following year and cash tax balancing on agreement with tax authorities will also occur in future periods. Fluctuations in profits from year to year may therefore give rise to divergence between the charge for the current year and taxes paid; and
- Petroleum revenue tax payments are based on income realised in the preceding period, with subsequent adjustments to reflect actual profits. Variations in production from period to period may therefore lead to temporary differences between tax charged and tax paid.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

14. Goodwill and other intangible assets

(a) Carrying amounts

	2012 Goodwill £m	2012 Application software (i) £m	2012 EUAs and ROCs £m	2012 Exploration and evaluation expenditure £m	2012 Other (ii) £m	2012 Total £m	2011 Goodwill £m	2011 Application software (i) £m	2011 EUAs and ROCs £m	2011 Exploration and evaluation expenditure £m	2011 Other (ii) £m	2011 Total £m
Cost												
1 January	2,526	959	122	306	351	**4,264**	2,378	796	186	376	231	3,967
Additions	–	205	250	370	4	**829**	–	219	216	85	–	520
Acquisitions (note 30)	74	–	–	6	42	**122**	153	4	–	–	129	286
Disposals	–	(22)	–	–	(5)	**(27)**	–	(66)	–	(6)	–	(72)
Surrenders	–	–	(227)	–	–	**(227)**	–	–	(280)	–	–	(280)
Write-downs	–	–	–	(122)	–	**(122)**	–	–	–	(46)	–	(46)
Transfers (iii)	–	–	–	–	–	**–**	–	–	–	(100)	(12)	(112)
Exchange adjustments	(47)	(5)	(1)	6	(10)	**(57)**	(5)	6	–	(3)	3	1
31 December	**2,553**	**1,137**	**144**	**566**	**382**	**4,782**	2,526	959	122	306	351	4,264
Accumulated amortisation and impairment												
1 January	8	407	4	–	106	**525**	8	401	16	–	88	513
Amortisation	–	79	–	–	31	**110**	–	74	–	–	14	88
Impairments	2	49	6	–	–	**57**	–	–	3	–	3	6
Disposals	–	(18)	–	–	(5)	**(23)**	–	(66)	–	–	–	(66)
Surrenders	–	–	(4)	–	–	**(4)**	–	–	(15)	–	–	(15)
Exchange adjustments	–	(2)	–	–	(3)	**(5)**	–	(2)	–	–	1	(1)
31 December	**10**	**515**	**6**	**–**	**129**	**660**	8	407	4	–	106	525
NBV at 31 December	**2,543**	**622**	**138**	**566**	**253**	**4,122**	2,518	552	118	306	245	3,739

(i) Application software includes assets under construction with a cost of £315 million (2011: £334 million). Additions to application software includes £7 million (2011: nil) of capitalised borrowing costs.
(ii) Mainly includes customer relationships and brands.
(iii) Includes transfers between other Balance Sheet captions, such as from intangible assets to property, plant and equipment.

(b) Carrying amount of goodwill and intangible assets with indefinite useful lives allocated to CGUs

Goodwill acquired through business combinations and indefinite-lived intangible assets have been allocated for impairment testing purposes to individual or groups of CGUs each representing the lowest level within the Group at which the goodwill or indefinite-lived intangible asset is monitored for internal management purposes as follows:

31 December CGU(s)	Principal acquisitions to which goodwill and intangibles with indefinite useful lives relate	2012 Carrying amount of goodwill £m	2012 Carrying amount of indefinite-lived intangible asset (i) £m	2012 Total £m	2011 Carrying amount of goodwill (restated) (iii) £m	2011 Carrying amount of indefinite-lived intangible asset (i) £m	2011 Total £m
British Gas – Business energy supply and services	Enron Direct/Electricity Direct (iii)	**178**	**–**	**178**	178	–	178
British Gas – Residential services	Dyno-Rod (iii)	**38**	**57**	**95**	38	57	95
Centrica Energy – Upstream gas and oil	Newfield/Heimdal/Venture	**929**	**–**	**929**	927	–	927
Direct Energy – Residential energy supply	Direct Energy/ATCO/ CPL/WTU/FCP	**742**	**–**	**742**	761	–	761
Direct Energy – Business energy supply	Direct Energy/ATCO/ Strategic Energy/FCP	**229**	**–**	**229**	212	–	212
Direct Energy – Residential and business services	Enbridge Services/Residential Services Group/Clockwork	**311**	**12**	**323**	289	9	298
Other	Various (ii) (iii)	**116**	**1**	**117**	113	1	114
		2,543	**70**	**2,613**	2,518	67	2,585

(i) The indefinite-lived assets mainly relate to Mr Sparky and Benjamin Franklin brands, acquired as part of the Clockwork business combination, and the Dyno-Rod brand.
(ii) Consists of goodwill balances allocated across multiple CGUs including £33 million for Centrica Storage (2011: £33 million) and £67 million for Trinidad and Tobago (2011: £70 million).
(iii) To align with changes to British Gas management responsibilities and reporting, goodwill has been reallocated from Other to British Gas – Business energy supply and services and British Gas – Residential services. The 2011 comparatives have been restated accordingly.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

14. Goodwill and other intangible assets continued

(c) Key assumptions used

Value in use calculations have been used to determine recoverable amounts for all of the goodwill and indefinite-lived intangible asset balances, with the exception of the impairment tests for the Centrica Energy – Upstream gas and oil CGUs, where fair value less costs to sell has been used as the basis for determining recoverable amount.

Value in use (VIU)

The VIU calculations use pre-tax cash flow projections based on the Group's Board-approved three-year business plans. The Group's business plans are based on past experience, and adjusted to reflect market trends, economic conditions, key risks, the implementation of strategic objectives and changes in commodity prices, as appropriate. Commodity prices used in the planning process are based in part on observable market data and in part on internal estimates. The extent to which the commodity prices used in the business plans are based on observable market data is determined by the extent to which the market for the underlying commodity is judged to be active. Note 24 provides additional detail on the active period of each of the commodity markets in which the Group operates.

(i) Growth rates and discount rates

Cash flows beyond the three-year plan period have been extrapolated using long-term growth rates in the market where the CGU operates. Long-term growth rates are determined using a blend of publicly available historical data and long-term growth rate forecasts published by external analysts. Cash flows are discounted using a discount rate specific to each CGU. Discount rates reflect the current market assessments of the time value of money and are based on the estimated cost of capital of each CGU. Additionally, risks specific to the cash flows of the CGUs are reflected within cash flow forecasts. Each CGU's weighted average cost of capital is then adjusted to reflect the impact of tax in order to calculate an equivalent pre-tax discount rate. Long-term growth rates and pre-tax discount rates used in the VIU calculations for each of the Group's CGUs are provided in the table below:

2012	**British Gas – Business energy supply and services**	**British Gas – Residential services**	**Direct Energy – Residential energy supply**	**Direct Energy – Business energy supply**	**Direct Energy – Residential and business services**
Growth rate to perpetuity	**1.9%**	**1.9%**	**2.0%**	**2.0%**	**2.0%**
Pre-tax discount rate	**7.5%**	**7.5%**	**8.5%**	**8.5%**	**8.5%**

2011	British Gas – Business energy supply and services	British Gas – Residential services	Direct Energy – Residential energy supply	Direct Energy – Business energy supply	Direct Energy – Residential and business services
Growth rate to perpetuity	2.0%	2.0%	2.1%	2.1%	2.1%
Pre-tax discount rate	7.5%	7.5%	8.5%	8.5%	8.5%

(ii) Inflation rates

Inflation rates used in the three-year business plan were based on a blend of a number of publicly available inflation forecasts for the UK, Canada and the US. Inflation rates used for the value in use calculations were as follows: UK: 1.9% (2011: 2.0%), Canada: 2.0% (2011: 2.1%) and the US: 2.3% (2011: 2.6%).

(iii) Key operating assumptions by CGUs using VIU

The key operating assumptions across all CGUs are Gross Margin, Revenues and Operating Costs. Each of these assumptions is tailored to the specific CGU using management's knowledge of the environment, as shown in the table overleaf.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

14. Goodwill and other intangible assets continued

CGU	Gross margin	Revenues	Operating costs
British Gas – Business energy supply and services	Existing customers: based on contractual terms. New customers and renewals: based on gross margins achieved in the period leading up to date of the business plan. Both adjusted for current market conditions and transportation cost inflation.	Market share: percentage immediately prior to business plan. Adjusted for: growth forecasts which are based on sales and marketing activity and recent customer acquisitions. Gas and electricity revenues based on forward market prices.	Wages: projected headcount in line with expected activity. Salary increases based on inflation expectations. Credit losses: historical assumptions regarding provisions have been updated to reflect the current UK environment.
British Gas – Residential services	Future sales: based on percentages achieved in the period up to the approval of the business plan.	Market share: percentage immediately prior to business plan. Adjusted for: change in growth rates to reflect the current economic environment in the UK.	Wages: projected headcount in line with expected efficiency programme.
Direct Energy – Residential energy supply	Existing customers: based on contractual terms. New customers and renewals: based on gross margins achieved in the period leading up to date of the business plan. Adjusted for: competitor data. Regulated gross margin percentages are based on regulatory applications submitted to the Alberta Utilities Commission in Canada.	Market share: average percentage immediately prior to business plan. Adjusted for: expectations of growth or decline to reflect regulatory or competitive differences. This includes a continued decline in Ontario revenues as a result of the challenging regulatory environment.	Wages: projected headcount in line with expected activity. Salary increases based on inflation expectations. Future developments: slight reduction in costs to reflect planned business process efficiencies. Customer acquisition: based on experience of costs required to support acquisition, renewal and other servicing activities.
Direct Energy – Business energy supply	Existing customers: based on contractual terms. New customers and renewals: based on gross margins achieved historically.	Market share: based on historical growth trends and planned sales activities by individual market sector. Adjusted for: prices based on contractual terms for fixed price contracts and forward market curves for both gas and electricity in Canada and the US.	Wages: projected headcount in line with expected activity. Salary increases based on inflation expectations. Future developments: reduction in costs to reflect expected savings.
Direct Energy – Residential and business services	New customers and renewals: based on gross margins achieved in the period leading up to date of the business plan. Adjusted for: current economic conditions including lower Canadian consumer confidence and weak housing markets in Canada and the US.	Market share: based on historical growth trends by individual market sector. Adjusted for: new product offerings and continued penetration into new markets.	Wages: projected headcount in line with expected activity. Salary increases based on inflation expectations. Credit losses: historical assumptions regarding provisions have been updated to reflect the current North American environment.

Fair value less costs to sell (FVLCS)

FVLCS is used as the basis for determining the recoverable amount of goodwill allocated to Centrica Energy – Upstream gas and oil. This methodology is deemed to be more appropriate as it is based on the post-tax cash flows arising from Centrica Energy – Upstream gas and oil as a whole. This is consistent with the approach taken by management to evaluate the economic value of the underlying assets.

Discount rate and cash-flow assumptions, Centrica Energy – Upstream gas and oil

FVLCS is determined by discounting the post-tax cash flows expected to be generated by the gas production and development assets, net of associated selling costs, taking into account those assumptions that market participants would use in estimating fair value. Post-tax cash flows are derived from projected production profiles of each field, taking into account forward prices for gas and liquids over the relevant period. Where forward market prices are not available, prices are determined based on internal model inputs. Note 24 provides additional detail on the active period of each of the commodity markets in which the Group operates. The date of cessation of production depends on the interaction of a number of variables, such as the recoverable quantities of hydrocarbons, production costs, the contractual duration of the licence area and the selling price of the gas and liquids produced. As each field has specific reservoir characteristics and economic circumstances, the post-tax cash flows for each field are computed using individual economic models. Post-tax cash flows used in the FVLCS calculation for the first three years are based on the Group's Board-approved three-year business plans and, thereafter, are based on long-term production and cash flow forecasts.

The future post-tax cash flows are discounted using a post-tax nominal discount rate of 8.5% (2011: 8.5%) to determine the FVLCS. The discount rate and inflation rate used in the FVLCS calculation are determined in the same manner as the rates used in the VIU calculations described above, with the exception of the adjustment required to determine an equivalent pre-tax discount rate.

(d) Summary of results

For all material CGUs, the recoverable amounts exceed their carrying values at the impairment test date. Reasonably possible changes in the key assumptions listed above would not cause the recoverable amounts of the goodwill balances to be less than the carrying amounts.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

15. Property, plant and equipment

(a) Carrying amounts

	Land and buildings £m	Plant, equipment and vehicles (i) (v) £m	Power generation (i) (ii) (iv) (v) £m	Gas production and storage (i) (ii) (v) £m	2012 Total £m	Land and buildings £m	Plant, equipment and vehicles (i) (v) £m	Power generation (i) (ii) (iv) (v) £m	Gas production and storage (i) (ii) (v) £m	2011 Total £m
Cost										
1 January	26	417	2,318	10,708	**13,469**	26	369	2,229	9,852	12,476
Additions	–	84	93	1,780	**1,957**	–	85	98	529	712
Capitalised borrowing costs (note 8)	–	–	–	53	**53**	–	–	–	46	46
Acquisitions (note 30)	–	–	–	67	**67**	–	10	–	33	43
Disposals	–	(38)	(19)	(210)	**(267)**	–	(44)	(12)	(2)	(58)
Transfers (iii)	–	–	–	–	**–**	–	–	5	100	105
Decommissioning liability revisions and additions (note 23)	–	–	4	536	**540**	–	–	(4)	200	196
Exchange adjustments	–	(1)	(14)	(32)	**(47)**	–	(3)	2	(50)	(51)
31 December	**26**	**462**	**2,382**	**12,902**	**15,772**	26	417	2,318	10,708	13,469
Accumulated depreciation and impairment										
1 January	13	190	1,064	5,790	**7,057**	12	178	743	5,145	6,078
Charge for the year	1	60	109	727	**897**	1	52	127	654	834
Impairments	–	4	13	73	**90**	–	–	205	16	221
Disposals	–	(20)	(4)	(181)	**(205)**	–	(39)	(12)	(2)	(53)
Exchange adjustments	–	(2)	(6)	(24)	**(32)**	–	(1)	1	(23)	(23)
31 December	**14**	**232**	**1,176**	**6,385**	**7,807**	13	190	1,064	5,790	7,057
NBV at 31 December	**12**	**230**	**1,206**	**6,517**	**7,965**	13	227	1,254	4,918	6,412

(i) Assets in the course of construction are included within the following categories: plant, equipment and vehicles £66 million, power generation £55 million, gas production £715 million and gas storage £143 million (2011: £61 million, £45 million, £996 million and £156 million respectively).
(ii) The NBV of decommissioning assets included within power generation and gas production and storage assets was £1,307 million (2011: £907 million).
(iii) Transfers to/from other Balance Sheet accounts, including transfers to inventory or transfers from intangible assets for exploration licences once a field is being developed.
(iv) The Humber power station has been pledged as security for pension liabilities up to a value of £400 million (2011: £300 million). The carrying value of Humber at 31 December 2012 was £380 million (2011: £382 million).
(v) Assets held under finance leases and to which title was restricted at 31 December 2012 included in totals above:

	Plant, equipment and vehicles £m	Power generation £m	Gas production and storage £m	2012 Total £m	Plant, equipment and vehicles £m	Power generation £m	Gas production and storage £m	2011 Total £m
Cost at 1 January	6	469	415	**890**	2	469	415	886
Additions	–	–	–	**–**	4	–	–	4
Disposals	(4)	–	–	**(4)**	–	–	–	–
Cost at 31 December	**2**	**469**	**415**	**886**	6	469	415	890
Aggregate depreciation at 1 January	3	201	380	**584**	1	173	375	549
Charge for the year	–	28	5	**33**	2	28	5	35
Disposals	(2)	–	–	**(2)**	–	–	–	–
Aggregate depreciation at 31 December	**1**	**229**	**385**	**615**	3	201	380	584
NBV at 31 December	**1**	**240**	**30**	**271**	3	268	35	306

(b) Impairment of property, plant and equipment

During 2012, impairment charges recorded by the Group include the following:

- Centrica Energy – Gas: production assets associated with the Ensign development well in the Southern North Sea were written down in the period, giving rise to an impairment charge of £73 million.
- Centrica Energy – Power: wind farm power generation assets associated with the Docking Shoal wind farm were impaired in the period following an unsuccessful planning consent application. This gave rise to an impairment charge of £11 million.

These charges are reflected in operating costs before exceptional items within the Income Statement.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

16. Interests in joint ventures and associates

(a) Interest in joint ventures and associates

	Investments in joint ventures and associates (i) £m	Shareholder loans £m	**2012 Total £m**	Investments in joint ventures and associates £m	Shareholder loans £m	2011 Total £m
1 January	2,351	269	**2,620**	2,343	164	2,507
Additions (i)	140	178	**318**	113	115	228
Decrease in shareholder loans	–	(42)	**(42)**	–	(10)	(10)
Share of profits for the year	134	–	**134**	67	–	67
Share of other comprehensive income	32	–	**32**	(25)	–	(25)
Impairment (ii)	(231)	–	**(231)**	–	–	–
Dividends	(110)	–	**(110)**	(147)	–	(147)
31 December	**2,316**	**405**	**2,721**	2,351	269	2,620

(i) Additions include £30 million in relation to the Group's retained 50% interest in Celtic Array Limited (Round 3). See note 31.
(ii) On 4 February 2013, the Group announced its decision not to proceed with the nuclear new build investment. Accordingly, the Group has recorded an exceptional impairment of £231 million. This amount includes the carrying value of its investment in NNB Holding Company Limited as well as value attributed to nuclear new build in the British Energy acquisition. See note 36.

(b) Share of joint ventures' and associates' assets and liabilities

The Group's share of joint ventures' and associates' gross assets and gross liabilities at 31 December 2012 principally comprised of its interests in the following entities (all reported in the Centrica Energy – Power segment):

- Wind farms – Braes of Doune Wind Farm (Scotland) Limited, Barrow Offshore Wind Limited, GLID Wind Farms TopCo Limited (i), Lincs Wind Farm Limited (i) and Celtic Array Limited (Round 3); and
- Nuclear – Lake Acquisitions Limited (British Energy) and NNB Holding Company Limited (Nuclear New Build).

31 December	Joint ventures Wind farms £m	Associates Nuclear £m	Other (ii) £m	**2012 Total £m**	2011 Total £m
Share of non-current assets	842	3,420	57	**4,319**	4,384
Share of current assets	128	634	3	**765**	676
	970	4,054	60	**5,084**	5,060
Share of current liabilities	(286)	(187)	–	**(473)**	(315)
Share of non-current liabilities	(523)	(1,744)	(16)	**(2,283)**	(2,385)
	(809)	(1,931)	(16)	**(2,756)**	(2,700)
Restricted interest on shareholder loan (iii)	(12)	–	–	**(12)**	(9)
Share of net assets of joint ventures and associates	149	2,123	44	**2,316**	2,351
Shareholder loans	384	–	21	**405**	269
Interests in joint ventures and associates	**533**	**2,123**	**65**	**2,721**	2,620
Net (debt)/cash included in share of net assets	(395)	128	(12)	**(279)**	(283)

(i) As part of the finance arrangements entered into by GLID Wind Farms TopCo Limited and Lincs Wind Farm Limited, the Group's shares in GLID Wind Farms TopCo Limited and Lincs Wind Farm Limited are secured in favour of third parties. The securities would only be enforced in the event that GLID Wind Farms TopCo Limited or Lincs Wind Farm Limited default on any of their obligations under their respective finance arrangements.
(ii) Other includes joint ventures of North Sea Infrastructure Partners Limited and Bacton Storage Company Limited.
(iii) The Group restricts an element of interest receivable on the shareholder loan to Lincs Wind Farm Limited.

(c) Share of profits in joint ventures and associates

Year ended 31 December	Joint ventures Wind farms £m	Associates Nuclear £m	**2012 Total £m**	2011 Total £m
Income	49	592	**641**	594
Expenses excluding certain re-measurements (i)	(33)	(420)	**(453)**	(444)
Certain re-measurements	–	(8)	**(8)**	(33)
	16	164	**180**	117
Interest paid	(17)	(27)	**(44)**	(58)
Taxation excluding certain re-measurements (i)	1	(5)	**(4)**	1
Taxation on certain re-measurements	–	2	**2**	7
Share of post-taxation results of joint ventures and associates (i)	**–**	**134**	**134**	67

(i) Includes £66 million (2011: £86 million) relating to depreciation of fair value uplifts to PP&E on acquiring the British Energy investments. The associated tax impact is £37 million credit (2011: £45 million credit).

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NOTES TO THE FINANCIAL STATEMENTS CONTINUED

16. Interests in joint ventures and associates continued

British Energy

During November 2009 the Group acquired a 20% interest in British Energy for £2,255 million and NNB Holding Company Limited ('Nuclear New Build') for £32 million. The Group's share of profit arising from its investment in British Energy for the year to 31 December 2012 as set out in table (c) includes the effect of unwinding the fair value adjustments. As explained in note 2 the depreciation, net of taxation, arising on fair value uplifts attributed to the nuclear power stations is reversed in arriving at adjusted profit for the period as shown in the reconciliation table below and as set out in notes 4(b) and 11.

(d) Reconciliation of share of profits in joint ventures and associates to share of adjusted profits in joint ventures and associates

Year ended 31 December	Joint ventures Wind farms £m	Associates Nuclear £m	2012 Total £m	2011 Total £m
Share of post-taxation results of joint ventures and associates	–	134	**134**	67
Certain re-measurements (net of taxation)	–	6	**6**	26
Depreciation – British Energy (net of taxation) (i)	–	29	**29**	41
Interest paid	17	27	**44**	58
Taxation (excluding certain re-measurements and British Energy depreciation)	(1)	42	**41**	44
Share of adjusted results of joint ventures and associates	**16**	**238**	**254**	236

(i) Relates to depreciation of fair value uplifts to PP&E on acquiring the British Energy investments.

17. Inventories

31 December	2012 £m	2011 £m
Gas in storage and transportation	**344**	243
Other raw materials and consumables	**156**	106
Finished goods and goods for resale	**45**	93
	545	442

The Group consumed £1,285 million of inventories (2011: £1,229 million) during the year. Write downs of inventory amounting to £7 million (2011: £21 million) were charged to the Income Statement in the year.

18. Trade and other receivables

31 December	2012 Current £m	2012 Non-current £m	2011 Current £m	2011 Non-current £m
Financial assets:				
Trade receivables	**1,951**	**5**	2,066	3
Accrued energy income	**1,812**	**–**	1,709	–
Other accrued income	**219**	**–**	193	–
Cash collateral pledged (note 25)	**125**	**–**	223	–
Other receivables	**326**	**–**	351	8
	4,433	**5**	4,542	11
Less: provision for credit losses	**(511)**	**–**	(599)	–
	3,922	**5**	3,943	11
Non-financial assets: prepayments and other receivables	**413**	**50**	269	63
	4,335	**55**	4,212	74

Trade and other receivables include financial assets representing the contractual right to receive cash or other financial assets from residential customers, business customers and treasury, trading and energy procurement counterparties as follows:

31 December	2012 Current £m	2012 Non-current £m	2011 Current £m	2011 Non-current £m
Financial assets by class:				
Residential customers	**1,922**	**5**	2,042	4
Business customers	**1,657**	**–**	1,562	7
Treasury, trading and energy procurement counterparties	**854**	**–**	938	–
	4,433	**5**	4,542	11
Less: provision for credit losses	**(511)**	**–**	(599)	–
	3,922	**5**	3,943	11

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

18. Trade and other receivables continued

Receivables from residential and business customers are generally considered to be fully performing until such time as the payment that is due remains outstanding past the contractual due date. Contractual due dates range from falling due upon receipt to falling due in 30 days.

At 31 December 2012, there were £39 million (2011: £24 million) of receivables, net of provisions for credit losses, from residential customers and nil (2011: £22 million) from treasury, trading and energy procurement counterparties that were individually impaired. Receivables from residential customers are generally reviewed for impairment on an individual basis once a customer discontinues their relationship with the Group.

The provision for credit losses is based on an incurred loss model and is determined by application of expected default and loss factors, determined by historical loss experience and current sampling to the various balances receivable from residential and business customers on a portfolio basis, in addition to provisions taken against individual accounts. Balances are written off when recoverability is assessed as being remote. Movements in the provision for credit losses by class are as follows:

	Residential customers £m	Business customers £m	Treasury, trading and energy procurement counterparties £m	**2012 Total £m**	Residential customers £m	Business customers £m	Treasury, trading and energy procurement counterparties £m	2011 Total £m
1 January	(360)	(226)	(13)	**(599)**	(375)	(253)	(13)	(641)
Impairment of trade receivables	(100)	(114)	8	**(206)**	(120)	(102)	–	(222)
Receivables written off	154	133	4	**291**	146	129	–	275
Acquisitions	–	–	–	**–**	(11)	–	–	(11)
Exchange adjustments	2	1	–	**3**	–	–	–	–
31 December	**(304)**	**(206)**	**(1)**	**(511)**	(360)	(226)	(13)	(599)

The impairment charge in trade receivables is stated net of credits for the release of specific provisions made in previous years, which are no longer required. These relate primarily to residential customers in the UK. At 31 December 2012, the Group took possession of £28 million (2011: £32 million) of customer deposits relating to customers in North America who had defaulted on their accounts receivable balance. At 31 December 2012, the Group held £35 million (2011: £50 million) of customer deposits for the purposes of mitigating the credit risk associated with receivables from residential and business customers.

19. Derivative financial instruments

Derivative financial instruments are held for the following purposes and accounted for accordingly:

Purpose	Accounting treatment
Proprietary energy trading and treasury management	Carried at fair value with changes in fair value recognised in the Group's results for the year before exceptional items and certain re-measurements (i)
Energy procurement	Carried at fair value, with changes in the fair value reflected in certain re-measurements (ii)

(i) With the exception of certain energy derivatives related to cross-border transportation and capacity contracts (note S2).
(ii) Energy contracts designated at fair value through profit or loss include certain energy contracts that the Group has, at its option, designated at fair value through profit or loss under IAS 39 because the energy contract contains one or more embedded derivatives that significantly modify the cash flows under the contract (note S2).

In cases where a derivative qualifies for hedge accounting, derivatives are classified as fair value hedges, or cash flow hedges. Notes 20 and S2 provide further detail on the Group's hedge accounting.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

19. Derivative financial instruments continued

The carrying values of derivative financial instruments by product type for accounting purposes are as follows:

31 December	2012 Assets £m	2012 Liabilities £m	2011 Assets £m	2011 Liabilities £m
Derivative financial instruments – held for trading under IAS 39:				
Energy derivatives – for procurement	**229**	**(772)**	332	(1,390)
Energy derivatives – for proprietary trading	**69**	**–**	61	(14)
Interest rate derivatives	**13**	**(86)**	22	(79)
Foreign exchange derivatives	**33**	**(42)**	23	(37)
Energy derivative contracts designated at fair value through profit or loss	**65**	**–**	7	(46)
Derivative financial instruments in hedge accounting relationships:				
Energy derivatives	**–**	**(14)**	–	(65)
Interest rate derivatives	**172**	**(2)**	157	(7)
Foreign exchange derivatives	**–**	**(26)**	3	(7)
Total derivative financial instruments	**581**	**(942)**	605	(1,645)
Included within:				
Derivative financial instruments – current	**268**	**(615)**	315	(1,140)
Derivative financial instruments – non-current	**313**	**(327)**	290	(505)

The contracts included within energy derivatives are subject to a wide range of detailed specific terms but comprise the following general components, analysed on a net carrying value basis:

31 December	2012 £m	2011 £m
Short-term forward market purchases and sales of gas and electricity:		
UK and Europe	**(163)**	(458)
North America	**(209)**	(406)
Structured gas purchase contracts	**(36)**	(91)
Structured gas sales contracts	**(78)**	(120)
Structured power purchase contracts	**54**	(27)
Other	**9**	(13)
Net total	**(423)**	(1,115)

Net gains/(losses) on derivative financial instruments due to re-measurement

31 December	2012 Income Statement £m	2012 Equity £m	2011 Income Statement £m	2011 Equity £m
Financial assets and liabilities measured at fair value:				
Derivative financial instruments – held for proprietary energy trading	**24**	**–**	30	–
Derivative financial instruments – held for trading under IAS 39	**465**	**–**	(576)	–
Energy contracts designated at fair value through profit or loss	**104**	**–**	104	–
Derivative financial instruments in hedge accounting relationships	**7**	**66**	52	(56)
	600	**66**	(390)	(56)

20. Hedge accounting

For the purposes of hedge accounting, hedges are classified as either fair value hedges or cash flow hedges. Note S2 details the Group's accounting policies in relation to derivatives qualifying for hedge accounting under IAS 39. The fair values of derivatives and primary financial instruments in hedge accounting relationships at 31 December were as follows:

31 December	2012 Assets £m	2012 Liabilities £m	2011 Assets £m	2011 Liabilities £m
Fair value hedges	**160**	**–**	153	–
Cash flow hedges	**12**	**(42)**	7	(79)

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

20. Hedge accounting continued

Fair value hedges

The Group's fair value hedges consist of interest rate swaps used to protect against changes in the fair value of fixed-rate, long-term debt due to movements in market interest rates. For qualifying fair value hedges, all changes in the fair value of the hedging instrument and in the fair value of the hedged item in relation to the risk being hedged are recognised in the Income Statement within net interest expense.

Gains or losses arising on fair value hedges at 31 December were as follows:

Gains/(losses) Year ended 31 December	2012 £m	2011 £m
On hedging instruments	**7**	49
On hedged items attributable to the hedged risk	**2**	(60)
	9	(11)

Cash flow hedges

The Group's cash flow hedges consist primarily of:

- physical and financial gas and power purchase contracts used to protect against the variability in future cash flows associated with highly probable forecast purchases of gas and power due to movements in market commodity prices;
- forward foreign exchange contracts used to protect against the variability of functional currency denominated cash flows associated with non-functional currency denominated highly probable forecast transactions;
- interest rate swaps used to protect against the variability in cash flows associated with floating-rate borrowings due to movements in market interest rates; and
- cross-currency interest rate swaps and forward foreign exchange contracts used to protect against the variability in cash flows associated with borrowings denominated in non-functional currencies.

Gains and losses are initially recognised in the cash flow hedging reserve in the Statement of Comprehensive Income and are transferred to the Income Statement or Balance Sheet when the forecast cash flows affect the Income Statement or Balance Sheet. Note 27 details movements in the cash flow hedging reserve. The ineffective portion of gains and losses on cash flow hedging are recognised immediately in the Income Statement. During 2012, the Group recognised a £2 million loss (2011: £3 million gain) due to cash flow hedge ineffectiveness.

Net investment hedges

Historically the Group engaged in net investment hedging (NIH) whereby it would obtain foreign currency debt issued in the same currency as the net investment. In 2009 the Group ceased NIH, however the opening balance of the foreign currency translation reserve includes exchange translation differences on borrowings and derivatives classified as NIH under the requirements of IAS 39. These balances will be recycled to the Income Statement on disposal of the foreign operation.

21. Trade and other payables

31 December	2012 Current £m	2012 Non-current £m	2011 Current £m	2011 Non-current £m
Financial liabilities:				
Trade payables	**1,022**	**–**	988	–
Deferred income	**263**	**–**	449	–
Capital payables	**256**	**–**	108	–
Other payables	**464**	**12**	388	2
Accruals:				
Commodity costs	**833**	**–**	719	–
Transportation, distribution and metering costs	**277**	**–**	177	–
Operating and other accruals	**841**	**–**	778	–
	1,951	**–**	1,674	–
	3,956	**12**	3,607	2
Non-financial liabilities:				
Other payables and accruals	**428**	**3**	359	11
Deferred income	**161**	**11**	128	20
	4,545	**26**	4,094	33

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NOTES TO THE FINANCIAL STATEMENTS CONTINUED

22. Deferred tax liabilities and assets

The following are the major deferred tax liabilities and assets recognised by the Group and movements thereon during the current and prior reporting periods:

	Accelerated tax depreciation (corporation tax) £m	Other timing differences including losses carried forward £m	Marked to market £m	Net deferred petroleum revenue tax (i) £m	Retirement benefit obligation and other provisions £m	**Total £m**
1 January 2011	(1,693)	276	215	6	67	(1,129)
Change to tax rates	(227)	60	1	–	(5)	(171)
(Charge)/credit to income	(103)	156	113	17	(84)	99
(Charge)/credit to equity	–	(10)	23	–	(59)	(46)
Acquisition of subsidiaries	(3)	–	–	–	–	(3)
Exchange and other adjustments	(1)	(23)	3	–	–	(21)
31 December 2011	(2,027)	459	355	23	(81)	**(1,271)**
Change to tax rates	28	(46)	(10)	9	9	**(10)**
(Charge)/credit to income	(269)	192	(177)	26	(16)	**(244)**
(Charge)/credit to equity	–	(2)	(20)	–	69	**47**
Acquisition of subsidiaries	(4)	–	–	–	–	**(4)**
Exchange and other adjustments	(7)	(2)	(4)	–	–	**(13)**
31 December 2012	**(2,279)**	**601**	**144**	**58**	**(19)**	**(1,495)**

(i) The deferred petroleum revenue tax amounts include the effect of deferred corporation tax as petroleum revenue taxation is deductible for corporation tax purposes.

Certain deferred tax assets and liabilities have been offset where there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income taxes relate to the same fiscal authority. The following is an analysis of the gross deferred tax balances and associated offsetting balances for financial reporting purposes:

31 December	**Assets £m**	**2012 Liabilities £m**	Assets £m	2011 Liabilities £m
Gross deferred tax balances crystallising within one year	**66**	**(261)**	187	(354)
Gross deferred tax balances crystallising after one year	**514**	**(1,814)**	993	(2,097)
	580	**(2,075)**	1,180	(2,451)
Offsetting deferred tax balances	**(397)**	**397**	(945)	945
Net deferred tax balances (after offsetting for financial reporting purposes)	**183**	**(1,678)**	235	(1,506)

At the balance sheet date the Group had certain deductible temporary differences of £382 million (2011: £454 million) available for utilisation against future profits. No deferred tax asset has been recognised in respect of these temporary differences, due to the unpredictability of future profit streams. A significant proportion of these assets may be carried forward indefinitely. At the balance sheet date, no temporary differences existed in respect of the Group's overseas investments (2011: nil). The deferred tax liability arising on these temporary differences is estimated to be nil (2011: nil).

23. Provisions for other liabilities and charges

Current provisions for other liabilities and charges	1 January 2012 £m	Acquisitions and disposals £m	Charged in the year £m	Unused and reversed in the year £m	Utilised £m	Transfers (vi) £m	Exchange adjustments £m	**31 December 2012 £m**
Restructuring costs (i)	147	–	172	–	(119)	(71)	–	**129**
Decommissioning costs (iii)	25	–	–	–	(43)	32	1	**15**
Purchase contract loss provision (iv)	85	–	3	–	(93)	84	(2)	**77**
Other (v)	51	–	6	–	(39)	27	–	**45**
	308	**–**	**181**	**–**	**(294)**	**72**	**(1)**	**266**

Non-current provisions for other liabilities and charges	1 January 2012 £m	Acquisitions and disposals £m	Charged in the year £m	Unused and reversed in the year £m	Revisions and additions £m	Transfers (vi) £m	Exchange adjustments £m	**31 December 2012 £m**
Restructuring costs (i) (ii)	17	–	3	–	–	–	–	**20**
Decommissioning costs (iii)	1,591	6	45	(6)	540	(32)	12	**2,156**
Purchase contract loss provision (iv)	217	–	104	–	–	(84)	(5)	**232**
Other (v)	78	–	5	–	–	(11)	–	**72**
	1,903	**6**	**157**	**(6)**	**540**	**(127)**	**7**	**2,480**

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

23. Provisions for other liabilities and charges continued

Included within the above liabilities are the following financial liabilities:

Financial liabilities

31 December	2012 Current £m	2012 Non-current £m	2011 Current £m	2011 Non-current £m
Restructuring costs (i) (ii)	**129**	**20**	144	15
Provisions other than restructuring costs	**66**	**135**	74	151
	195	**155**	218	166

(i) The brought forward restructuring provisions relate to significant restructuring programmes undertaken to achieve cost reductions across the Group. Included within the closing provision are costs related to surplus properties of £26 million (2011: £24 million) estimated with reference to the expected cost to be incurred to the point of lease termination, including costs for dilapidations and sub-letting. The provisions are expected to be utilised by 2022.

(ii) The non-current element of exceptional restructuring provisions charged in the year are expected to be utilised by 2016.

(iii) Provision has been made for the estimated net present cost of decommissioning gas production and storage facilities at the end of their useful lives. The estimate has been based on 2P reserves, price levels and technology at the Balance Sheet date. The timing of decommissioning payments is dependent on the lives of the facilities but is expected to occur by 2055, with the majority of the provision being utilised between 2020 and 2030. The charge to income includes £41 million of notional interest (2011: £40 million). Additions in the year include £450 million in relation to the Statoil, ConocoPhillips and Total asset purchases (see note 30).

(iv) The purchase contract loss provision relates to a number of European gas transportation contracts, the Rijnmond tolling contract and Direct Energy wind farm power purchase agreements (see note 7). The majority of the provisions are expected to be utilised by 2018.

(v) Other provisions include UK contract migration costs, National Insurance payable in respect of Long Term Incentive Scheme liabilities, costs for certain long term take-or-pay contracts renegotiated by the Group in prior years and outstanding litigation for a number of items (none of which are individually significant). The provisions are expected to be utilised by 2016.

(vi) Includes transfers to/from other Balance Sheet accounts. During 2012, £71 million was transferred from restructuring provisions to pension liabilities in respect of changes to employee pension benefits.

24. Fair value of financial instruments

The fair value of a financial instrument is the amount at which the financial instrument could be exchanged in an arm's length transaction between knowledgeable and willing parties under no compulsion to act. The Group has documented internal policies for determining fair value, including methodologies used to establish valuation adjustments required for credit risk.

Financial liabilities

31 December	Notes	2012 Carrying value £m	2012 Fair value £m	2011 Carrying value £m	2011 Fair value £m
Financial liabilities measured at amortised cost:					
Trade and other payables	21	**(3,968)**	**(3,968)**	(3,609)	(3,609)
Bank overdrafts, loans and other borrowings:					
Bank overdrafts and loans	12	**(369)**	**(388)**	(267)	(274)
Bonds	12	**(4,578)**	**(5,119)**	(3,460)	(3,891)
Commercial paper	12	**(82)**	**(82)**	(114)	(114)
Obligations under finance leases	12	**(299)**	**(337)**	(330)	(328)
Provisions	23	**(350)**	**(350)**	(384)	(384)
		(9,646)	**(10,244)**	(8,164)	(8,600)
Financial liabilities at fair value: Derivative financial instruments	19	**(942)**	**(942)**	(1,645)	(1,645)

Financial assets

The carrying values of the Group's financial assets (disclosed in notes 12, 18 and 19) are equal to the fair values of those assets.

Bank overdrafts, loans and other borrowings

The fair values of bonds are based on quoted market prices. The fair values of bank loans have been determined by discounting cash flows with reference to relevant market rates of interest. The fair values of overdrafts and commercial paper are assumed to equal their book values due to the short-term nature of these amounts. The fair values of obligations under finance leases have been determined by discounting contractual cash flows with reference to the Group's cost of borrowing.

Other financial instruments

Due to their nature and/or short-term maturity, the fair values of trade and other receivables, cash and cash equivalents, trade and other payables and provisions are estimated to approximate their carrying values.

Derivative financial instruments and energy contracts designated at fair value through profit or loss

The fair values of foreign exchange and interest rate derivatives are determined by reference to closing market rates at the Balance Sheet date. The fair values of energy derivatives are determined using valuation techniques based in part on observable market data and in part on internal estimates not currently supported by observable market data. The extent to which fair values of energy derivatives are based on observable market data is determined by the extent to which the market for the underlying commodity is judged to be active.

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NOTES TO THE FINANCIAL STATEMENTS CONTINUED

24. Fair value of financial instruments continued

The Group has judged each of the markets in which it operates as active for the purposes of accounting as follows:

Active period of markets	Gas	Power	Coal	Emissions	Oil
UK (years)	**2**	**2**	**3**	**2**	**3**
North America (years)	**5**	**Up to 5**	**n/a**	**Up to 5**	**3**

The fair values of energy contracts within the scope of IAS 39 that settle inside the active period of the market are based on quoted market prices and expected volumes, discounted at an average rate of 1% per annum (2011: 1%). The fair values of derivative financial instruments in North America and Europe are based primarily on quoted market prices. In the UK, however, certain energy contracts extend beyond the active period of the market. The fair values of energy contracts that extend beyond the active period of the market are determined by reference in part to published price quotations in active markets and in part by using valuation techniques based on commodity prices derived using assumptions that are based on internal market expectations and expected volumes, discounted using an average discount rate of 2% per annum for 2012 (2011: 2%).

Where the fair value at initial recognition for contracts which extend beyond the active period differs from the transaction price, a day-one gain or loss will arise. Such gains and losses are deferred and amortised to the Income Statement based on volumes purchased or delivered over the contractual period until such time as observable market data becomes available (see note S2 for further detail). The amount that has yet to be recognised in the Income Statement relating to the differences between the transaction prices and the amounts that would have arisen had valuation techniques used for subsequent measurement been applied at initial recognition, less subsequent releases, is as follows:

Net deferred (gains)/losses	2012 £m	2011 £m
1 January	**(59)**	(109)
Net losses deferred on new transactions	**20**	7
Recognised in the Income Statement during the year	**(2)**	43
31 December	**(41)**	(59)

Fair value hierarchy

Financial assets and financial liabilities measured and held at fair value are classified into one of three categories:

31 December	Level 1 £m	Level 2 £m	Level 3 £m	2012 Total £m	Level 1 £m	Level 2 £m	Level 3 £m	2011 Total £m
Financial assets								
Derivative financial instruments:								
Energy derivatives	29	195	139	**363**	40	318	42	400
Interest rate derivatives	–	185	–	**185**	–	179	–	179
Foreign exchange derivatives	–	33	–	**33**	–	26	–	26
Treasury gilts designated at fair value through profit or loss	130	–	–	**130**	128	–	–	128
Debt instruments	56	–	2	**58**	69	–	3	72
Equity instruments	12	–	6	**18**	11	–	7	18
Total financial assets	**227**	**413**	**147**	**787**	248	523	52	823
Financial liabilities								
Derivative financial instruments:								
Energy derivatives	(59)	(570)	(157)	**(786)**	(169)	(1,140)	(206)	(1,515)
Interest rate derivatives	–	(88)	–	**(88)**	–	(86)	–	(86)
Foreign exchange derivatives	–	(68)	–	**(68)**	–	(44)	–	(44)
Total financial liabilities	**(59)**	**(726)**	**(157)**	**(942)**	(169)	(1,270)	(206)	(1,645)

There were no significant transfers between Level 1 and Level 2 during 2012 and 2011.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

24. Fair value of financial instruments continued

The reconciliation of the Level 3 fair value measurements during the year is as follows:

	2012 Financial assets £m	2012 Financial liabilities £m	2011 Financial assets £m	2011 Financial liabilities £m
Level 3 financial instruments				
1 January	**52**	**(206)**	131	(320)
Total realised and unrealised gains/(losses):				
Recognised in Income Statement	**115**	**31**	(45)	68
Losses recognised in other comprehensive income	**–**	**–**	–	(3)
Purchases, sales, insurances and settlements (net)	**(20)**	**–**	–	–
Transfers from Level 3 to Level 2	**–**	**18**	(34)	49
31 December	**147**	**(157)**	52	(206)
Total gains/(losses) for the year for Level 3 financial instruments held at the end of the reporting period (i)	**100**	**34**	(21)	65

(i) £100 million gains (2011: £21 million losses) for the year for Level 3 financial assets held at the end of the reporting year were recognised within certain re-measurements and no gains or losses (2011: nil) were recognised in other comprehensive income. £34 million gains (2011: £68 million) for the year for Level 3 financial liabilities held at the end of the reporting year were recognised within certain re-measurements and no gains or losses (2011: £3 million losses) were recognised in other comprehensive income.

The impacts of reasonably possible changes to assumed gas, power, coal, emissions and oil prices on the net fair value of the Group's fair value measurements categorised as Level 3 are as follows:

Energy price	2012 Reasonably possible change in variable	2011 Reasonably possible change in variable
UK gas (p/therm)	**+/–5**	+/–9
UK power (£/MWh)	**+/–4**	+/–6
UK coal (US$/tonne)	**+/–13**	+/–13
UK emissions (€/tonne)	**+/–2**	+/–2
UK oil (US$/bbl)	**+/–17**	+/–20

Increase/(decrease) in fair value	2012 £m	2011 £m
UK energy prices – increase/(decrease)	**17/(5)**	52/(38)

The impacts disclosed above result from changing the assumptions used for fair valuing energy contracts in relation to gas, power, emissions, coal and oil prices to reasonably possible alternative assumptions at the Balance Sheet date. The fair value impacts only concern those contracts entered into which are within the scope of IAS 39 and are marked-to-market based on valuation models using assumptions that are not currently observable in an active market. The sensitivity analysis provided is hypothetical only and should be used with caution, as the impacts provided are not necessarily indicative of the actual impacts that would be experienced. This is because the Group's actual exposure to market rates is constantly changing as the Group's portfolio of energy contracts changes. Changes in fair values based on a variation in a market variable cannot be extrapolated as the relationship between the change in market variable and the change in fair value will not always be linear. This can be seen in the results from the above sensitivity analysis.

25. Financial risk management

The Group's normal operating, investing and financing activities expose it to a variety of financial risks. The processes for managing these risks are set out in note S3. The information in this note sets out financial metrics related to these risks.

Transactional and translational currency risks

It is the Group's policy to hedge material transactional exposures using forward contracts to fix the functional currency value of non-functional currency cash flows, except where there is an economic hedge inherent in the transaction. At 31 December 2012, there were no material unhedged non-functional currency monetary assets or liabilities, firm commitments or probable forecast transactions (2011: nil), other than transactions which have an inherent economic hedge and foreign currency borrowings used to hedge translational exposures.

The Group manages translational currency risk taking into consideration the cash impact of any hedging activity as well as the risk to the net asset numbers in the Group's Financial Statements. The translation hedging programme including the potential cash impact is monitored by the GFRMC (Group Financial Risk Management Committee).

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NOTES TO THE FINANCIAL STATEMENTS CONTINUED

25. Financial risk management continued

The impacts of reasonably possible changes in foreign currency rates relative to pounds sterling on profit and equity, both after taxation, based on the assumptions set out in note S3 are as follows:

Foreign exchange rates and incremental profit/(loss)	2012 Reasonably possible change in variable (ii) %	2012 Impact on profit £m	2012 Impact on equity £m	2011 Reasonably possible change in variable (ii) %	2011 Impact on profit £m	2011 Impact on equity (restated) (i) £m
US dollar	**+/–10**	**(5)/5**	**(1)/1**	+/–10	14/(23)	(1)/1
Canadian dollar	**+/–10**	**(11)/13**	**–/–**	+/–10	(18)/20	–/–
Euro	**+/–10**	**(8)/6**	**(4)/–**	+/–10	33/(20)	5/(6)

(i) Restated to remove foreign exchange impacts of consolidation of non-sterling functional currency subsidiaries.
(ii) + is strengthening of pounds sterling, – is weakening of pounds sterling.

Interest rate risk

The impacts of reasonably possible changes in interest rates on profit and equity, both after taxation, based on the assumptions set out in note S3 are as follows:

Interest rates and incremental profit/(loss)	2012 Reasonably possible change in variable %	2012 Impact on profit £m	2012 Impact on equity £m	2011 Reasonably possible change in variable %	2011 Impact on profit £m	2011 Impact on equity (restated) (i) £m
UK interest rates	**+/–1.0**	**5/(5)**	**(11)/10**	+/–1.0	6/(4)	11/(14)
US interest rates	**+/–1.0**	**3/(2)**	**–/–**	+/–1.0	2/(4)	–/–
Euro interest rates	**+/–1.0**	**(2)/2**	**(16)/18**	+/–1.0	(4)/5	–/–

(i) Restated for updated sensitivity methodology adopted in the current year.

Commodity price risk

The impacts of reasonably possible changes in commodity prices on profit and equity, both after taxation, based on the assumptions set out in note S3 are as follows:

Energy prices	2012 Base price (i)	2012 Reasonably possible change in variable	2011 Base price (i)	2011 Reasonably possible change in variable
UK gas (p/therm)	**64**	**+/–5**	59	+/–9
UK power (£/MWh)	**51**	**+/–4**	47	+/–6
UK coal (US$/tonne)	**97**	**+/–13**	117	+/–13
UK emissions (€/tonne)	**7**	**+/–2**	8	+/–2
UK oil (US$/bbl)	**103**	**+/–17**	101	+/–20
North American gas (USc/therm)	**42**	**+/–6**	42	+/–6
North American power (US$/MWh)	**39**	**+/–4**	43	+/–4

(i) The base price represents the average forward market price over the duration of the active market curve used in the sensitivity analysis provided.

Incremental profit/(loss)	2012 Impact on profit £m	2012 Impact on equity £m	2011 Impact on profit £m	2011 Impact on equity £m
UK energy prices (combined) – increase/(decrease)	**92/(83)**	**4/(4)**	245/(235)	24/(24)
North American energy prices (combined) – increase/(decrease)	**93/(93)**	**–/–**	56/(56)	–/–

Liquidity risk

The Group has a number of treasury and risk policies to monitor and manage liquidity risk. Cash forecasts identifying the Group's liquidity requirements are produced regularly and are stress-tested for different scenarios, including, but not limited to, reasonably possible increases or decreases in commodity prices and the potential cash implications of a credit rating downgrade. The Group seeks to ensure that sufficient financial headroom exists for at least a 12-month period to safeguard the Group's ability to continue as a going concern. It is the Group's policy to maintain committed facilities and/or available surplus cash resources of at least £1,200 million, raise at least 75% of its net debt (excluding non-recourse debt) in the long-term debt market and to maintain an average term to maturity in the recourse long-term debt portfolio greater than five years.

At 31 December 2012, the Group had undrawn committed credit facilities of £3,029 million (2011: £3,254 million) and £931 million (2011: £518 million) of cash and cash equivalents. 130% (2011: 115%) of the Group's net debt has been raised in the long-term debt market and the average term to maturity of the long-term debt portfolio was 12.6 years (2011: 9.6 years).

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

25. Financial risk management continued

The Group's liquidity is impacted by the cash pledged under margin/collateral agreements, the table below summarises the movements in margin cash:

	2012 £m	2011 £m
Cash pledged as collateral at 1 January	**(219)**	(173)
Net cash inflow/(outflow)	**114**	(26)
Transferred from discontinued operations	**–**	(2)
Acquisition of businesses	**(4)**	(17)
Foreign exchange	**7**	(1)
Cash pledged as collateral at 31 December (i)	**(102)**	(219)

(i) Of the net cash collateral pledged of £102 million (2011: £219 million), £23 million (2011: £4 million) is included within trade payables and £125 million (2011: £223 million) within trade receivables. In 2011 there was also a net £8 million cash collateral inflow within discontinued operations.

The relatively high level of undrawn committed bank borrowing facilities and available cash resources has enabled the Directors to conclude that the Group has sufficient headroom to continue as a going concern. The statement of going concern is included in the Directors' Report – Governance, on page 60.

Maturity profiles

Maturities of derivative financial instruments, provisions, borrowings, finance leases and trade and other payables are provided in the following tables (all amounts are remaining contractual undiscounted cash flows):

Due for payment	<1 year £m	1 to 2 years £m	2 to 3 years £m	3 to 4 years £m	4 to 5 years £m	>5 years £m
2012						
Energy and interest derivatives in a loss position that will be settled on a net basis	**(130)**	**(47)**	**(10)**	**(2)**	**(1)**	**(4)**
Gross energy procurement contracts and related derivatives carried at fair value	**(19,525)**	**(7,076)**	**(4,032)**	**(2,274)**	**(262)**	**(701)**
Foreign exchange derivatives that will be settled on a gross basis:						
Outflow	**(3,741)**	**(823)**	**(25)**	**(7)**	**(7)**	**(447)**
Inflow	**3,689**	**820**	**22**	**5**	**4**	**363**
Financial liabilities within provisions	**(195)**	**(46)**	**(26)**	**(59)**	**(24)**	**(9)**
Borrowings (i)	**(685)**	**(621)**	**(255)**	**(512)**	**(195)**	**(5,976)**
Finance lease: (ii)						
Minimum lease payments	**(46)**	**(47)**	**(48)**	**(48)**	**(39)**	**(148)**
Capital elements of leases	**(30)**	**(32)**	**(35)**	**(38)**	**(30)**	**(134)**

(i) Includes bank loans, bonds, commercial paper and interest.
(ii) Note the difference between the total minimum lease payments and the total capital elements of leases is due to future finance charges.

Due for payment	<1 year £m	1 to 2 years £m	2 to 3 years £m	3 to 4 years £m	4 to 5 years £m	>5 years £m
2011						
Energy and interest derivatives in a loss position that will be settled on a net basis	(326)	(85)	(17)	(3)	(2)	(24)
Gross energy procurement contracts and related derivatives carried at fair value	(16,174)	(7,033)	(4,396)	(3,552)	(2,054)	(1,077)
Foreign exchange derivatives that will be settled on a gross basis:						
Outflow	(2,920)	(699)	(36)	(19)	(2)	(319)
Inflow	2,921	656	39	17	–	263
Financial liabilities within provisions	(218)	(40)	(30)	(22)	(45)	(29)
Borrowings (i)	(627)	(528)	(497)	(151)	(451)	(3,505)
Finance lease: (ii)						
Minimum lease payments	(46)	(46)	(47)	(48)	(48)	(187)
Capital elements of leases	(28)	(33)	(32)	(35)	(38)	(164)

(i) Includes bank loans, bonds, commercial paper and interest.
(ii) Note the difference between the total minimum lease payments and the total capital elements of leases is due to future finance charges.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

25. Financial risk management continued

Financial liabilities within trade and other payables on an undiscounted basis	2012 £m	2011 £m
Less than 90 days	**3,797**	3,356
90 to 182 days	**81**	90
183 to 365 days	**78**	161
	3,956	3,607
Greater than 365 days	**12**	2
	3,968	3,609

Credit risk for financial assets

Credit risk from financial asset transactions is generated by the potential for the counterparty to default on its contractual obligations. Counterparty credit exposure issues remained a focal point within the Group throughout 2012 and the Group continues to be vigilant in managing counterparty risks in accordance with its financial risk management policies. The period has seen a large number of credit rating downgrades for both financial institutions and European energy majors. In spite of this, the Group has not altered its rating thresholds for counterparty credit limits and continues to operate within its limits. In the US and Europe, on-going regulatory changes are resulting in an increase in trading over exchanges or via zero threshold margined contracts. This helps to reduce counterparty credit risk, but carries increased liquidity requirements. Details of how credit risk is managed across the asset categories shown below are included in note S3. Credit risk from financial assets is measured by counterparty credit rating as follows:

	2012			2011		
	Derivative financial instruments with positive fair values £m	**Receivables from treasury, trading and energy procurement counterparties £m**	**Cash and cash equivalents £m**	Derivative financial instruments with positive fair values £m	Receivables from treasury, trading and energy procurement counterparties £m	Cash and cash equivalents £m
AAA to AA	**1**	**78**	**550**	5	128	411
AA– to A–	**392**	**439**	**354**	469	408	106
BBB+ to BBB–	**85**	**108**	**2**	23	137	–
BB+ to BB–	**71**	**42**	**1**	20	27	1
B or lower	**–**	**5**	**–**	3	1	–
Unrated (i)	**32**	**182**	**24**	85	237	–
	581	**854**	**931**	605	938	518

(i) The unrated counterparty receivables primarily comprise amounts due from subsidiaries of rated entities, exchanges or clearing houses.

An ageing of the carrying value of trade and other receivables that are past due that are not considered to be individually impaired is as follows:

Financial assets within trade and other receivables on an undiscounted basis	2012 £m	2011 £m
Days past due:		
Less than 30 days	**582**	446
30 to 89 days	**235**	268
Less than 90 days	**817**	714
90 to 182 days	**135**	124
183 to 365 days	**179**	192
Greater than 365 days	**90**	114
	1,221	1,144

For additional information on financial risk management see note S3.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

26. Share capital

Allotted and fully paid share capital of the Company

31 December	2012 £m	2011 £m
5,199,019,674 ordinary shares of 6[14]/81p each (2011: 5,173,244,808)	**321**	319

The number of allotted and fully paid shares of the Company issued under employee share schemes for the year was 26 million (2011: 19 million). Ordinary shares were allotted and issued to satisfy the exercise of share options, share incentive schemes, the Direct Energy Employee Share Purchase Plan and the matching element of the Share Incentive Plan as follows:

	2012	2011
Number of shares (millions)	**26**	19
Nominal value (£million)	**1.6**	1.2
Cash consideration (£million)	**33**	23
Service consideration (£million)	**24**	19

The closing price of one Centrica ordinary share on 31 December 2012 was 333.60 pence (2011: 289.30 pence). Centrica employee share ownership trusts purchase Centrica ordinary shares from the open market and receive newly issued shares to satisfy future obligations of certain employee share schemes. During the year, the trusts purchased 2.2 million shares (2011: 0.9 million), received 5.8 million newly allotted shares (2011: 4.9 million) and released 9.1 million shares (2011: 7.0 million) to employees on vesting. At 31 December 2012, the trusts held 6.2 million shares (2011: 7.3 million) at a carrying amount of £19 million (2011: £19 million). Until such time as the Company's own shares held by these trusts vest unconditionally, the amount paid for those shares, or the value they were issued at, are held as own shares and are deducted from equity.

27. Accumulated other comprehensive (loss)/income

					2012					2011
	Available-for-sale reserve (AFS) £m	Cash flow hedging reserve £m	Foreign currency translation reserve £m	Actuarial gains and losses reserve £m	Total £m	Available-for-sale reserve (AFS) £m	Cash flow hedging reserve £m	Foreign currency translation reserve £m	Actuarial gains and losses reserve £m	Total £m
1 January	6	(92)	76	(228)	**(238)**	(11)	(56)	91	(343)	(319)
Exchange differences on translation of foreign operations	–	1	(44)	–	**(43)**	–	(3)	(12)	–	(15)
Recycling of foreign exchange on disposal of business	–	–	–	–	**–**	–	–	(3)	–	(3)
Actuarial (losses)/gains (note 29)	–	–	–	(319)	**(319)**	–	–	–	198	198
Revaluation of available-for-sale securities	7	–	–	–	**7**	(4)	–	–	–	(4)
Transfer of AFS reserve to Income Statement	–	–	–	–	**–**	23	–	–	–	23
Cash flow hedges:										
Net losses	–	(27)	–	–	**(27)**	–	(99)	–	–	(99)
Transferred to income and expense	–	108	–	–	**108**	–	42	–	–	42
Transferred to assets and liabilities	–	(1)	–	–	**(1)**	–	2	–	–	2
Share of other comprehensive income/(loss) of joint ventures and associates net of taxation	–	(12)	–	44	**32**	–	(1)	–	(24)	(25)
Taxation on above items	(2)	(20)	–	69	**47**	(2)	23	–	(59)	(38)
31 December	**11**	**(43)**	**32**	**(434)**	**(434)**	6	(92)	76	(228)	(238)

Foreign currency translation reserve

The foreign currency translation reserve comprises exchange translation differences on foreign currency net investments. Historically the Group has hedged its foreign investments and so the opening balance of foreign currency translation reserve includes exchange translation differences on borrowings and derivatives classified as net investment hedges under the requirements of IAS 39.

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NOTES TO THE FINANCIAL STATEMENTS CONTINUED

27. Accumulated other comprehensive (loss)/income continued

Cash flow hedging reserve

The cash flow hedging reserve comprises fair value movements on instruments designated as cash flow hedges under the requirements of IAS 39. Note 20 provides further detail on cash flow hedging.

The maturity analysis of amounts included in the cash flow hedging reserve, which includes fair value gains and losses in relation to commodity, interest rate and currency hedges, is as follows:

	2012 £m	2011 £m
Within one year	**(18)**	(57)
Between one and five years	**(26)**	(13)
After five years	**1**	(22)
	(43)	(92)

The maturity profile reflects the timing of expected transfers from the cash flow hedging reserve to the Income Statement or Balance Sheet as and when the hedged item affects the Income Statement or Balance Sheet which is, for the most part, on delivery of physical volumes for energy contracts and straight-line amortisation of losses and gains on debt derivatives.

28. Other equity

	2012					2011				
	Revaluation reserve £m	Own shares reserve £m	Share-based payments reserve £m	Merger and capital redemption reserve £m	**Total £m**	Revaluation reserve £m	Own shares reserve £m	Share-based payments reserve £m	Merger and capital redemption reserve £m	Total £m
1 January	26	(19)	112	483	**602**	27	(22)	113	483	601
Employee share schemes:										
Increase in own shares	–	(21)	–	–	**(21)**	–	(19)	–	–	(19)
Exercise of awards	–	21	(45)	–	**(24)**	–	22	(33)	–	(11)
Value of services provided	–	–	43	–	**43**	–	–	40	–	40
Taxation on above items	–	–	(1)	–	**(1)**	–	–	(8)	–	(8)
Exchange adjustments	1	–	–	–	**1**	(1)	–	–	–	(1)
31 December	**27**	**(19)**	**109**	**483**	**600**	26	(19)	112	483	602

For additional explanation of the reserves that are included in the above table see note S5.

29. Pensions

(a) Summary of main defined benefit schemes

Name of scheme	Section	Status	Funding/tax status	Country
Centrica Engineers Pension Scheme	Final salary section	Closed to new members	Funded/tax-registered	UK
	Career average section	Open to new members	Funded/tax-registered	UK
Centrica Pension Plan	Management section	Closed to new members	Funded/tax-registered	UK
	2008 section	Closed to new members	Funded/tax-registered	UK
Centrica Pension Scheme	Final salary section	Closed to new members	Funded/tax-registered	UK
	Career average section	Closed to new members	Funded/tax-registered	UK
Direct Energy Marketing Limited Pension Plan		Closed to new members	Funded/tax-registered	Canada

The Centrica Pension Scheme also has a defined contribution section which is open to new members.

The Centrica Engineers Pension Scheme (CEPS), Centrica Pension Plan (CPP) and Centrica Pension Scheme form the majority of the Group's defined benefit obligation and are referred to below as the 'Registered Pension Schemes'.

For additional background information to the Group's pension schemes see note S6.

(b) 2011 curtailment gain

During 2011, the Group announced changes to the terms of the final salary sections of the CEPS and the CPP with the changes taking effect from 1 January 2012 and 1 March 2012 respectively. Employees' annual increases in pensionable pay will be capped to 2% and annual increases in respect of future years' service for pensions in deferment will be the lower of CPI and 2.5%. Following agreement of the changes in October 2011 (for CEPS) and December 2011 (for CPP) with the trade unions and the trustees, the Group recognised exceptional curtailment gains in 2011 of £333 million, as disclosed in note 7.

The final salary section of the Centrica Pension Scheme has an active membership of approximately 50 employees.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

29. Pensions continued

(c) Accounting assumptions

The accounting assumptions for the Registered Pension Schemes have been given below.

Major assumptions used for the actuarial valuation

31 December	2012 %	2011 %
Rate of increase in employee earnings:		
Subject to cap	**1.7**	2.0
Other	**3.2**	4.3
Rate of increase in pensions in payment	**3.2**	3.3
Rate of increase in deferred pensions:		
In line with CPI capped at 2.5%	**2.5**	2.3
In line with RPI	**3.2**	3.3
Discount rate	**4.8**	5.4

The assumptions relating to longevity underlying the pension liabilities at the balance sheet date have been based on a combination of standard actuarial mortality tables, scheme experience and other relevant data, and include an allowance for future improvements in mortality. The longevity assumptions for members in normal health are as follows:

Life expectancy at age 65 for a member	2012 Male Years	2012 Female Years	2011 Male Years	2011 Female Years
Currently aged 65	**22.8**	**25.2**	22.7	24.0
Currently aged 45	**24.6**	**27.2**	24.5	25.4

At 31 March 2012, the date of the most recent actuarial review, the schemes had approximately 40,200 members and beneficiaries, of which approximately 4,000 were members of the defined contribution section of the Centrica Pension Scheme. The other demographic assumptions have been set having regard to the latest trends in scheme experience and other relevant data. The assumptions are reviewed and updated as necessary as part of the periodic actuarial valuation of the pension schemes.

Impact of changing material assumptions	2012 Increase/ decrease in assumption	2012 Indicative effect on scheme liabilities %	2011 Increase/ decrease in assumption	2011 Indicative effect on scheme liabilities %
Rate of increase in employee earnings subject to cap	**0.25%**	**+/–1**	0.25%	+0/–1
Rate of increase in pensions in payment and deferred pensions	**0.25%**	**+/–4**	0.25%	+/–5
Discount rate	**0.25%**	**–/+5**	0.25%	–/+6
Inflation assumption	**0.25%**	**+/–4**	0.25%	+/–5
Longevity assumption	**1 year**	**+/–2**	1 year	+/–2

The remaining disclosures in this note cover all of the Group's defined benefit schemes.

(d) Amounts included in the Balance Sheet

31 December	2012 £m	2011 £m
Fair value of plan assets	**5,133**	4,670
Present value of defined benefit obligation	**(5,045)**	(4,340)
Net asset recognised in the Balance Sheet	**88**	330
Associated deferred tax liability recognised in the Balance Sheet	**(19)**	(81)
Net pension asset after deferred tax	**69**	249
Pension asset presented in the Balance Sheet as:		
Retirement benefit assets	**254**	413
Retirement benefit liabilities	**(166)**	(83)
Net pension asset	**88**	330

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NOTES TO THE FINANCIAL STATEMENTS CONTINUED

29. Pensions continued

(e) Movement in the year

	2012 Pension liabilities £m	2012 Pension assets £m	2011 Pension liabilities £m	2011 Pension assets £m
1 January	**(4,340)**	**4,670**	(4,574)	4,335
Items included in the Income Statement:				
Current service cost	**(87)**	**–**	(118)	–
Gain/(loss) on curtailment	**3**	**–**	(1)	–
Exceptional gains on curtailment	**–**	**–**	333	–
Interest on scheme liabilities	**(235)**	**–**	(258)	–
Expected return on scheme assets	**–**	**280**	–	285
Items included in Other Comprehensive Income:				
Actuarial (loss)/gain	**(449)**	**130**	198	–
Exchange adjustments	**2**	**(2)**	1	(1)
Items included in the Cash Flow Statement:				
Employer contributions	**–**	**187**	–	130
Other movements:				
Plan participants' contributions	**(27)**	**27**	(29)	29
Benefits paid from schemes	**159**	**(159)**	108	(108)
Transfers from provisions for other liabilities and charges	**(71)**	**–**	–	–
31 December	**(5,045)**	**5,133**	(4,340)	4,670

In addition to current service cost on the Group's defined benefit pension schemes, the Group also charged £13 million (2011: £10 million) to operating profit in respect of defined contribution pension schemes.

(f) Analysis of the actuarial gains/(losses) recognised in the Statement of Comprehensive Income

Year ended 31 December	2012 £m	2011 £m
Actuarial gain (actual return less expected return on pension scheme assets)	**130**	–
Experience gains arising on the scheme liabilities	**87**	57
Changes in assumptions underlying the present value of the scheme liabilities	**(536)**	141
Actuarial (loss)/gain recognised in accumulated other comprehensive loss (before taxation)	**(319)**	198
Cumulative actuarial losses recognised in reserves at 1 January, before adjustment for taxation	**(291)**	(489)
Cumulative actuarial losses recognised in reserves at 31 December, before adjustment for taxation	**(610)**	(291)

(g) Pension scheme assets

The expected long-term rate of return and the market value of plan assets were:

31 December	2012 Fair value £m	2012 Proportion of total fair value %	2012 Expected long-term rate of return per annum %	2011 Fair value £m	2011 Proportion of total fair value %	2011 Expected long-term rate of return per annum %
UK equities	**322**	**6.3**	**6.8**	400	8.6	7.5
Non-UK equities	**1,580**	**30.8**	**7.3**	1,337	28.6	7.7
Fixed-interest bonds	**1,412**	**27.5**	**4.4**	1,370	29.3	5.3
Inflation-linked assets (i)	**1,027**	**20.0**	**4.1**	1,067	22.8	3.9
High-yield debt	**324**	**6.3**	**5.3**	292	6.3	6.3
Diversified asset funds	**246**	**4.8**	**6.8**	–	–	–
Property	**210**	**4.1**	**6.8**	168	3.6	6.8
Cash pending investment	**12**	**0.2**	**5.9**	36	0.8	4.6
	5,133	**100.0**	**5.7**	4,670	100.0	6.0

(i) Consists of government bonds and other assets providing inflation-linked revenue.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

29. Pensions continued

The overall expected rate of return on assets is a weighted average based on the actual plan assets held in each class and the expected returns on separate asset classes less costs of administering the plan and taxes paid by the plan itself. The returns on separate asset classes are based on the expected median return over a 10-year period (for equities, high-yield debt and property) and appropriate market indices (for fixed-interest bonds and inflation-linked assets). These returns are calculated by the independent company actuary, and adjusted for factors specific to the investment portfolio of the Centrica Combined Common Investment Fund.

Included within the Balance Sheet within non-current securities are £61 million (2011: £54 million) of investments, held by the Law Debenture Trust on behalf of the Company, as security in respect of the Centrica Unfunded Pension Scheme defined benefit section. Included within the pension scheme liabilities above are £37 million (2011: £34 million) relating to this scheme.

(h) Pension scheme contributions

The UK Registered Pension Schemes were subject to their triennial valuation carried out by Towers Watson, the schemes' independent actuaries, at 31 March 2012. The results of this valuation were approved by the trustees of the schemes on 11 December 2012. Based on the valuation, the Group and the trustees agreed a revised schedule for deficit payments consisting of an amount of £37 million paid in the year to 31 December 2012 and £77 million per annum from 2013 to 2016. This payment profile replaces the deficit payments as agreed to in the 2009 triennial valuation. A continuing charge over the Humber power station provides additional security for the trustees.

On 31 December 2012 the Group and the trustees also agreed to partially fund the deficit payments using an asset-backed contribution arrangement. Under the arrangement, certain loans to UK Group companies were transferred to a Scottish Limited Partnership established by the Group. The Group made a special contribution to the UK Registered Pension Schemes of £84 million; on the same date the schemes used this contribution to acquire an interest in the partnership for its fair value of £84 million. The schemes' partnership interests entitle them to a distribution from the income of the partnership of £22 million per annum for 4 years. The partnership is controlled by Centrica and its results are consolidated by the Group. As the trustees' interest in the partnership does not meet the definition of a plan asset under IAS 19, it is not reflected in the Balance Sheet. Distributions from the partnership to the schemes will be recognised as scheme assets in the future as they occur.

Deficit payments are also being made in respect of the Direct Energy Marketing Limited Pension Plan in Canada. £4 million was paid in the year to 31 December 2012 and £7 million per annum is to be paid from 2013 to 2016 and £3 million in 2017.

The Group also estimates that it will pay £105 million of ordinary employer contributions during 2013 at an average rate of 21% of pensionable pay.

(i) Five-year histories

Five-year history of surplus/(deficit)	2012 £m	2011 £m	2010 £m	2009 £m	2008 £m
Plan assets	**5,133**	4,670	4,335	3,533	2,642
Defined benefit obligations	**(5,045)**	(4,340)	(4,574)	(4,098)	(2,755)
Surplus/(deficit)	**88**	330	(239)	(565)	(113)

Five-year history of experience gains/(losses)	2012	2011	2010	2009	2008
Difference between the expected and actual return on scheme assets:					
Amount (£m)	**130**	–	154	344	(1,121)
Percentage of scheme assets	**2.5%**	–	3.6%	9.7%	42.4%
Experience gains/(losses) on scheme liabilities:					
Amount (£m)	**87**	57	74	(104)	–
Percentage of the present value of scheme liabilities	**1.7%**	1.3%	1.6%	2.5%	–
Total actuarial (losses)/gains recognised in the Statement of Comprehensive Income:					
Amount (£m)	**(319)**	198	(9)	(804)	(399)
Percentage of the present value of scheme liabilities	**6.3%**	4.6%	0.2%	19.6%	14.5%

30. Business combinations and asset purchases

Principal acquisitions made during the year are described below.

Business combinations

The business combinations are immaterial in aggregate to the Group's consolidated Financial Statements. The fair values are provisional unless stated otherwise.

Carrot Creek

On 10 January 2012, the Group acquired control of a business comprising a portfolio of interests in a number of gas assets located in west central Alberta, Canada from Encana Corporation for CA$59 million (£37 million) in cash and Direct Energy's existing Entice asset with a fair value of CA$48 million (£30 million). No goodwill arose on the acquisition. The acquisition allows the Group to grow its North American Upstream gas business. The acquisition is included in the Direct Energy – Upstream and wholesale energy segment.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

30. Business combinations and asset purchases continued

Home Warranty of America

On 1 March 2012, the Group acquired 100% of the shares of Home Warranty Holding Corporation as well as the assets of HWOA LLC (HWA) for total cash consideration of $52 million (£32 million) including $10 million (£6 million) of deferred consideration. Goodwill of $47 million (£29 million) arose on the acquisition, of which 40% is expected to be deductible for tax purposes. HWA is a US home warranty protection plan company. The acquisition allows Direct Energy to sell home protection plans nationwide and provides further growth and integration opportunities. The acquisition is included in the Direct Energy – Residential and business services segment.

Energetix Inc and NYSEG Solutions Inc

On 22 August 2012, the Group acquired 100% of the shares of New York based energy retailers Energetix Inc. and NYSEG Solutions Inc. for total cash consideration of $121 million (£77 million) including $5 million (£3 million) of deferred consideration. Goodwill of $43 million (£27 million) arose on the acquisition, of which 100% is expected to be deductible for tax purposes. This acquisition will further strengthen Direct Energy's position as a leading competitive energy retailer in the US Northeast, increasing the number of residential and small commercial customer accounts by approximately 245,000. The acquisition is included in the Direct Energy – Residential energy supply and Business energy supply segments.

Goodwill recognised on the above acquisitions is attributable to enhanced geographical presence, cost savings, synergies and growth opportunities.

2011 Business Combinations – fair value updates

During the year, there have been no significant updates to the fair value entries posted in relation to acquisitions which occurred in 2011. The net impact of fair value updates on goodwill is an increase of £18 million.

Asset purchases

Statoil asset acquisition

On 30 April 2012, the Group completed its acquisition of certain oil and gas production and development assets in the Norwegian North Sea from Statoil for total cash consideration of £770 million with an additional payment of up to $100 million (£62 million) contingent on future production performance. In addition, a tax liability of £144 million was assumed which is included in the purchase cost.

ConocoPhillips asset acquisition

On 30 April 2012, the Group completed its acquisition of certain non-operated interests in the gas and oil producing Statfjord field and associated satellite fields from ConocoPhillips for total cash consideration of £141 million. As part of this transaction, a pre-existing contract with ConocoPhillips with a fair value of £20 million (asset) was novated so that it is now entirely between Group companies. Accordingly, the value of this contract forms part of the asset acquisition cost. In addition, a tax liability of £25 million was assumed which is included in the purchase cost.

Total asset acquisition

During the year, the Group completed its acquisition of a portfolio of non-operated interests in producing oil and gas assets in the UK North Sea from Total for total cash consideration of £133 million. The acquisition of the interests was executed through separate purchase agreements which completed on 11 May, 1 August and 23 August 2012. Certain assets in the original portfolio, when the deal was announced in February 2012, were not acquired since pre-emption rights in the respective fields were exercised.

These asset purchases will help to deliver UK energy security and further expand the Group's upstream business. The acquisitions are included within the Centrica Energy – Gas segment.

31. Disposals, discontinued operations and disposal groups held for sale

On 30 April 2012, the Group disposed of a 50% interest in its Round 3 wind farm, which resulted in a profit on disposal of £43 million.

On 1 June 2011, the Group completed its planned disposal of its European segment with the sale of the trade and assets of Oxxio B.V. for a total consideration of £111 million, which resulted in a loss on disposal of £56 million.

32. Auditors' remuneration

Year ended 31 December	2012 £m	2011 £m
Fees payable to the Company's auditors for the audit of the Company's individual and consolidated financial statements	**4.2**	4.3
Audit of the Company's subsidiaries	**1.1**	1.4
Total fees related to audit of parent and subsidiary entities	**5.3**	5.7
Fees payable to the Company's auditors and its associates for other services:		
Audit related assurance services	**1.0**	0.9
Tax advisory services	**0.2**	0.3
Corporate finance services	**0.2**	0.2
All other services	**0.7**	0.7
	7.4	7.8
Fees in respect of pension scheme audits	**0.1**	0.1

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

32. Auditors' remuneration continued

It is the Group's policy to seek competitive tenders for all major consultancy and advisory projects. Appointments are made taking into account factors including expertise, experience and cost. In addition, the Audit Committee has approved a detailed policy defining the types of work for which the Company's auditors can tender and the approvals required. In the past, the auditors have been engaged on assignments in addition to their statutory audit duties where their expertise and experience with the Group are particularly important, including due diligence reporting and reporting accountant services on acquisitions.

33. Commitments and contingencies

(a) Commitments

The Group procures commodities through a mixture of production from gas fields, power stations, wind farms and procurement contracts. Procurement contracts include short-term forward market purchases of gas and electricity at fixed and floating prices. They also include gas and electricity contracts indexed to market prices and long-term gas contracts with non-gas indexation. The commitments in relation to commodity purchase contracts disclosed below are stated net of amounts receivable under commodity sales contracts, where there is a right of set-off with the counterparty.

The total volume of gas to be taken under certain long-term structured contracts depends on a number of factors, including the actual reserves of gas that are eventually determined to be extractable on an economic basis. The commitments disclosed below are based on the minimum quantities of gas that the Group is contracted to buy at estimated future prices.

The commitments in this note differ in scope and in basis from the maturity analysis of energy derivatives disclosed in note 25. Whilst the commitments in relation to commodity purchase contracts include all purchase contracts, only certain procurement and sales contracts are within the scope of IAS 39 and included in note 25. In addition, the volumes used in calculating the maturity analysis in note 25 are estimated using valuation techniques, rather than being based on minimum contractual quantities and in note 25 there is no offset of amounts receivable under commodity sales contracts where there is a right of set-off with the counterparty.

31 December	2012 £m	2011 £m
Commitments in relation to the acquisition of property, plant and equipment:		
Acquisition of Statoil oil and gas assets	**–**	983
Development of Norwegian oil and gas assets	**283**	–
Development of Cygnus gas field	**88**	–
Development of York gas field	**–**	82
Other capital expenditure	**21**	87
Commitments in relation to the acquisition of intangible assets:		
Renewable obligation certificates to be purchased from joint ventures (i)	**1,376**	1,377
Renewable obligation certificates to be purchased from other parties	**784**	774
EUAs and CERs	**42**	44
Other intangible assets (iv)	**105**	193
Other commitments:		
Commodity purchase contracts (ii)	**51,933**	58,311
LNG capacity	**844**	844
Transportation capacity	**936**	969
Outsourcing of services	**277**	348
Commitments to invest in joint ventures	**174**	234
Other long term commitments	**562**	777
Operating lease commitments:		
Future minimum lease payments under non-cancellable operating leases (iii) (iv)	**974**	950

(i) Renewable obligation certificates are purchased from several joint ventures which produce power from wind energy under long term offtake agreements (up to 15 years). The commitments disclosed above are the gross contractual commitments and do not take into account the Group's economic interest in the joint venture.
(ii) At 31 December the maturity analysis for commodity purchase contracts was: <1 year £9.2 billion, 1-2 years £7.2 billion, 2-3 years £5.9 billion, 3-4 years £5.1 billion, 4-5 years £3.0 billion and >5 years £21.5 billion (2011: <1 year £10.3 billion, 1-2 years £8.0 billion, 2-3 years £6.3 billion, 3-4 years £5.6 billion, 4-5 years £4.7 billion and >5 years £23.4 billion).
(iii) At 31 December the maturity analysis for the total minimum lease payments under non-cancellable operating leases was: <1 year £222 million, 1-2 years £98 million, 2-3 years £82 million, 3-4 years £64 million, 4-5 years £54 million and >5 years £454 million (2011: <1 year £157 million, 1-2 years £130 million, 2-3 years £88 million, 3-4 years £65 million, 4-5 years £54 million and >5 years £456 million).
(iv) Included within future minimum lease payments and other intangible assets are commitments of £67 million (2011: £122 million) relating to exploration activity.

Financial Statements

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

33. Commitments and contingencies continued

Lease payments recognised as an expense in the year were as follows:

Year ended 31 December	2012 £m	2011 £m
Minimum lease payments (net of sub-lease receipts)	125	126
Contingent rents – renewables (i)	130	132

(i) The Group has entered into long-term arrangements with renewable providers to purchase physical power, renewable obligation certificates and levy exemption certificates from renewable sources. Payments made under these contracts are contingent upon actual production and so there is no commitment to a minimum lease payment (2011: nil). Payments made for physical power are charged to the Income Statement as incurred and disclosed as contingent rents.

(b) Guarantees and indemnities

In connection with the Group's energy trading, transportation and upstream activities, certain Group companies have entered into contracts under which they may be required to prepay, provide credit support or other collateral in the event of a significant deterioration in creditworthiness. The extent of credit support is contingent upon the balance owing to the third party at the point of deterioration.

The Group has provided a number of guarantees and indemnities in respect of decommissioning costs; the two most significant indemnities relate to the decommissioning costs associated with the Morecambe and Statfjord fields. These indemnities are to the previous owners of these fields. Under the licence conditions of the fields, the previous owners will have exposure to the decommissioning costs should these liabilities not be fully discharged by the Group.

The security is to be provided when the estimated future net revenue stream from the associated gas field falls below a predetermined proportion of the estimated decommissioning cost. The nature of the security may take a number of different forms and will remain in force until the costs of such decommissioning have been irrevocably discharged and the relevant legal decommissioning notices in respect of the relevant fields have been revoked.

(c) Contingent liabilities

Under the Carbon Emissions Reduction Target ('CERT') scheme, British Gas was required to meet a variety of carbon emissions reduction targets by 31 December 2012. Ofgem has indicated that mitigating actions undertaken after this date will also be taken into account when assessing delivery. Accordingly the Group believes it will have fulfilled the CERT requirements. Ofgem is still to formally conclude on the Group's compliance and has the option of enforcement action if they consider the targets have not been met.

As the outcome of the Ofgem review cannot be predicted with any degree of certainty, it is not possible to accurately assess the impact of enforcement action (if any).

There are no other material contingent liabilities.

34. Related party transactions

During the year, the Group entered into the following arms length transactions with related parties who are not members of the Group and had the following associated balances:

	2012				2011			
	Sale of goods and services £m	Purchase of goods and services £m	Amounts owed from £m	Amounts owed to £m	Sale of goods and services £m	Purchase of goods and services £m	Amounts owed from £m	Amounts owed to £m
Joint ventures:								
Wind farms (as defined in note 16)	27	78	459	47	25	92	312	46
Associates:								
Nuclear (as defined in note 16)	157	598	8	73	278	516	19	65
Other	4	–	18	–	–	8	17	–
	188	676	485	120	303	616	348	111

Investment and funding transactions for joint ventures and associates are disclosed in note 16. The terms of the outstanding balances related to trade receivables from related parties are typically 30 to 120 days. The balances are unsecured and will be settled in cash. No provision for bad or doubtful debts owed by related parties was required (2011: nil).

Key management personnel comprise members of the Board and Executive Committee, a total of 14 individuals at 31 December 2012 (2011: 15). Key management personnel and their families purchase gas, electricity and home services products from the Group for domestic purposes on terms equal to those for other employees of the Group.

Remuneration of key management personnel

31 December	2012 £m	2011 £m
Short-term benefits	8	7
Post-employment benefits	2	2
Share-based payments	6	8
	16	17

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

35. Fixed-fee service and insurance contracts

The fixed-fee service claims and insurance claims notified during the year were £92 million (2011: £115 million) and £342 million (2011: £356 million) respectively and were exactly matched by expenses related to fixed-fee service and insurance contracts. All claims are settled immediately and in full. Due to the short lead time between claims being incurred and claims being rectified, there are no material provisions outstanding at the Balance Sheet date (2011: nil).

Year ended 31 December	2012 £m	2011 £m
Total revenue	**1,239**	1,167
Expenses relating to fixed-fee service and insurance contracts	**954**	904
Deferred income	**84**	68
Accrued income	**35**	28

The Group considers the adequacy of estimated future cash flows under the contracts to meet expected future costs under the contracts. Any deficiency is charged immediately to the Income Statement. Service requests are sensitive to the reliability of appliances as well as the impact of weather conditions. Each incremental 1% increase in service and insurance requests would impact profit and equity by approximately £10 million (2011: £9 million). The contracts are not exposed to any interest rate risk or significant credit risk and do not contain any embedded derivatives. See note S8 for more information.

36. Events after the balance sheet date

Dividends

The Directors propose a final dividend of 11.78 pence per ordinary share (totalling £602 million) for the year ended 31 December 2012. The dividend will be submitted for formal approval at the Annual General Meeting to be held on 13 May 2013 and, subject to approval, will be paid on 12 June 2013 to those shareholders registered on 26 April 2013.

Nuclear new build and share repurchase programme

As part of the 2009 transaction to acquire a 20% interest in British Energy, EDF Energy and the Group formed an 80/20 arrangement to undertake pre-development activities for a nuclear new build programme, with the intention of constructing, operating and decommissioning four European Pressurised Nuclear Reactors. On 4 February 2013, the Group announced its decision not to proceed with this nuclear new build investment. Accordingly, the Group has recorded an impairment of £231 million at the year end. This amount includes the carrying value of its investment in NNB Holding Company Limited as well as value attributed to nuclear new build in the British Energy acquisition. No further impairments are expected as a result of this decision and the Group's 20% interest in the existing nuclear power stations in the UK remains unaffected.

As a result of this decision, the Group also announced on 4 February 2013 its intention to launch a £500 million share repurchase programme to return surplus capital to shareholders, to be conducted over 12 months.

SUPPLEMENTARY INFORMATION

S1. General information

Centrica plc is a Company domiciled and incorporated in the UK. The address of the registered office is Millstream, Maidenhead Road, Windsor, Berkshire, SL4 5GD. The nature of the Group's operations and principal activities are set out in note S4 and in the Directors' Report – Business Review on pages 5 to 50.

The consolidated Financial Statements of Centrica plc are presented in pounds sterling. Operations and transactions conducted in currencies other than pounds sterling are included in the consolidated Financial Statements in accordance with the foreign currencies accounting policy set out in note S2.

S2. Summary of significant accounting policies

Income Statement presentation

The Group's Income Statement and segmental note separately identify the effects of re-measurement of certain financial instruments, and items which are exceptional, in order to provide readers with a clear and consistent presentation of the Group's underlying performance, as described below.

(i) Certain re-measurements

As part of its energy procurement activities, the Group enters into a range of commodity contracts designed to achieve security of energy supply. These contracts comprise both purchases and sales and cover a wide range of volumes, prices and timescales. The majority of the underlying supply comes from high-volume, long-term contracts which are complemented by short-term arrangements. These short-term contracts are entered into for the purpose of balancing energy supplies and customer demand and to optimise the price paid by the Group. Short-term demand can vary significantly as a result of factors such as weather, power generation profiles and short-term movements in market prices.

Many of the energy procurement contracts are held for the purpose of receipt or delivery of commodities in accordance with the Group's purchase, sale or usage requirements and are therefore out of scope of IAS 39. However, a number of contracts are considered to be derivative financial instruments and are required to be fair valued under IAS 39, primarily because their terms include the ability to trade elements of the contracted volumes on a net-settled basis.

The Group has shown the fair value adjustments arising on these contracts separately in the certain re-measurements column. This is because the intention of management is, subject to short-term demand balancing, to use these energy supplies to meet customer demand. Accordingly, management believes the ultimate net charge to cost of sales will be consistent with the price of energy agreed in these contracts and that the fair value adjustments will reverse as the energy is supplied over the life of the contract. This makes the fair value re-measurements very different in nature from costs arising from the physical delivery of energy in the year.

At the balance sheet date the fair value represents the difference between the prices agreed in the respective contracts and the actual or anticipated market price of acquiring the same amount of energy on the open market. The movement in the fair value taken to certain re-measurements in the Group Income Statement represents the unwinding of the contracted volume delivered or consumed during the year, combined with the change in fair value of future contracted energy as a result of movements in forward energy prices during the year.

The Group utilises over the counter and exchange traded instruments to optimise the price paid by the Group. The Group recognises the realised gains and losses on these contracts in business performance when the underlying transaction occurs.

As an integrated energy business the Group also enters into a range of commodity contracts designed to secure the value of its underlying production, generation, storage and transportation assets, consistent with an integrated energy business in the UK and North America. The fair value movements on these contracts are also shown separately in the certain re-measurements column. This is because the fair value movements on these contracts are not matched with fair value movements of the underlying assets, since not all the underlying assets are fair valued. These adjustments represent the significant majority of the items included in certain re-measurements.

In addition to these, however, the Group has identified a number of comparable contractual arrangements where the difference between the price which the Group expects to pay or receive under a contract and the market price is required to be fair valued by IAS 39. These additional items relate to cross-border transportation or transmission capacity, storage capacity and contracts relating to the sale of energy by-products, on which economic value has been created which is not wholly recognised under the requirements of IAS 39. For these arrangements the related fair value adjustments are also included under certain re-measurements.

These arrangements are managed separately from proprietary energy trading activities where trades are entered into speculatively for the purpose of making profits in their own right. These proprietary trades are included in the results before certain re-measurements.

In addition, certain re-measurements include the effects of unwinding the acquisition-date fair values attributable to forward energy procurement and energy sales contracts arising on the acquisition of Strategic Investments, as described in note 2. The Group has shown the effect of unwinding the acquisition-date fair values attributable to forward energy procurement and energy sales contracts for these investments separately as a certain re-measurement as the intention is to use these energy supplies in the normal course of business and management believes the ultimate net charge reflected before the unwind of acquisition-date fair values will be consistent with the price of energy agreed within these contracts. Such presentation is consistent with the internal performance measures used by the Group.

(ii) Exceptional items

As permitted by IAS 1 (Revised), Presentation of Financial Statements, certain items are presented separately. The items that the Group separately presents as exceptional are items which are of a non-recurring nature and in the judgement of the Directors, need to be disclosed separately by virtue of their nature, size or incidence in order to obtain a clear and consistent presentation of the Group's underlying business performance.

Basis of consolidation

The Group Financial Statements consolidate the Financial Statements of the Company and entities controlled by the Company (its subsidiaries) up to 31 December each year, and incorporates its share of the results of jointly controlled entities and associates using the equity method of accounting.

Control is achieved where the Company has the power to govern the financial and operating policies of an investee entity so as to obtain benefits from its activities.

The results of subsidiaries acquired or disposed of during the year are consolidated from the effective date of acquisition or up to the effective date of disposal, as appropriate. Where necessary, adjustments are made to the Financial Statements of subsidiaries, associates and jointly-controlled entities to bring the accounting policies used into line with those used by the Group.

When the Group ceases to have control or significant influence, any retained interest in the entity is re-measured to its fair value with the change in carrying amount recognised in profit or loss. This fair value becomes the initial carrying amount for the purposes of subsequently accounting for the retained interest as a joint venture, associate or financial asset.

Segmental reporting

The Group's operating segments are reported in a manner consistent with the internal reporting provided to and regularly reviewed by the Group's Executive Committee for the purposes of evaluating segment performance and allocating resources.

Revenue

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be measured reliably. Revenue includes amounts receivable for goods and services provided in the normal course of business, net of discounts, rebates, VAT and other sales-related taxes.

Energy supply: revenue is recognised on the basis of energy supplied during the year. Revenue for energy supply activities includes an assessment

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SUPPLEMENTARY INFORMATION CONTINUED

S2. Summary of significant accounting policies continued

of energy supplied to customers between the date of the last meter reading and the year end (unread). Unread gas and electricity is estimated using historical consumption patterns, taking into account the industry reconciliation process for total gas and total electricity usage by supplier, and is included in accrued energy income within trade and other receivables.

Proprietary energy trading: revenue comprises both realised (settled) and unrealised (fair value changes) net gains and losses from trading in physical and financial energy contracts.

Fixed-fee service and insurance contracts: revenue from these contracts is recognised in the Group Income Statement with regard to the incidence of risk over the life of the contract, reflecting the seasonal propensity of claims to be made under the contracts and the benefits receivable by the customer, which span the life of the contract as a result of emergency maintenance being available throughout the contract term.

Amounts paid in advance greater than recognised revenue are treated as deferred income, with any paid in arrears recognised as accrued income. For one-off services, such as installations, revenue is recognised at the date of service provision.

Storage services: storage capacity revenues are recognised evenly over the contract period, whilst commodity revenues for the injection and withdrawal of gas are recognised at the point of gas flowing into or out of the storage facilities. Gas purchases and gas sales transactions entered into to optimise the performance of the gas storage facilities are presented net within revenue.

Upstream production: revenue associated with exploration and production sales (of natural gas, crude oil and condensates) is recognised when title passes to the customer. Revenue from the production of natural gas, oil and condensates in which the Group has an interest with other producers is recognised based on the Group's working interest and the terms of the relevant production sharing arrangements (the entitlement method). Where differences arise between production sold and the Group's share of production, this is accounted for as an overlift or underlift (see separate accounting policy). Purchases and sales entered into to optimise the performance of production facilities are presented net within revenue.

Power generation: revenue is recognised on the basis of power supplied during the period. Power purchases and sales entered into to optimise the performance of power generation facilities are presented net within revenue.

Interest income: interest income is accrued on a time basis, by reference to the principal outstanding and at the effective interest rate applicable, which is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset to that asset's net carrying value.

Cost of sales

Energy supply includes the cost of gas and electricity produced and purchased during the year taking into account the industry reconciliation process for total gas and total electricity usage by supplier, and related transportation, distribution, royalty costs and bought-in materials and services.

Cost of sales relating to fixed-fee service and insurance contracts includes direct labour and related overheads on installation work, repairs and service contracts in the year.

Borrowing costs

Borrowing costs that arise in connection with the acquisition, construction or production of a qualifying asset are capitalised and subsequently amortised in line with the depreciation of the related asset. Borrowing costs are capitalised from the time of acquisition or from the beginning of construction or production until the point at which the qualifying asset is ready for use. Where a specific financing arrangement is in place, the specific borrowing rate for that arrangement is applied. For non-specific financing arrangements, a Group financing rate representative of the weighted average borrowing rate of the Group is used. Borrowing costs not arising in connection with the acquisition, construction or production of a qualifying asset are expensed.

Employee share schemes

The Group operates a number of employee share schemes, detailed in the Remuneration Report on pages 61 to 75 and in note S7, under which it makes equity-settled share-based payments to certain employees. Equity-settled share-based payments are measured at fair value at the date of grant (excluding the effect of non-market-based vesting conditions). The fair value determined at the grant date is expensed on a straight-line basis together with a corresponding increase in equity over the vesting period, based on the Group's estimate of the number of awards that will vest, and adjusted for the effect of non-market-based vesting conditions.

Fair value is measured using methods appropriate to each of the different schemes as follows:

LTIS: EPS, EP and KPI awards	Market value on the date of grant
LTIS: TSR awards	A Monte Carlo simulation to predict the total shareholder return performance
SAS and DMSS	Market value on the date of grant

Foreign currencies

The consolidated Financial Statements are presented in pounds sterling, which is the functional currency of the Company and the Group's presentation currency. Each entity in the Group determines its own functional currency and items included in the Financial Statements of each entity are measured using that functional currency. Transactions in foreign currencies are, on initial recognition, recorded at the functional currency rate ruling at the date of the transaction.

Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange ruling at the balance sheet date. All differences are included in the Group Income Statement for the period with the exception of exchange differences on foreign currency borrowings that provide a hedge against a net investment in a foreign entity. These are taken directly to equity until the disposal or partial disposal of the net investment, at which time they are recognised in the Group Income Statement.

Non-monetary items that are measured in terms of historical cost in a currency other than the functional currency of the entity concerned are translated using the exchange rates as at the dates of the initial transactions.

For the purpose of presenting consolidated Financial Statements, the assets and liabilities of the Group's foreign subsidiary undertakings, jointly controlled entities and associates are translated into pounds sterling at exchange rates prevailing on the balance sheet date. The results of foreign subsidiary undertakings, jointly controlled entities and associates are translated into pounds sterling at average rates of exchange for the relevant period.

Exchange differences arising from the retranslation of the opening net assets and the results are transferred to the Group's foreign currency translation reserve, a separate component of equity, and are reported in the Statement of Comprehensive Income. In the event of the disposal of an undertaking with assets and liabilities denominated in a foreign currency, the cumulative translation difference arising in the foreign currency translation reserve is charged or credited to the Group Income Statement on disposal.

Exchange differences on foreign currency borrowings, foreign currency swaps and forward exchange contracts used to hedge foreign currency net investments in foreign subsidiary undertakings, jointly controlled entities and associates are taken directly to reserves and are reported in the Statement of Comprehensive Income. All other exchange movements are recognised in the Group Income Statement for the year.

Business combinations and goodwill

The acquisition of subsidiaries is accounted for using the purchase method. The cost of the acquisition is measured as the cash paid and the aggregate of the fair values, at the date of exchange, of other assets transferred, liabilities incurred or assumed, and equity instruments issued by the Group in exchange for control of the acquiree. Acquisition-related costs are expensed as incurred. The acquiree's identifiable assets, liabilities and contingent liabilities that meet the conditions for recognition under IFRS 3 (revised), Business Combinations,

SUPPLEMENTARY INFORMATION CONTINUED

S2. Summary of significant accounting policies continued

are recognised at their fair value at the acquisition date, except for non-current assets (or disposal groups) that are classified as held for resale in accordance with IFRS 5, Non-Current Assets Held for Sale and Discontinued Operations, which are recognised and measured at fair value less costs to sell.

Goodwill arising on a business combination represents the excess of the cost of acquisition over the Group's interest in the fair value of the identifiable assets and liabilities of a subsidiary, jointly controlled entity or associate at the date of acquisition. Goodwill is initially recognised as an asset at cost and is subsequently measured at cost less any accumulated impairment losses. If, after reassessment, the Group's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities exceeds the cost of the business combination, the excess is recognised immediately in the Group Income Statement.

On disposal of a subsidiary, associate or joint venture entity, any amount of goodwill attributed to that entity is included in the determination of the profit or loss on disposal.

Other intangible assets

Intangible assets acquired separately are measured on initial recognition at cost. Intangible assets include emissions trading schemes, renewable obligation certificates, certain exploration and evaluation expenditures, brands and application software, the accounting policies for which are dealt with separately below. For purchased application software, for example investments in customer relationship management and billing systems, cost includes contractors' charges, materials, directly-attributable labour and directly-attributable overheads.

Capitalisation begins when expenditure for the asset is being incurred and activities necessary to prepare the asset for use are in progress. Capitalisation ceases when substantially all the activities that are necessary to prepare the asset for use are complete. Amortisation commences at the point of commercial deployment. The cost of intangible assets acquired in a business combination is their fair value as at the date of acquisition.

Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses. The useful lives of intangible assets are assessed to be either finite or indefinite. Intangible assets with finite lives are amortised over their useful economic life and assessed for impairment whenever there is an indication that the intangible asset could be impaired. The amortisation period and the amortisation method for an intangible asset are reviewed at least at each financial year end. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset are accounted for on a prospective basis by changing the amortisation period or method, as appropriate, and treated as changes in accounting estimates.

Intangible assets are derecognised on disposal, or when no future economic benefits are expected from their use.

Intangible assets with indefinite useful lives are tested for impairment annually, and whenever there is an indication that the intangible asset could be impaired, either individually or at the CGU level. Such intangibles are not amortised. The useful life of an intangible asset with an indefinite useful life is reviewed annually to determine whether the indefinite life assessment continues to be supportable. If not, the change in the useful life assessment from indefinite to finite is made on a prospective basis.

The amortisation periods for the principal categories of intangible assets are as follows:

Application software	up to 15 years
Licences	up to 20 years
Contractual customer relationships	up to 20 years
Strategic identifiable acquired brand	Indefinite

EU Emissions Trading Scheme and renewable obligations certificates

Granted carbon dioxide emissions allowances received in a period are recognised initially at nominal value (nil value). Purchased carbon dioxide emissions allowances are recognised initially at cost (purchase price) within intangible assets. A liability is recognised when the level of emissions exceeds the level of allowances granted. The liability is measured at the cost of purchased allowances up to the level of purchased allowances held, and then at the market price of allowances ruling at the balance sheet date, with movements in the liability recognised in operating profit.

Forward contracts for the purchase or sale of carbon dioxide emissions allowances are measured at fair value with gains and losses arising from changes in fair value recognised in the Group Income Statement. The intangible asset is surrendered and the liability is utilised at the end of the compliance period to reflect the consumption of economic benefits.

Purchased renewable obligation certificates are recognised initially at cost within intangible assets. A liability for the renewables obligation is recognised based on the level of electricity supplied to customers, and is calculated in accordance with percentages set by the UK Government and the renewable obligation certificate buyout price for that period.

The intangible asset is surrendered and the liability is utilised at the end of the compliance period to reflect the consumption of economic benefits. Any recycling benefit related to the submission of renewable obligation certificates is recognised in the Group Income Statement when received.

Exploration, evaluation, development and production assets

The Group uses the successful efforts method of accounting for exploration and evaluation expenditure. Exploration and evaluation expenditure associated with an exploration well, including acquisition costs related to exploration and evaluation activities, are capitalised initially as intangible assets. Certain expenditures such as geological and geophysical exploration costs are expensed. If the prospects are subsequently determined to be successful on completion of evaluation, the relevant expenditure including licence acquisition costs is transferred to PP&E and is subsequently depreciated on a unit of production basis. If the prospects are subsequently determined to be unsuccessful on completion of evaluation, the associated costs are expensed in the period in which that determination is made.

All field development costs are capitalised as PP&E. Such costs relate to the acquisition and installation of production facilities and include development drilling costs, project-related engineering and other technical services costs. PP&E, including rights and concessions related to production activities, are depreciated from the commencement of production in the fields concerned, using the unit of production method, based on all of the 2P reserves of those fields. Changes in these estimates are dealt with prospectively.

The net carrying value of fields in production and development is compared on a field-by-field basis with the likely discounted future net revenues to be derived from the remaining commercial reserves. An impairment loss is recognised where it is considered that recorded amounts are unlikely to be fully recovered from the net present value of future net revenues. Exploration assets are reviewed annually for indicators of impairment and production and development assets are tested annually for impairment.

Interests in joint ventures and associates

Under the equity method, investments in jointly controlled entities and associates are carried at cost plus post-acquisition changes in the Group's share of net assets, less any impairment in value in individual investments. The Group Income Statement reflects the Group's share of the results of operations after tax and interest.

Certain exploration and production activity is conducted through joint ventures, where the venturers have a direct interest in and jointly control the assets of the venture. The results, assets, liabilities and cash flows of these jointly controlled assets are included in the consolidated Financial Statements in proportion to the Group's interest.

SUPPLEMENTARY INFORMATION CONTINUED

S2. Summary of significant accounting policies continued

Property, plant and equipment

PP&E is included in the Group Balance Sheet at cost, less accumulated depreciation and any provisions for impairment. The initial cost of an asset comprises its purchase price or construction cost and any costs directly attributable to bringing the asset into operation. The purchase price or construction cost is the aggregate amount paid and the fair value of any other consideration given to acquire the asset.

Subsequent expenditure in respect of items of PP&E such as the replacement of major parts, major inspections or overhauls, are capitalised as part of the cost of the related asset where it is probable that future economic benefits will arise as a result of the expenditure and the cost can be reliably measured. All other subsequent expenditure, including the costs of day-to-day servicing, repairs and maintenance, is expensed as incurred.

Freehold land is not depreciated. Other PP&E, with the exception of upstream production assets (see above), are depreciated on a straight-line basis at rates sufficient to write off the cost, less estimated residual values, of individual assets over their estimated useful lives. The depreciation periods for the principal categories of assets are as follows:

Freehold and leasehold buildings	up to 50 years
Plant	5 to 20 years
Power stations and wind farms	up to 30 years
Equipment and vehicles	3 to 10 years
Storage	up to 40 years

Assets held under finance leases are depreciated over their expected useful economic lives on the same basis as for owned assets, or where shorter, the lease term.

The carrying values of PP&E are reviewed for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable. Residual values and useful lives are reassessed annually and if necessary changes are accounted for prospectively.

Impairment of property, plant and equipment, intangible assets, investments in joint ventures and associates and goodwill

The Group reviews the carrying amounts of PP&E, intangible assets, interests in joint ventures and associates and goodwill annually, or more frequently if events or changes in circumstances indicate that the recoverable amounts may be lower than their carrying amounts. Where an asset does not generate cash flows that are independent from other assets, the Group estimates the recoverable amount of the CGU to which the asset belongs. The recoverable amount is the higher of value in use and fair value less costs to sell. At inception, goodwill is allocated to each of the Group's CGUs or groups of CGUs that expect to benefit from the business combination in which the goodwill arose. If the recoverable amount of an asset (or CGU) is estimated to be less than its carrying amount, the carrying amount of the asset (or CGU) is reduced to its recoverable amount. Any impairment is expensed immediately in the Group Income Statement. Any goodwill impairment loss is allocated first to reduce the carrying amount of any goodwill allocated to the CGU and then to the other assets of the unit pro rata on the basis of the carrying amount of each asset in the unit.

An impairment loss is reversed only if there has been a change in the estimate used to determine the asset's recoverable amount since the last impairment loss was recognised, with the exception of goodwill impairment which is never reversed. Where an impairment loss subsequently reverses, the carrying amount of the asset (or CGU) is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset (or CGU) in prior years. A reversal of an impairment loss is recognised in the Group Income Statement immediately. After such a reversal the depreciation or amortisation charge, where relevant, is adjusted in future periods to allocate the asset's revised carrying amount, less any residual value, on a systematic basis over its remaining useful life.

Overlift and underlift

Offtake arrangements for oil and gas produced from jointly owned operations are often such that it is not practical for each participant to receive or sell its precise share of the overall production during the period. This results in short-term imbalances between cumulative production entitlement and cumulative sales, referred to as overlift and underlift.

An overlift payable, or underlift receivable, is recognised at the balance sheet date within Trade and other payables, or Trade and other receivables, respectively and measured at market value, with movements in the period recognised within cost of sales.

Leases

The determination of whether an arrangement is, or contains, a lease is based on the substance of the arrangement and requires an assessment of whether the fulfilment of the arrangement is dependent on the use of a specific asset or assets and whether the arrangement conveys a right to use the asset. Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases. Assets held under finance leases are capitalised and included in PP&E at their fair value, or if lower, at the present value of the minimum lease payments, each determined at the inception of the lease. The obligations relating to finance leases, net of finance charges in respect of future periods, are included within bank loans and other borrowings, with the amount payable within 12 months included in bank overdrafts and loans within current liabilities.

Lease payments are apportioned between finance charges and reduction of the finance lease obligation so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged directly against income.

Payments under operating leases are charged to the Group Income Statement on a straight-line basis over the term of the relevant lease.

Inventories

Inventories are valued on a weighted-average cost basis and at the lower of cost and estimated net realisable value after allowance for redundant and slow-moving items.

Decommissioning costs

Provision is made for the net present value of the estimated cost of decommissioning gas production facilities at the end of the producing lives of fields, and storage facilities and power stations at the end of the useful life of the facilities, based on price levels and technology at the balance sheet date.

When this provision gives access to future economic benefits, a decommissioning asset is recognised and included as part of the associated PP&E and depreciated accordingly. Changes in these estimates and changes to the discount rates are dealt with prospectively and reflected as an adjustment to the provision and corresponding decommissioning asset included within PP&E. The unwinding of the discount on the provision is included in the Group Income Statement within interest expense.

Non-current assets and disposal groups held for sale and discontinued operations

Non-current assets (and disposal groups) classified as held for sale are measured at the lower of carrying amount and fair value less costs to sell. No depreciation is charged in respect of non-current assets classified as held for sale.

Non-current assets and disposal groups are classified as held for sale if their carrying amount will be recovered through a sale transaction rather than through continuing use. This condition is regarded as met only when the sale is highly probable and the asset (or disposal group) is available for immediate sale in its present condition. Management must be committed to the sale which should be expected to qualify for recognition as a completed sale within one year from the date of classification.

The profits or losses and cash flows that relate to a major component of the Group or geographical region that has been sold or is classified as held

SUPPLEMENTARY INFORMATION CONTINUED

S2. Summary of significant accounting policies continued

for sale are presented separately from continuing operations as discontinued operations within the Group Income Statement and Group Cash Flow Statement.

Pensions and other post-employment benefits

The Group operates a number of defined benefit pension schemes. The cost of providing benefits under the defined benefit schemes is determined separately for each scheme using the projected unit credit actuarial valuation method. Actuarial gains and losses are recognised in full in the period in which they occur. They are recognised in the Statement of Comprehensive Income.

The cost of providing retirement pensions and other benefits is charged to the Group Income Statement over the periods benefiting from employees' service. Past service cost is recognised immediately to the extent that the benefits are already vested, and otherwise is amortised on a straight-line basis over the average period until the benefits become vested. The difference between the expected return on scheme assets and the change in present value of scheme obligations resulting from the passage of time is recognised in the Group Income Statement within interest income or interest expense.

The retirement benefit liability or asset recognised in the Group Balance Sheet represents the present value of the defined benefit obligation of the schemes as adjusted for unrecognised past service cost, and the fair value of the schemes' assets. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows using interest rates of high-quality corporate bonds that are denominated in the currency in which the benefits are paid, and that have terms of maturity approximating to the terms of the related pension liability.

Payments to defined contribution retirement benefit schemes are charged as an operating expense as they fall due.

Provisions

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, that can be measured reliably, and it is probable that the Group will be required to settle that obligation. Provisions are measured at the Directors' best estimate of the expenditure required to settle the obligation at the balance sheet date, and are discounted to present value where the effect is material. Where discounting is used, the increase in the provision due to the passage of time is recognised in the Group Income Statement within interest expense. Onerous contract provisions are recognised where the unavoidable costs of meeting the obligations under a contract exceed the economic benefits expected to be received under it. Contracts to purchase or sell energy are reviewed on a portfolio basis given the fungible nature of energy, whereby it is assumed that the highest priced purchase contract supplies the highest priced sales contract and the lowest priced sales contract is supplied by the lowest priced purchase contract.

Taxation

Current tax, including UK corporation tax, UK petroleum revenue tax and foreign tax is provided at amounts expected to be paid (or recovered) using the tax rates and laws that have been enacted or substantively enacted by the balance sheet date.

Deferred tax is recognised in respect of all temporary differences identified at the balance sheet date, except to the extent that the deferred tax arises from the initial recognition of goodwill (if amortisation of goodwill is not deductible for tax purposes) or the initial recognition of an asset or liability in a transaction which is not a business combination and at the time of the transaction affects neither accounting profit nor taxable profit and loss. Temporary differences are differences between the carrying amount of the Group's assets and liabilities and their tax base.

Deferred tax liabilities may be offset against deferred tax assets within the same taxable entity or qualifying local tax group. Any remaining deferred tax asset is recognised only when, on the basis of all available evidence, it can be regarded as probable that there will be suitable taxable profits, within the same jurisdiction, in the foreseeable future, against which the deductible temporary difference can be utilised.

Deferred tax is provided on temporary differences arising on subsidiaries, jointly controlled entities and associates, except where the timing of the reversal of the temporary difference can be controlled and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred tax is measured at the average tax rates that are expected to apply in the periods in which the asset is realised or liability settled, based on tax rates and laws that have been enacted or substantively enacted by the balance sheet date. Measurement of deferred tax liabilities and assets reflects the tax consequences expected from the manner in which the asset or liability is recovered or settled.

Financial instruments

Financial assets and financial liabilities are recognised in the Group Balance Sheet when the Group becomes a party to the contractual provisions of the instrument. Financial assets are de-recognised when the Group no longer has the rights to cash flows, the risks and rewards of ownership or control of the asset. Financial liabilities are de-recognised when the obligation under the liability is discharged, cancelled or expires.

(a) Trade receivables

Trade receivables are recognised and carried at original invoice amount less an allowance for any uncollectible amounts. Provision is made when there is objective evidence that the Group may not be able to collect the trade receivable. Balances are written off when recoverability is assessed as being remote. If collection is due in one year or less they are classified as current assets. If not they are presented as non-current assets.

(b) Trade payables

Trade payables are recognised at original invoice amount. If payment is due within one year or less they are classified as current liabilities. If not, they are presented as non-current liabilities.

(c) Share capital

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of new shares are shown in equity as a deduction from the proceeds received. Own equity instruments that are reacquired (treasury or own shares) are deducted from equity. No gain or loss is recognised in the Group Income Statement on the purchase, sale, issue or cancellation of the Group's own equity instruments.

(d) Cash and cash equivalents

Cash and cash equivalents comprise cash in hand and current balances with banks and similar institutions, which are readily convertible to known amounts of cash and which are subject to insignificant risk of changes in value and have an original maturity of three months or less.

For the purpose of the Group Cash Flow Statement, cash and cash equivalents consist of cash and cash equivalents as defined above, net of outstanding bank overdrafts.

(e) Interest-bearing loans and other borrowings

All interest-bearing loans and other borrowings are initially recognised at fair value net of directly attributable transaction costs. After initial recognition, interest-bearing loans and other borrowings are subsequently measured at amortised cost using the effective interest method, except when they are the hedged item in an effective fair value hedge relationship where the carrying value is also adjusted to reflect the fair value movements associated with the hedged risks. Such fair value movements are recognised in the Group Income Statement. Amortised cost is calculated by taking into account any issue costs, discount or premium.

(f) Available-for-sale financial assets

Available-for-sale financial assets are those non-derivative financial assets that are designated as available-for-sale, which are recognised initially at fair value within the Group Balance Sheet. Available-for-sale financial assets are re-measured subsequently at fair value with gains and losses arising from changes in fair value recognised directly in equity and presented in the Statement of Comprehensive Income, until the asset is disposed of or is determined to be impaired, at which time the cumulative gain or loss previously recognised in equity is included in the Group Income Statement for the period. Accrued interest or dividends arising on available-for-sale financial assets are recognised in the Group Income Statement.

SUPPLEMENTARY INFORMATION CONTINUED

S2. Summary of significant accounting policies continued

At each balance sheet date the Group assesses whether there is objective evidence that available-for-sale financial assets are impaired. If any such evidence exists, cumulative losses recognised in equity are removed from equity and recognised in the Group Income Statement. The cumulative loss removed from equity represents the difference between the acquisition cost and current fair value, less any impairment loss on that financial asset previously recognised in the Group Income Statement.

Impairment losses recognised in the Group Income Statement for equity investments classified as available-for-sale are not subsequently reversed through the Income Statement. Impairment losses recognised in the Group Income Statement for debt instruments classified as available-for-sale are subsequently reversed if an increase in the fair value of the instrument can be objectively related to an event occurring after the recognition of the impairment loss.

(g) Financial assets at fair value through profit or loss

The Group holds investments in gilts which it designates as fair value through profit or loss. Investments are measured at fair value on initial recognition and are re-measured to fair value in each subsequent reporting period. Gains and losses arising from changes in fair value are recognised in the Group Income Statement within interest income or interest expense.

(h) Derivative financial instruments

The Group routinely enters into sale and purchase transactions for physical delivery of gas, power and oil. A portion of these transactions take the form of contracts that were entered into and continue to be held for the purpose of receipt or delivery of the physical commodity in accordance with the Group's expected sale, purchase or usage requirements, and are not within the scope of IAS 39.

Certain purchase and sales contracts for the physical delivery of gas, power and oil are within the scope of IAS 39 due to the fact that they net settle or contain written options. Such contracts are accounted for as derivatives under IAS 39 and are recognised in the Group Balance Sheet at fair value. Gains and losses arising from changes in fair value on derivatives that do not qualify for hedge accounting are taken directly to the Group Income Statement for the year.

The Group uses a range of derivatives for both trading and to hedge exposures to financial risks, such as interest rate, foreign exchange and energy price risks, arising in the normal course of business. The use of derivative financial instruments is governed by the Group's policies which are approved by the Board of Directors. Further detail on the Group's risk management policies is included within the Directors' Report - Governance on pages 58 to 60 and in note S3.

The accounting treatment for derivatives is dependent on whether they are entered into for trading or hedging purposes. A derivative instrument is considered to be used for hedging purposes when it alters the risk profile of an underlying exposure of the Group in line with the Group's risk management policies and is in accordance with established guidelines, which require the hedging relationship to be documented at its inception, ensure that the derivative is highly effective in achieving its objective, and require that its effectiveness can be reliably measured. The Group also holds derivatives which are not designated as hedges and are held for trading.

All derivatives are recognised at fair value on the date on which the derivative is entered into and are re-measured to fair value at each reporting date. Derivatives are carried as assets when the fair value is positive and as liabilities when the fair value is negative. Derivative assets and derivative liabilities are offset and presented on a net basis only when both a legal right of set-off exists and the intention to net settle the derivative contracts is present.

The Group enters into certain energy derivative contracts covering periods for which observable market data does not exist. The fair value of such derivatives is estimated by reference in part to published price quotations from active markets, to the extent that such observable market data exists, and in part by using valuation techniques, whose inputs include data which is not based on or derived from observable markets. Where the fair value at initial recognition for such contracts differs from the transaction price, a fair value gain or fair value loss will arise. This is referred to as a day-one gain or day-one loss. Such gains and losses are deferred and amortised to the Group Income Statement based on volumes purchased or delivered over the contractual period until such time observable market data becomes available. When observable market data becomes available, any remaining deferred day-one gains or losses are recognised within the Group Income Statement. Recognition of the gains or losses resulting from changes in fair value depends on the purpose for issuing or holding the derivative. For derivatives that do not qualify for hedge accounting, any gains or losses arising from changes in fair value are taken directly to the Group Income Statement and are included within gross profit or interest income and interest expense. Gains and losses arising on derivatives entered into for speculative energy trading purposes are presented on a net basis within revenue.

Embedded derivatives: derivatives embedded in other financial instruments or other host contracts are treated as separate derivatives when their risks and characteristics are not closely related to those of the host contracts and the host contracts are not carried at fair value, with gains or losses reported in the Group Income Statement. The closely-related nature of embedded derivatives is reassessed when there is a change in the terms of the contract which significantly modifies the future cash flows under the contract. Where a contract contains one or more embedded derivatives, and providing that the embedded derivative significantly modifies the cash flows under the contract, the option to fair value the entire contract may be taken and the contract will be recognised at fair value with changes in fair value recognised in the Group Income Statement.

(i) Hedge accounting

For the purposes of hedge accounting, hedges are classified either as fair value hedges, cash flow hedges or hedges of net investments in foreign operations.

Fair value hedges: a derivative is classified as a fair value hedge when it hedges the exposure to changes in the fair value of a recognised asset or liability. Any gain or loss from re-measuring the hedging instrument to fair value is recognised immediately in the Group Income Statement. Any gain or loss on the hedged item attributable to the hedged risk is adjusted against the carrying amount of the hedged item and recognised in the Group Income Statement. The Group discontinues fair value hedge accounting if the hedging instrument expires or is sold, terminated or exercised, the hedge no longer qualifies for hedge accounting or the Group revokes the designation. Any adjustment to the carrying amount of a hedged financial instrument for which the effective interest method is used is amortised to the Group Income Statement. Amortisation may begin as soon as an adjustment exists and shall begin no later than when the hedged item ceases to be adjusted for changes in its fair value attributable to the risk being hedged.

Cash flow hedges: a derivative is classified as a cash flow hedge when it hedges exposure to variability in cash flows that is attributable to a particular risk either associated with a recognised asset, liability or a highly probable forecast transaction. The portion of the gain or loss on the hedging instrument which is effective is recognised directly in equity while any ineffectiveness is recognised in the Group Income Statement. The gains or losses that are recognised directly in equity are transferred to the Group Income Statement in the same period in which the highly probable forecast transaction affects income, for example when the future sale of physical gas or physical power actually occurs. Where the hedged item is the cost of a non-financial asset or liability, the amounts taken to equity are transferred to the initial carrying amount of the non-financial asset or liability on its recognition. Hedge accounting is discontinued when the hedging instrument expires or is sold, terminated or exercised without replacement or rollover, no longer qualifies for hedge accounting or the Group revokes the designation. At that point in time, any cumulative gain or loss on the hedging instrument recognised in equity remains in equity until the highly probable forecast transaction occurs. If the transaction is no longer expected to occur, the cumulative gain or loss recognised in equity is recognised in the Group Income Statement.

Net investment hedges: hedges of net investments in foreign operations are accounted for similarly to cash flow hedges. Any gain or loss on the effective portion of the hedge is recognised in equity, any gain or loss on the ineffective portion of the hedge is recognised in the Group Income Statement. On

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S2. Summary of significant accounting policies continued

disposal of the foreign operation, the cumulative value of any gains or losses recognised directly in equity is transferred to the Group Income Statement.

Nuclear activity

The Group's investments in Lake Acquisitions Limited ('British Energy') and NNB Holding Company Limited ('Nuclear New Build') are accounted for as associates. The following accounting policies are specific to the accounting for the nuclear activity of these associates.

(a) Fuel costs – nuclear front end

Front end fuel costs consist of the costs of procurement of uranium, conversion and enrichment services and fuel element fabrication. All costs are capitalised into inventory and charged to the Group Income Statement in proportion to the amount of fuel burnt.

(b) Fuel costs – nuclear back end

Advanced Gas-cooled Reactors (AGR)

Spent fuel extracted from the reactors is sent for reprocessing and/or long-term storage and eventual disposal of resulting waste products. Back end fuel costs comprise a loading related cost per tonne of uranium and a rebate/surcharge to this cost dependent on the out-turn market electricity price in the year and are capitalised into inventory and charged to the Group Income Statement in proportion to the amount of fuel burnt.

Pressurised Water Reactor (PWR)

Back end fuel costs are based on wet storage in station ponds followed by dry storage and subsequent direct disposal of fuel. Back end fuel costs are capitalised into inventory on loading and charged to the Group Income Statement in proportion to the amount of fuel burnt.

(c) Nuclear property, plant and equipment and depreciation

The nuclear fleet are depreciated from the date of the Group acquiring its share of British Energy on a straight-line basis, with remaining depreciable periods currently of up to 23 years.

Expenditure on major inspection and overhauls of production plant is depreciated over the period until the next outage which for AGR power stations is three years and for the PWR power station is 18 months.

(d) Nuclear Liabilities Fund (NLF) funding arrangements

Under the arrangements in place with the Secretary of State, the NLF will fund, subject to certain exceptions, British Energy's qualifying uncontracted nuclear liabilities and qualifying decommissioning costs.

In part consideration for the assumption of these liabilities by the Secretary of State and the NLF, British Energy agreed to pay fixed decommissioning contributions each year and £150,000 (indexed to RPI) for every tonne of uranium in PWR fuel loaded into the Sizewell B reactor after the date of these arrangements.

(e) NLF and nuclear liabilities receivables

The Government indemnity is provided to indemnify any future shortfall on NLF funding of qualifying uncontracted nuclear liabilities (including PWR back end fuel services) and qualifying nuclear decommissioning costs such that the receivable equals the present value of the associated qualifying nuclear liabilities.

(f) Nuclear liabilities

Nuclear liabilities represent provision for British Energy's liabilities in respect of the costs of waste management of spent fuel and nuclear decommissioning.

(g) Unburnt fuels at shutdown

Due to the nature of the nuclear fuel process there will be quantities of unburnt fuel in the reactors at station closure. The costs relating to this unburnt fuel (final core) are estimated by applying a long-term inflation index to the projected costs, which are then discounted.

S3. Financial risk management

The Group's normal operating, investing and financing activities expose it to a variety of financial risks: market risk (including commodity price risk, currency risk, interest rate risk and equity price risk), credit risk and liquidity risk. The Group's overall risk management process is designed to identify, manage and mitigate business risk, which includes, among others, financial risk. Further detail on the Group's overall risk management process is included within the Directors' Report – Governance on pages 58 to 60.

Financial risk management is overseen by the GFRMC according to objectives, targets and policies set by the Board. Commodity price risk management is carried out in accordance with individual business unit Financial Risk Management Committees and their respective financial risk management policies, as approved by the GFRMC under delegated authority from the Board. Treasury risk management, including management of currency risk, interest rate risk, equity price risk and liquidity risk is carried out by a central Group Treasury function in accordance with the Group's financing and treasury policy, as approved by the Board.

The wholesale credit risks associated with commodity trading and treasury positions are managed in accordance with the Group's credit risk policy and collateral risk policy. Downstream credit risk management is carried out in accordance with individual business unit credit policies.

Market risk management

Market risk is the risk of loss that results from changes in market prices (commodity prices, foreign exchange rates, interest rates and equity prices). The level of market risk to which the Group is exposed at a point in time varies depending on market conditions, expectations of future price or market rate movements and the composition of the Group's physical asset and contract portfolios.

(a) Commodity price risk management

The Group is exposed to commodity price risk in its upstream assets, energy procurement contracts, downstream and proprietary energy trading activities and uses specific limits to manage the exposure to commodity prices associated with the Group's activities to an acceptable level. Volumetric limits are supported by Profit at Risk (PaR) and Value at Risk (VaR) metrics in the UK and in North America to measure the Group's exposure to commodity price risk. Limits are also set on PaR and VaR measurements as a further control over exposure to market prices.

(i) Energy procurement, upstream and downstream activities

The Group's energy procurement, upstream and downstream activities consist of equity gas and liquids production, equity power generation, bilateral procurement and sales contracts, market-traded purchase and sales contracts and derivative positions taken on with the intent of securing gas and power for the Group's downstream customers in the UK and North America from a variety of sources at an optimal cost. The Group actively manages commodity price risk by optimising its asset and contract portfolios and making use of volume flexibility.

The Group is exposed to commodity price risk in its energy procurement, upstream and downstream activities because the cost of procuring gas and electricity to serve its downstream customers varies with wholesale commodity prices. The risk is primarily that market prices for commodities will fluctuate between the time that sales prices are fixed or tariffs are set and the time at which the corresponding procurement cost is fixed, thereby potentially reducing expected margins or making sales unprofitable.

The Group is also exposed to volumetric risk in the form of an uncertain consumption profile arising from a range of factors, including weather, energy consumption changes, customer attrition and economic climate.

In order to manage the exposure to market prices associated with the Group's energy procurement, upstream and downstream activities the Group uses a specific set of limits (including position, volumetric, VaR/PaR) established by the Executive Committee and governed by GFRMC oversight along with business unit market risk policies.

Volumetric limits are supported by PaR and VaR metrics in the UK and in North America to measure the Group's exposure to commodity price risk. Limits are also set on PaR and VaR measurements as a further control over exposure to market prices. PaR measures the estimated potential loss in a position or portfolio of positions associated with the movement of a commodity price for a given confidence level, over the remaining term of the position or contract portfolio. VaR measures the estimated potential loss for a given confidence level over a predetermined holding period. The standard

SUPPLEMENTARY INFORMATION CONTINUED

S3. Financial risk management continued

confidence level used is 95%. In addition, stress tests are regularly performed to evaluate the impact of substantial movements in commodity prices.

The Group measures and manages the commodity price risk associated with the Group's entire energy procurement, upstream and downstream portfolio. Only certain of the Group's energy procurement, upstream and downstream contracts constitute financial instruments under IAS 39 (note 24).

As a result, while the Group manages the commodity price risk associated with both financial and non-financial energy procurement, upstream and downstream contracts, it is the notional value of energy contracts being carried at fair value that represents the exposure of the Group's energy procurement, upstream and downstream activities to commodity price risk according to IFRS 7, Financial Instruments: Disclosures. This is because energy contracts that are financial instruments under IAS 39 are accounted for on a fair value basis and changes in fair value immediately impact profit or equity. Conversely, energy contracts that are not financial instruments under IAS 39 are accounted for as executory contracts and changes in fair value do not immediately impact profit or equity, and as such, are not exposed to commodity price risk as defined by IFRS 7. So whilst the PaR or VaR associated with energy procurement and downstream contracts outside the scope of IAS 39 is monitored for internal risk management purposes, only those energy contracts within the scope of IAS 39 are within the scope of the IFRS 7 disclosure requirements.

(ii) Proprietary energy trading

The Group's proprietary energy trading activities consist of physical and financial commodity purchases and sales contracts taken on with the intent of benefiting in the short term from changes in market prices or differences between buying and selling prices. The Group conducts its trading activities in the over-the-counter market and through exchanges in the UK, North America and continental Europe. The Group is exposed to commodity price risk as a result of its proprietary energy trading activities because the value of its trading assets and liabilities will fluctuate with changes in market prices for commodities.

The Group sets volumetric and VaR limits to manage the commodity price risk exposure associated with the Group's proprietary energy trading activities. The VaR used measures the estimated potential loss for a 95% confidence level over a one-day holding period. The holding period used is based on market liquidity and the number of days the Group would expect it to take to close out a trading position. The VaR limits set for proprietary trading activities are relatively small compared to the Group's overall operations and are less than £5 million. The carrying value of energy contracts used in proprietary energy trading activities at 31 December 2012 is disclosed in note 19.

As with any modelled risk measure, there are certain limitations that arise from the assumptions used in the VaR analysis. VaR assumes that the future will behave like the past and that the Group's trading positions can be unwound or hedged within the predetermined holding period. Furthermore, the use of a 95% confidence level, by definition, does not take into account changes in value that might occur beyond this confidence level.

(b) Currency risk management

The Group is exposed to currency risk on foreign currency denominated forecast transactions, firm commitments, monetary assets and liabilities (transactional exposure) and on its net investments in foreign operations (translational exposure).

(i) Transactional currency risk

The Group is exposed to transactional currency risk on transactions denominated in currencies other than the underlying functional currency of the commercial operation transacting. The Group's primary functional currencies are pounds sterling in the UK, Canadian dollars in Canada, US dollars in the US, Norwegian kroner in Norway and euros in the Netherlands. The risk is that the functional currency value of cash flows will vary as a result of movements in exchange rates. Transactional exposure arises from the Group's energy procurement activities in the UK and in Canada, where a proportion of transactions are denominated in euros or US dollars and on certain capital commitments denominated in foreign currencies. In addition, in order to optimise the cost of funding, the Group has, in certain cases, issued foreign currency denominated debt, primarily in US dollars, New Zealand dollars, euros or Japanese yen.

(ii) Translational currency risk

The Group is exposed to translational currency risk as a result of its net investments in North America and Europe. The risk is that the pounds sterling value of the net assets of foreign operations will decrease with changes in foreign exchange rates. The Group's policy is to protect the pounds sterling book value of its net investments in foreign operations where possible, subject to certain parameters monitored by the GFRMC, by holding foreign currency debt, entering into foreign currency derivatives, or a mixture of both.

The Group measures and manages the currency risk associated with all transactional and translational exposures. In contrast, IFRS 7 only requires disclosure of currency risk arising on financial instruments denominated in a currency other than the functional currency of the commercial operation transacting. As a result, for the purposes of IFRS 7, currency risk excludes the Group's net investments in North America and Europe as well as foreign currency denominated forecast transactions and firm commitments. A sensitivity analysis that is intended to illustrate the sensitivity of the Group's financial position and performance to changes in the fair value or future cash flows of foreign currency denominated financial instruments as a result of changes in foreign exchange rates is provided in note 25.

(c) Interest rate risk management

In the normal course of business the Group borrows to finance its operations. The Group is exposed to interest rate risk because the fair value of fixed rate borrowings and the cash flows associated with floating rate borrowings will fluctuate with changes in interest rates. The Group's policy is to manage the interest rate risk on long-term borrowings by ensuring the exposure to floating interest rates remains within a 30% to 70% range, including the impact of interest rate derivatives. A sensitivity analysis that is intended to illustrate the sensitivity of the Group's financial position and performance to changes in interest rates is provided in note 25.

(d) Equity price risk management

The Group is exposed to equity price risk because certain available-for-sale financial assets, held by the Law Debenture Trust on behalf of the Company as security in respect of the Centrica Unfunded Pension Scheme defined benefit section, are linked to equity indices (note 29). Investments in equity indices are inherently exposed to less risk than individual equity investments because they represent a naturally diverse portfolio. Note 29 details the Group's other retirement benefit assets and liabilities.

(e) Sensitivity analysis

IFRS 7 requires disclosure of a sensitivity analysis that is intended to illustrate the sensitivity of the Group's financial position and performance to changes in market variables (commodity prices, foreign exchange rates and interest rates) as a result of changes in the fair value or cash flows associated with the Group's financial instruments. The sensitivity analysis provided discloses the effect on profit or loss and equity at 31 December 2012 assuming that a reasonably possible change in the relevant risk variable had occurred at 31 December 2012 and been applied to the risk exposures in existence at that date to show the effects of reasonably possible changes in price on profit or loss and equity to the next annual reporting date. Reasonably possible changes in market variables used in the sensitivity analysis are based on implied volatilities, where available, or historical data for energy prices and foreign exchange rates. Reasonably possible changes in interest rates are based on management judgement and historical experience.

The sensitivity analysis has been prepared based on 31 December 2012 balances and on the basis that the balances, the ratio of fixed to floating rates of debt and derivatives, the proportion of energy contracts that are financial instruments, the proportion of financial instruments in foreign currencies and the hedge designations in place at 31 December 2012 are all constant. Excluded from this analysis are all non-financial assets and liabilities and energy contracts that are not financial instruments under IAS 39. The sensitivity to foreign exchange rates relates only to monetary assets and liabilities denominated in a currency other than the functional currency of the commercial operation transacting, and excludes the translation of the net assets of foreign operations to pounds sterling, but includes the corresponding impact of financial instruments used in net investment hedges.

SUPPLEMENTARY INFORMATION CONTINUED

S3. Financial risk management continued

The sensitivity analysis provided is hypothetical only and should be used with caution as the impacts provided are not necessarily indicative of the actual impacts that would be experienced because the Group's actual exposure to market rates is changing constantly as the Group's portfolio of commodity, debt and foreign currency contracts changes. Changes in fair values or cash flows based on a variation in a market variable cannot be extrapolated because the relationship between the change in market variable and the change in fair value or cash flows may not be linear. In addition, the effect of a change in a particular market variable on fair values or cash flows is calculated without considering interrelationships between the various market rates or mitigating actions that would be taken by the Group. The sensitivity analysis provided in note 25 excludes the impact of proprietary energy trading assets and liabilities because the VaR associated with the Group's proprietary energy trading activities is less than £5 million.

Credit risk management

Credit risk is the risk of loss associated with a counterparty's inability or failure to discharge its obligations under a contract. The Group is exposed to credit risk in its treasury, trading, energy procurement and downstream activities. The Group continues to take steps to tighten downstream credit policies, including the tightening of credit scores in customer management processes, whilst continuing to manage credit risk in accordance with financial risk management processes.

Note 25 provides further detail of the Group's exposure to credit risk on its financial assets.

(a) Treasury, trading and energy procurement activities

Wholesale counterparty credit exposures are monitored by individual counterparty and by category of credit rating, and are subject to approved limits. The majority of significant exposures are with counterparties rated A–/A3 or better. The Group uses master netting agreements to reduce credit risk and net settles payments with counterparties where net settlement provisions exist. In addition, the Group employs a variety of other methods to mitigate credit risk: margining, various forms of bank and parent company guarantees and letters of credit. 100% of the Group's credit risk associated with its treasury, trading and energy procurement activities is with counterparties in related energy industries or with financial institutions.

IFRS 7 requires disclosure of information about the exposure to credit risk arising from financial instruments only. Only certain of the Group's energy procurement contracts constitute financial instruments under IAS 39 (note 24). As a result, whilst the Group manages the credit risk associated with both financial and non-financial energy procurement contracts, it is the carrying value of financial assets within the scope of IAS 39 (note 24) that represents the maximum exposure to credit risk in accordance with IFRS 7.

(b) Downstream activities

In the case of business customers, credit risk is managed by checking a company's creditworthiness and financial strength both before commencing trade and during the business relationship. For residential customers, creditworthiness is ascertained normally before commencing trade to determine the payment mechanism required to reduce credit risk to an acceptable level. Certain customers will only be accepted on a prepayment basis or with a security deposit. In some cases, an ageing of receivables is monitored and used to manage the exposure to credit risk associated with both business and residential customers. In other cases, credit risk is monitored and managed by grouping customers according to method of payment or profile.

Liquidity risk management and going concern

Liquidity risk is the risk that the Group is unable to meet its financial obligations as they fall due. The Group experiences significant movements in its liquidity position due primarily to the seasonal nature of its business and margin cash arrangements associated with certain wholesale commodity contracts. To mitigate this risk the Group maintains significant committed facilities and holds cash on deposit. The Group's liquidity position has remained strong throughout 2012.

S4. Segmental analysis

The measure of profit used by the Centrica Executive Committee is adjusted operating profit. Adjusted operating profit is operating profit before exceptional items and certain re-measurements (note 7), before additional depreciation resulting from any fair value uplifts on Strategic Investments (notes 2 and 11) and including the results from joint ventures and associates which are included before interest and tax. All transactions between segments are on an arm's length basis.

The Group's operating segments are those used internally by management to run the business and make decisions. The Group's operating segments are based on products and services provided in each geographical area. The operating segments are also the Group's reportable segments. The types of products and services from which each reportable segment derives its revenues are:

Segment	Description
British Gas:	
Residential energy supply	The supply of gas and electricity to residential customers in the UK
Residential services	Installation, repair and maintenance of domestic central heating, plumbing and drains, gas appliances and kitchen appliances, including the provision of fixed-fee maintenance/breakdown service and insurance contracts in the UK
Business energy supply and services	The supply of gas and electricity and provision of energy-related services to business customers in the UK
Centrica Energy:	
Gas	Production, processing, trading and optimisation of gas and oil and the development of new fields to grow reserves
Power	Generation, trading and optimisation of power from thermal, nuclear and wind sources
Centrica Storage	Gas storage in the UK
Direct Energy:	
Residential energy supply	The supply of gas and electricity to residential customers in North America
Business energy supply	The supply of gas, electricity and energy management solutions to commercial and industrial customers in North America
Residential and business services	Installation and maintenance of Heating, Ventilation and Air Conditioning (HVAC) equipment, water heaters and the provision of breakdown services in North America
Upstream and wholesale energy	Gas and oil production, power generation and procurement and trading activities in the North American wholesale energy markets

S5. Other equity

Merger reserve

During February 1997, BG plc (formerly British Gas plc) demerged certain businesses (grouped together under GB Gas Holdings Limited (GBGH)) to form Centrica plc. Upon demerger, the share capital of GBGH was transferred to Centrica plc and was recorded at the nominal value of shares issued to BG plc shareholders. In accordance with the Companies Act 1985, no premium was recorded on the shares issued. On consolidation, the difference between the nominal value of the Company's shares issued and the amount of share capital and share premium of GBGH at the date of demerger was credited to a merger reserve.

Capital redemption reserve

In accordance with the Companies Act 1985, the Company transferred to the capital redemption reserve an amount equal to the nominal value of shares repurchased and subsequently cancelled (£16 million).

Revaluation reserve

During 2005, the revaluation of the Group's existing interest in Centrica SHB Limited to fair value, following the acquisition by the Group of the remaining 40% stake in the company, was recorded as a revaluation reserve adjustment. The remainder of the revaluation reserve relates to a 2009 revaluation of

SUPPLEMENTARY INFORMATION CONTINUED

S5. Other equity continued

producing gas and oil assets located in Alberta, Canada, following the acquisition by the Group of additional interests.

Own shares reserve

The own shares reserve reflects the cost of shares in the Company held in the Centrica employee share ownership trusts to meet the future requirements of the Group's share based payment plans.

Share-based payments reserve

The share-based payments reserve reflects the obligation to deliver shares to employees under the Group's share schemes in return for services provided.

S6. Pensions

Pension schemes

The Registered Pensions Schemes are subject to independent valuations at least every three years, on the basis of which the qualified actuary certifies the rate of employer contributions which, together with the specified contributions payable by the employees and proceeds from the schemes' assets, are expected to be sufficient to fund the benefits payable under the schemes.

The latest full actuarial valuations were carried out at the following dates: the Registered Pensions Schemes at 31 March 2012, the Centrica Unfunded Pension Scheme at 6 April 2012 and the Direct Energy Marketing Limited Pension Plan at 31 December 2011. These have been updated to 31 December 2012 for the purposes of meeting the requirements of IAS 19. Investments have been valued for this purpose at market value.

Governance

The Registered Pension Schemes are managed by trustee companies whose boards consist of both company-nominated and member-nominated directors. Each scheme holds units in the Centrica Combined Common Investment Fund (CCCIF), which holds the combined assets of the participating schemes. The method of allocation of units is set out in the Trust Deed of the CCCIF. The board of CCCIF Limited is comprised of nine directors; three independent directors, three directors appointed by Centrica plc (including the chairman) and one director appointed by each of the three participating schemes. Apart from the investment in the Scottish Limited Partnership described in note 29, no direct investments are made in securities issued by Centrica plc or any of its subsidiaries, property leased to or owned by Centrica plc or any of its subsidiaries, or securities of any fund manager or any of their associated companies.

Under the terms of the Pensions Act 2004, Centrica plc and each trustee board must agree the funding rate for its defined benefit pension scheme and a recovery plan to fund any deficit against the scheme-specific statutory funding objective. This approach was first adopted for the triennial valuations completed at 31 March 2006 and was again reflected in the 31 March 2012 valuations.

S7. Share schemes

The majority of the share-based payment charge arises from three schemes. More information is found in the Remuneration Report on pages 61 to 75.

Deferred Matching Share Scheme (DMSS):

- Applicable employees: Senior Executive Group.
- Vesting period of four years, comprising bonus year and three-year performance period.
- Participants must defer between 20% and 40% of annual pre-tax bonus into scheme and can elect to invest additional amounts of annual bonus up to a maximum of 50% of total potential bonus.
- Deferred and investment shares will be matched with conditional shares, released upon achievement of performance target over three-year period.
- Performance measured through Group and segment EP targets.
- Shares are held in trust over the three-year period and cannot be withdrawn.
- Leaving prior to vesting date will normally mean forfeiting right to shares, except for investment shares which will be returned.

Long Term Incentive Scheme (LTIS):

- Applicable employees: Senior management.
- Vesting period of three years following grant date.
- Grants after 2012 - number of shares calculated according to EPS, Group EP, TSR and non-financial KPI's.
- Grants before 2012 - number of shares calculated according to EPS growth and TSR.
- Shares released immediately following the end of the assessed performance period subject to continued employment at that date.

Share Award Scheme (SAS):

- Applicable employees: Middle management.
- Shares vest subject to continued employment within the Group in two stages – half vests after two years, the other half after three years.

S8. Fixed-fee service and insurance contracts

Fixed-fee service contracts are entered into with home services customers in the UK and home and business services customers in North America. These contracts continue until cancelled by either party.

Insurance contracts are entered into with home service customers in the UK by British Gas Insurance Limited (BGIL), a fully owned subsidiary of Centrica plc, an entity regulated by the Financial Services Authority (FSA). Product offerings include central heating, boiler and controls, plumbing and drains and electrical appliance insurance cover. These contracts are normally for periods of 12 months with the option of renewal.

The contracts protect holders against the risk of breakdown, resulting in the transfer of an element of risk to BGIL. Benefits provided to customers vary in accordance with terms and conditions of the contracts entered into, however, generally include repair and/or replacement of the items affected.

The risk and level of service required within these contracts is dependent upon the occurrence of uncertain future events, in particular the number of call-outs, the cost per call-out and the nature of the fault. Accordingly, the timing and amount of future cash outflows related to the contracts is uncertain. The key terms and conditions that affect future cash flows are as follows:

- provision of labour and parts for repairs, dependent on the agreement and associated level of service;
- one safety and maintenance inspection either annually or in every continuous two-year period, as set out in the agreement;
- no limit to the number of call-outs to carry out repair work; and
- caps on certain maintenance and repair costs.

Revenue from these contracts is recognised with regard to the incidence of risk over the life of the contract, reflecting the seasonal propensity of claims to be made under the contracts and the benefits receivable by the customer, which span the life of the contract as a result of emergency maintenance being available throughout the contract term. Cost of sales relates directly to the engineer workforce employed by Centrica within home services, the cost of which is accounted for over a 12-month period with adjustments made to reflect the seasonality of workload over a given year. The costs of claims under the contracts will be the costs of the engineer workforce employed by Centrica within home services. These costs are accounted for over a 12-month period with adjustments made to reflect the seasonality of workload over a given year.

Weather conditions and the seasonality of maintenance can affect the number of call-outs, the cost per call-out and the nature of the fault. BGIL's obligations under the terms of the contracts are based on the number of breakdowns occurring within the contract period. BGIL actively manages the risk exposure of these uncertain events by undertaking the following risk mitigation activities:

- an initial service visit is performed for central heating care and insurance cover. If, at the initial visit, faults that cannot be rectified are identified, the contract will be cancelled and no further cover provided;
- an annual or biennial safety and maintenance inspection is performed to ensure all issues are identified prior to them developing into significant maintenance or breakdown issues; and
- caps on certain maintenance and repair work are incorporated into the contracts to limit liability in areas considered to be higher risk in terms of prevalence and cost to repair.

Financial Statements

SUPPLEMENTARY INFORMATION CONTINUED

S9. Principal undertakings

All principal undertakings (including joint ventures and associates) listed below are held indirectly by Centrica plc. The principal undertakings shown here is a list of those companies which in the Directors' opinion principally affect the figures shown in the Group Financial Statements. A full list of related undertakings is included in Centrica plc's Annual Return submitted to the Registrar of Companies.

31 December 2012	Country of incorporation/formation	Principal activity
Subsidiary undertakings (i)		
British Gas Trading Limited	England	Energy supply
British Gas New Heating Limited	England	Electrical and gas installations
British Gas Services Limited	England	Home services
British Gas Insurance Limited	England	Insurance provision
Centrica Norway Limited, Centrica Resources Limited, Hydrocarbon Resources Limited	England	Gas and/or oil exploration and production
Centrica Production Nederland B.V.	Netherlands	Gas and/or oil exploration and production
Centrica North Sea Gas Limited, Centrica North Sea Oil Limited	Scotland	Gas and/or oil exploration and production
Centrica Langage Limited, Humberland Limited	England	Power generation
Centrica LNG Company Limited	England	LNG trading
Centrica Energy Limited, Centrica Energy (Trading) Limited	England	Wholesale energy trading
Centrica Storage Limited	England	Gas storage
GB Gas Holdings Limited	England	Holding company
Direct Energy Partnership	Canada	Energy supply
CPL Retail Energy LP, Direct Energy Business LLC, Direct Energy LP, Direct Energy Source LLC (ii), Energetix Inc (iii), Energy America LLC, FCP Enterprises Inc, Gateway Energy Services Corporation, NYSEG Solutions Inc (iii), WTU Retail Energy LP	USA	Energy supply
Direct Energy Marketing Limited	Canada	Energy supply and home services
Direct Energy Services LLC	USA	Energy supply and home services
Airtron Inc, Clockwork Inc, Direct Energy US Home Services Inc	USA	Home and/or commercial services
Home Warranty Holding Corporation (iii)	USA	Insurance provision
Direct Energy Resources Partnership	Canada	Gas production
Bastrop Energy Partners LP, Frontera Generation LP, Paris Generation LP	USA	Power generation
Direct Energy Marketing Inc	USA	Wholesale energy trading
Brae Canada Ltd (iv)	Canada	Holding company

31 December 2012	Country of incorporation/formation	Percentage holding in ordinary shares and net assets	Principal activity
Joint ventures and associates (v)			
Celtic Array Limited ('Round 3')	England	50	Wind farm development
GLID Wind Farms TopCo Limited	England	50	Power generation
Lake Acquisitions Limited ('British Energy'), NNB Holding Company Limited ('Nuclear New Build')	England	20	Holding company
Lincs Wind Farm Limited	Scotland	50	Power generation

(i) Centrica holds 100% of the ordinary shares and net assets of all subsidiary undertakings in this list.
(ii) Previously called Vectren Retail LLC.
(iii) Acquired in 2012.
(iv) Brae Canada Ltd has a branch registered in England.
(v) Further information on the principal joint ventures and associate investments held by the Group are disclosed in Note 16.

The companies incorporated in England and Scotland principally operate in the UK. The companies incorporated in the USA, Canada and the Netherlands principally operate within North America and the Netherlands respectively.

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF CENTRICA PLC

We have audited the parent Company Financial Statements of Centrica plc for the year ended 31 December 2012 which comprise the Company Balance Sheet and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice).

Respective responsibilities of Directors and auditors

As explained more fully in the Directors' Responsibility Statement set out on page 60 the Directors are responsible for the preparation of the parent Company Financial Statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the parent Company Financial Statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the Company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

Scope of the audit of the Financial Statements

An audit involves obtaining evidence about the amounts and disclosures in the Financial Statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the parent Company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Directors; and the overall presentation of the Financial Statements. In addition, we read all the financial and non-financial information in the Annual Report and Accounts to identify material inconsistencies with the audited Financial Statements. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Opinion on Financial Statements

In our opinion the parent Company Financial Statements:

- give a true and fair view of the state of the Company's affairs as at 31 December 2012;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Opinion on other matters prescribed by the Companies Act 2006

In our opinion:

- the part of the Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006; and
- the information given in the Directors' Report for the financial year for which the parent Company Financial Statements are prepared is consistent with the parent Company Financial Statements.

Matter on which we are required to report by exception

We have nothing to report in respect of the following:

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- adequate accounting records have not been kept by the parent Company, or returns adequate for our audit have not been received from branches not visited by us; or
- the parent Company Financial Statements and the part of the Directors' Remuneration Report to be audited are not in agreement with the accounting records and returns; or
- certain disclosures of Directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

Other matter

We have reported separately on the Group Financial Statements of Centrica plc for the year ended 31 December 2012.

Charles Bowman

Charles Bowman
Senior Statutory Auditor
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
London
27 February 2013

Financial Statements

COMPANY BALANCE SHEET

31 December	Notes	2012 £m	2011 (restated) (i) £m
Fixed assets			
Tangible assets	III	**96**	64
Investments	IV	**2,434**	2,154
		2,530	2,218
Current assets			
Debtors	V	**11,897**	10,522
Current asset investments	VI	**192**	181
Cash at bank and in hand		**479**	164
		12,568	10,867
Creditors (amounts falling due within one year)			
Borrowings	VII	**(468)**	(454)
Other creditors	VIII	**(6,605)**	(5,695)
		(7,073)	(6,149)
Net current assets		**5,495**	4,718
Total assets less current liabilities		**8,025**	6,936
Creditors (amounts falling due after more than one year)			
Borrowings	VII	**(4,589)**	(3,361)
Other creditors	VIII	**(66)**	(92)
Provisions for liabilities	IX	**(16)**	(16)
		(4,671)	(3,469)
Net assets excluding pension assets/(liabilities)		**3,354**	3,467
Defined benefit pension assets	X	**9**	21
Defined benefit pension liabilities	X	**(37)**	(34)
Net assets		**3,326**	3,454
Capital and reserves – equity interests			
Share capital	XI	**321**	319
Share premium	XI	**929**	874
Capital redemption reserve	XI	**16**	16
Profit and loss account	XI	**2,060**	2,245
Shareholders' funds	XI	**3,326**	3,454

(i) See note I and note X.

The Financial Statements on pages 136 to 142 were approved and authorised for issue by the Board of Directors on 27 February 2013 and were signed on its behalf by:

Sam Laidlaw Nick Luff

Sam Laidlaw
Chief Executive

Nick Luff
Group Finance Director

The notes on pages 137 to 142 form part of these Financial Statements, along with note 26 to the Group Financial Statements.

NOTES TO THE COMPANY FINANCIAL STATEMENTS

I. Principal accounting policies of the Company

Basis of preparation

The Company Financial Statements have been prepared under the historical cost convention as modified for the treatment of financial instruments in accordance with applicable UK Accounting Standards consistently applied and under the Companies Act 2006. The accounts have been prepared under the going concern basis. No profit and loss account is presented for the Company as permitted by the Companies Act 2006 (section 408). The Company profit after tax for the year was £625 million (2011 restated: £918 million).

Presentation of derivative financial instruments

In line with the Group's accounting policy for derivative financial instruments, the Company has classified those derivatives held for the purpose of treasury management as current or non-current, based on expected settlement dates.

Employee share schemes

The Group has a number of employee share schemes under which it makes equity-settled share-based payments as detailed in the Remuneration Report on pages 61 to 75 and in note S7. Equity-settled share-based payments are measured at fair value at the date of grant (excluding the effect of non-market-based vesting conditions). The fair value determined at the grant date is expensed on a straight-line basis together with a corresponding increase in equity over the vesting period, based on the Group's estimate of the number of awards that will vest and adjusted for the effect of non-market-based vesting conditions. The issue of share incentives by the Company to employees of its subsidiaries represents additional capital contributions. The addition to the Company's investment in subsidiary undertakings is reduced on the issue of share incentives as these are recharged to the subsidiaries.

Fair value is measured using methods appropriate to each of the different schemes as follows:

LTIS – EPS, EP and KPI awards	Market value on the date of grant
LTIS – TSR awards	A Monte Carlo simulation to predict the total shareholder return performance
SAS and DMSS	Market value on the date of grant

Foreign currencies

The Company's functional and presentational currency is pounds sterling. Transactions in foreign currencies are translated at the rate of exchange ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated into pounds sterling at closing rates of exchange. Exchange differences on monetary assets and liabilities and transactions are taken to the Profit and Loss Account, unless hedge accounting is applied whereby the differences are taken to reserves until the hedged item is realised.

Tangible fixed assets

Tangible fixed assets are held at cost, less accumulated depreciation and any provisions for impairment. Cost includes the original purchase price of the asset and the cost attributable to bringing it to its working condition for its intended use. Tangible fixed assets are depreciated on a straight-line basis at rates sufficient to write off the cost, less estimated residual values, of individual assets over their estimated useful lives of up to ten years.

Leases

Rentals under operating leases are charged to the Profit and Loss Account on a straight-line basis over the lease term.

Investments

Fixed asset investments in subsidiaries' shares are held at cost, less any provision for impairment as necessary. Fixed asset investments in the form of loans are held at amortised cost using the effective interest rate method, less any provision for impairment as necessary. Current asset investments are stated at the lower of cost and net realisable value.

Pensions and other post-employment benefits

The Company's employees participate in a number of the Group's defined benefit pension schemes. The total Group cost of providing benefits under defined benefit schemes is determined separately for each of the Group's schemes under the projected unit credit actuarial valuation method. Actuarial gains and losses are recognised in full in the period in which they occur. The key assumptions used for the actuarial valuation are based on the Group's best estimate of the variables that will determine the ultimate cost of providing post-employment benefits, on which further detail is provided in notes 29 and S6 to the Group Financial Statements.

The Company's share of the total Group surplus or deficit at the end of the reporting period for each scheme is calculated in proportion to the Company's share of ordinary employer contributions in to that scheme during the year; ordinary employer contributions are determined by the pensionable pay of the Company's employees within the scheme and the cash contribution rates set by the scheme trustees. Current service cost is calculated with reference to the pensionable pay of the Company's employees. The Company's share of the total Group interest on scheme liabilities, expected return on scheme assets and actuarial gains or losses is calculated in proportion to ordinary employer contributions in the prior accounting period. Changes in the surplus or deficit arising as a result of the changes in the Company's share of total ordinary employer contributions are also treated as actuarial gains or losses.

This is a change in accounting policy from prior years when the Company accounted for the schemes as if they were defined contribution schemes and the charge to the Profit and Loss Account was equal to the contributions payable to the schemes in the accounting period. The accounting policy has been amended because the Group has now identified a methodology for allocating the Company's share of the underlying assets and liabilities in the schemes on a consistent and reasonable basis.

Comparative figures have been restated accordingly. The change in accounting policy increased profit after tax for the year by £6 million (2011: £19 million increase) and reduced opening reserves by £13 million (2011: £41 million).

Taxation

Current tax, including UK corporation tax, is provided at amounts expected to be paid (or recovered) using the tax rates and laws that have been enacted or substantively enacted by the balance sheet date.

Deferred tax is recognised in respect of all timing differences that have originated, but not reversed, at the balance sheet date where transactions or events that result in an obligation to pay more tax in the future, or a right to pay less tax in the future, have occurred at the balance sheet date. Timing differences are differences between the Group's taxable profits and its results as stated in the Financial Statements that arise from the inclusion of gains and losses in tax assessments in periods different from those in which they are recognised in the Financial Statements.

A deferred tax asset is regarded as recoverable and therefore recognised only when, on the basis of all available evidence, it can be

Financial Statements

NOTES TO THE COMPANY FINANCIAL STATEMENTS CONTINUED

I. Principal accounting policies of the Company continued

regarded as more likely than not that there will be suitable taxable profits in the foreseeable future from which the reversal of the underlying timing differences can be deducted.

Deferred tax is measured at the average tax rates that are expected to apply in the periods in which the timing differences are expected to reverse, based on tax rates and laws that have been enacted or substantively enacted by the balance sheet date. Deferred tax is measured on an undiscounted basis.

Financial instruments and borrowings

The Company's accounting policies for financial instruments and borrowings are consistent with those of the Group, and are disclosed in note S2. The Company's financial risk management policies are consistent with those of the Group and are described in the Directors' Report – Governance on pages 58 to 60 and in note S3 to the Group Financial Statements. The Company is exempted by FRS 29 from providing detailed disclosures in respect of its financial instruments because the Company is included within the Group's consolidated Financial Statements and its financial instruments are incorporated into the disclosures in the notes to the Group Financial Statements prepared under IFRS 7 Financial Instruments disclosures.

Provisions

A provision is recognised when the Company has a legal or constructive obligation as a result of a past event and it is probable that an outflow of economic benefit will be required to settle the obligation.

II. Directors and employees

Details of Directors' remuneration, share-based payments and pension entitlements in the Remuneration Report on pages 61 to 75 form part of these Financial Statements. Information on the main employee share-based payments is given in note S7. Details of the remuneration of key management personnel are given in note 34 to the Group Financial Statements.

III. Tangible assets

	2012 Plant, equipment and vehicles £m	2011 Plant, equipment and vehicles £m
Cost		
1 January	**152**	111
Additions	**56**	44
Disposals	**(13)**	(3)
31 December	**195**	152
Accumulated Depreciation		
1 January	**88**	73
Charge for the year	**13**	17
Disposals	**(2)**	(2)
31 December	**99**	88
NBV at 31 December	**96**	64

IV. Investments

	2012			2011		
	Loans (i) £m	Investments in subsidiaries' shares (ii) £m	**Total £m**	Loans £m	Investments in subsidiaries' shares £m	Total £m
Cost						
1 January	–	2,154	**2,154**	–	2,132	2,132
Advances/additions	247	33	**280**	–	22	22
31 December	**247**	**2,187**	**2,434**	–	2,154	2,154

(i) The loan is to Lincs Wind Farm Limited, joint venture of the Centrica plc Group.
(ii) Additions include the net change in shares to be issued under employee share schemes in Group undertakings. Direct investments are held in Centrica Holdings Limited, Centrica Trading Limited and Centrica Beta Holdings Limited, all of which are incorporated in England. Principal undertakings are listed in note S9. The Directors believe that the carrying value of the investments is supported by their underlying net assets.

NOTES TO THE COMPANY FINANCIAL STATEMENTS CONTINUED

V. Debtors

31 December	Due within one year £m	Due after more than one year £m	2012 Total £m	Due within one year £m	Due after more than one year £m	2011 Total £m
Amounts owed by Group undertakings (i)	11,667	8	**11,675**	10,304	8	10,312
Derivative financial instruments (ii)	21	173	**194**	8	175	183
Other debtors	6	–	**6**	3	–	3
Prepayments and other accrued income	14	8	**22**	13	11	24
	11,708	**189**	**11,897**	10,328	194	10,522

(i) The amounts receivable by the Company includes £3,292 million (2011: £3,819 million) that bears interest at a quarterly rate determined by Group Treasury and linked to the Group cost of funds. The quarterly rates ranged between 3.28 and 3.51% per annum during 2012 (2011: 1.71 and 2.71%). The other amounts receivable from Group undertakings are interest-free. All amounts receivable from Group undertakings are unsecured and repayable on demand.
(ii) Derivative financial instruments comprise foreign currency derivatives held for trading of £8 million (2011: £3 million), interest rate derivatives held for hedging of £173 million (2011: £158 million) and foreign currency derivatives held for hedging of £13 million (2011: £22 million). The fair value of these derivatives is equivalent to the carrying value.

VI. Current asset investments

31 December	2012 £m	2011 £m
Short-term investments	**192**	181

£61 million (2011: £54 million) of investments were held by the Law Debenture Trust, on behalf of the Company, as security in respect of the Centrica Unfunded Pension Scheme defined benefit section (refer to note X).

VII. Borrowings

Amounts falling due

31 December	2012 Within one year £m	2012 After one year £m	2011 Within one year £m	2011 After one year £m
Bank loans and overdrafts	**59**	**338**	49	192
Commercial paper	**82**	**–**	114	–
Bonds	**327**	**4,251**	291	3,169
	468	**4,589**	454	3,361

The Company's financial instruments and related disclosures are included within the consolidated Group Financial Statements. As permitted by FRS 29, Financial Instruments: Disclosures, further detailed disclosure in respect of the Company's financial instruments is not included. Disclosures in respect of the Group's borrowings are provided in note 12 to the Group Financial Statements.

VIII. Other creditors

31 December	2012 Due within one year £m	2012 Due after more than one year £m	2011 Due within one year £m	2011 Due after more than one year £m
Trade creditors	**37**	**–**	44	–
Amounts owed to Group undertakings (i)	**6,454**	**–**	5,582	–
Derivative financial instruments (ii)	**63**	**60**	5	92
Taxation and social security	**2**	**–**	4	–
Accruals and deferred income	**49**	**6**	60	–
	6,605	**66**	5,695	92

(i) The amounts payable by the Company bear interest at a quarterly rate determined by Group Treasury and linked to the Group cost of funds. The quarterly rates ranged between 3.28 and 3.51% per annum during 2012 (2011: 1.71 and 2.71%).
(ii) Derivative financial instruments comprise foreign currency derivatives held for trading of £10 million (2011: £5 million), interest rate derivatives held for trading of £85 million (2011: £80 million), interest rate derivatives held for hedging of £2 million (2011: £6 million) and foreign currency derivatives held for hedging of £26 million (2011: £6 million). The fair value of these derivatives is equivalent to the carrying value.

IX. Provisions for liabilities

	1 January 2012 £m	Profit and loss charge £m	Utilised in the year £m	Reserves movement £m	Transfers £m	31 December 2012 £m
Other provisions	16	3	(2)	–	(1)	**16**
Deferred tax	–	6	–	(6)	–	**–**
	16	9	(2)	(6)	(1)	**16**

NOTES TO THE COMPANY FINANCIAL STATEMENTS CONTINUED

IX. Provisions for liabilities continued

Potential unrecognised deferred corporation tax assets amounted to £8 million (2011: £14 million), primarily relating to other timing differences. Other provisions principally represent estimated liabilities for contractual settlements, business restructuring and National Insurance in respect of employee share scheme liabilities. The National Insurance provision was based on a share price of 333.60 pence at 31 December 2012 (2011: 289.30 pence). The majority of the amounts are expected to be utilised by 2015.

X. Pensions

The accounting policy in respect of defined benefit pension schemes has been changed in the year (see note I). Comparatives have been restated accordingly.

(a) Summary of main schemes

The Company's employees participate in the following Group defined benefit pension schemes: Centrica Pension Plan (CPP), Centrica Pension Scheme (CPS), Centrica Engineers Pension Scheme (CEPS) and Centrica Unfunded Pension Scheme. Its employees also participate in the defined contribution section of the Centrica Pension Scheme. Information on these schemes is provided in notes 29 and S6 to the Group Financial Statements.

The CPP, CPS and CEPS form the majority of the Group's and Company's defined benefit obligation and are referred to below and in the Group Financial Statements as the 'Registered Pension Schemes'.

(b) Curtailment gains

During 2011, the Group announced changes to the terms of the final salary sections of the CEPS and the CPP. Further details are provided in note 29 to the Group Financial Statements. The total Group gains of £333 million have been apportioned to the Company in proportion to ordinary employer contributions in the prior accounting period. This results in a gain of £14 million in the Company's restated Profit and Loss Account.

(c) Accounting assumptions

The accounting assumptions for the Registered Pension Schemes are provided in note 29 to the Group Financial Statements.

(d) Movements in the year

	2012		2011	
	Pension liabilities £m	**Pension assets £m**	Pension liabilities (restated) £m	Pension assets (restated) £m
1 January	**(283)**	**270**	(288)	247
Items included in the Profit and Loss Account:				
Current service cost	**(3)**	**–**	(6)	–
Exceptional gain on curtailment	**–**	**–**	14	–
Interest on scheme liabilities	**(15)**	**–**	(17)	–
Expected return on scheme assets	**–**	**16**	–	16
Other movements:				
Actuarial gain/(loss)	**30**	**(56)**	7	5
Employer contributions	**–**	**14**	–	9
Plan participants' contributions	**(1)**	**1**	(1)	1
Benefits paid from schemes	**11**	**(11)**	8	(8)
Transfers from provisions for liabilities	**(1)**	**–**	–	–
31 December	**(262)**	**234**	(283)	270

The net pension liability is presented in the Balance Sheet as:

31 December	2012 £m	2011 (restated) £m
Defined benefit pension assets	**9**	21
Defined benefit pension liabilities	**(37)**	(34)
Net liability recognised in the Company Balance Sheet	**(28)**	(13)

NOTES TO THE COMPANY FINANCIAL STATEMENTS CONTINUED

X. Pensions continued

Included within the pension scheme liabilities are £37 million (2011: £34 million) relating to the Centrica Unfunded Pension Scheme defined benefit section.

(e) Analysis of the actuarial (losses)/gains recognised in reserves (note XI)

Year ended 31 December	2012 £m	2011 (restated) £m
Actuarial (loss)/gain (actual return less expected return on pension scheme assets)	**(56)**	5
Experience gains arising on the scheme liabilities	**3**	2
Changes in assumptions underlying the present value of the scheme liabilities	**27**	5
Actuarial (loss)/gain recognised in Statement of Total Recognised Gains and Losses, before adjustment for taxation	**(26)**	12
Cumulative actuarial gains recognised in reserves at 1 January, before adjustment for taxation	**12**	–
Cumulative actuarial (losses)/gains recognised in reserves at 31 December, before adjustment for taxation	**(14)**	12

(f) Pension scheme contributions

Note 29 to the Group Financial Statements provides details of the triennial review carried out at 31 March 2012 in respect of the UK Registered Pension Schemes and the asset-backed contribution arrangement set up on 31 December 2012. During the year the Group made a £37 million deficit payment and a contribution of £84 million via the asset-backed contribution arrangement of which the Company's share was £2 million and £8 million respectively. Under FRS 17, Retirement Benefits, the Company's contribution and trustee interest in the Scottish Limited Partnership are recognised as scheme assets.

The Company estimates that it will pay £4 million of employer contributions during 2013 at an average rate of 24% of pensionable pay.

(g) Pension scheme assets

31 December	2012 £m	2011 (restated) £m
UK equities	**322**	400
Non-UK equities	**1,522**	1,311
Fixed-interest bonds	**1,411**	1,369
Inflation-linked assets	**997**	1,040
High-yield debt	**324**	292
Diversified asset funds	**246**	–
Property	**204**	163
Cash pending investment	**12**	36
Asset backed contribution assets	**84**	–
Group pension scheme assets (i)	**5,122**	4,611

	2012	2011 (restated)
Company share of the above (£m)	**234**	270
Expected long-term rate of return on assets per annum	**5.6%**	6.0%

(i) Total pension scheme assets for the UK pension schemes.

The basis for determining the overall expected rate of return on assets is explained in note 29 to the Group Financial Statements.

(h) Histories

History of surplus/(deficit)	2012 £m	2011 (restated) £m
Plan assets	**234**	270
Defined benefit obligations	**(262)**	(283)
Pension deficit	**(28)**	(13)
Difference between expected and actual return on scheme assets	**(56)**	5
Experience gains on scheme liabilities	**3**	2

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NOTES TO THE COMPANY FINANCIAL STATEMENTS CONTINUED

XI. Shareholders' funds and reserves

	Profit and loss account								2012	2011
	Cash flow hedging reserve £m	Own shares £m	Share-based payments reserve £m	Retained earnings £m	**Profit and loss account £m**	Share capital £m	Share premium £m	Capital redemption reserve £m	**Total £m**	(restated) (i) Total £m
1 January as previously reported	(26)	(19)	90	2,213	**2,258**	319	874	16	**3,467**	3,310
Prior year adjustment	–	–	–	(13)	**(13)**	–	–	–	**(13)**	(41)
1 January (i)	(26)	(19)	90	2,200	**2,245**	319	874	16	**3,454**	3,269
Profit for the year (ii)	–	–	–	625	**625**	–	–	–	**625**	918
Gains/(losses) on revaluation of cash flow hedges (net of taxation)	10	–	–	–	**10**	–	–	–	**10**	(27)
Dividends	–	–	–	(816)	**(816)**	–	–	–	**(816)**	(762)
Employee share schemes:										
Increase in own shares	–	(21)	–	–	**(21)**	–	–	–	**(21)**	(19)
Value of services provided	–	–	43	–	**43**	–	–	–	**43**	40
Exercise of awards	–	21	(45)	12	**(12)**	–	–	–	**(12)**	(15)
Gains on revaluation of available-for-sale securities (net of taxation)	–	–	–	6	**6**	–	–	–	**6**	(1)
Actuarial (losses)/gains net of taxation	–	–	–	(20)	**(20)**	–	–	–	**(20)**	9
Share issue	–	–	–	–	**–**	2	55	–	**57**	42
Net movement for the financial year	**10**	**–**	**(2)**	**(193)**	**(185)**	**2**	**55**	**–**	**(128)**	185
31 December	**(16)**	**(19)**	**88**	**2,007**	**2,060**	**321**	**929**	**16**	**3,326**	3,454

(i) Restated for the change in accounting policy in respect of defined benefit pensions which reduced opening reserves as at 1 January 2011 by £41 million, increased profit after tax for the year ended 31 December 2011 by £19 million and increased actuarial gains net of taxation for the year ended 31 December 2011 by £9 million.
(ii) As permitted by section 408(3) of the Companies Act 2006, no profit and loss account is presented.

The Directors propose a final dividend of 11.78 pence per share (totalling £602 million) for the year ended 31 December 2012. Details of the dividends are given in note 10 to the Group Financial Statements.

Details of the Company's share capital are provided in the Group Statement of Changes in Equity and note 26 to the Group Financial Statements.

XII. Commitments

At 31 December 2012, the Company had commitments of £148 million (2011: £171 million) relating to contracts with outsource service providers. At 31 December 2012, lease commitments over land and buildings included non-cancellable operating lease payments due under one year of nil (2011: £1 million), within one to five years of £2 million (2011: £1 million) and guaranteed operating commitments of a subsidiary undertaking of £7 million (2011: £7 million).

XIII. Related parties

The Company has taken advantage of the exemption in FRS 8 not to disclose transactions with its wholly owned subsidiaries. During the year the Company received interest and fees on its loan to Lincs Wind Farm Limited of £7 million (2011: nil). The loan balance outstanding is analysed in note IV.

GAS AND LIQUIDS RESERVES (UNAUDITED)

The Group's estimates of reserves of gas and liquids are reviewed as part of the half year and full year reporting process and updated accordingly. A number of factors affect the volumes of gas and liquids reserves, including the available reservoir data, commodity prices and future costs. Due to the inherent uncertainties and the limited nature of reservoir data, estimates of reserves are subject to change as additional information becomes available.

The Group discloses 2P gas and liquids reserves, representing the central estimate of future hydrocarbon recovery. Reserves for Centrica-operated fields are estimated by in-house technical teams composed of geoscientists and reservoir engineers. Reserves for non-operated fields are estimated by the operator, but are subject to internal review and challenge.

As part of the internal control process related to reserves estimation, an assessment of the reserves, including the application of the reserves definitions is undertaken by an independent technical auditor. An annual reserves assessment has been carried out by DeGoyler and MacNaughton for the Group's global reserves. Reserves are estimated in accordance with a formal policy and procedure standard.

The Group has estimated 2P gas and liquids reserves in Europe, North America and Trinidad and Tobago.

The principal fields in Centrica Energy are the Kvitebjorn, South Morecambe, Cygnus, Statfjord, Valemon, Chiswick, NCMA Poinsettia, York, Maria, Rhyl and Grove fields. The principal field in Centrica Storage is the Rough field. The European and Trinidad and Tobago reserves estimates are consistent with the guidelines and definitions of the Society of Petroleum Engineers, the Society of Petroleum Evaluation Engineers and the World Petroleum Council's Petroleum Resources Management System using accepted principles.

The principal fields in Direct Energy are the Foothills, Medicine Hat, Carrot Creek and Central Alberta fields located in the province of Alberta, Canada. The Direct Energy reserves estimates have been evaluated in accordance with the Canadian Oil and Gas Evaluation Handbook (COGEH) reserves definitions and are consistent with the guidelines and definitions of the Society of Petroleum Engineers and the World Petroleum Council.

Estimated net 2P reserves of gas (billion cubic feet)	Europe	Trinidad and Tobago (iii)	**Centrica Energy**	Centrica Storage	Direct Energy	**Total**
1 January 2012	1,858	161	**2,019**	182	603	**2,804**
Revisions of previous estimates	(73)	(2)	**(75)**	–	(10)	**(85)**
Purchases/(disposals) of reserves in place (i)	632	–	**632**	–	37	**669**
Extensions, discoveries and other additions (ii)	39	–	**39**	–	5	**44**
Production (iv)	(220)	(19)	**(239)**	–	(54)	**(293)**
31 December 2012	**2,236**	**140**	**2,376**	**182**	**581**	**3,139**

Estimated net 2P reserves of liquids (million barrels)	Europe	Trinidad and Tobago (iii)	**Centrica Energy**	Centrica Storage	Direct Energy	**Total**
1 January 2012	73	–	**73**	–	8	**81**
Revisions of previous estimates	6	–	**6**	–	2	**8**
Purchases/(disposals) of reserves in place (i)	55	–	**55**	–	2	**57**
Extensions, discoveries and other additions (ii)	10	–	**10**	–	–	**10**
Production (iv)	(15)	–	**(15)**	–	(1)	**(16)**
31 December 2012	**129**	**–**	**129**	**–**	**11**	**140**

Estimated net 2P reserves (million barrels of oil equivalent)	Europe	Trinidad and Tobago (iii)	**Centrica Energy**	Centrica Storage	Direct Energy	**Total**
31 December 2012 (v)	502	23	**525**	30	108	**663**

(i) Reflects the acquisition of additional equity in the Statfjord, Seymour, Armada, Skirne, Vale, Heimdal and Maria fields and the acquisition of equity in the Alba, Kvitebjorn, and Valemon fields in Centrica Energy and the Carrot Creek field in Direct Energy.
(ii) Recognition of reserves associated with the Rhyl and Maria fields in Centrica Energy.
(iii) The Trinidad and Tobago reserves are subject to a production sharing contract and accordingly have been stated on an entitlement basis (including tax barrels).
(iv) Represents total gas and oil produced from the Group's reserves.
(v) Includes the total of estimated gas and liquid reserves at 31 December 2012 in million barrels of oil equivalent.

Liquids reserves include oil, condensate and natural gas liquids.

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FIVE YEAR RECORD (UNAUDITED)

Year ended 31 December	2008 (restated) (i) (ii) (iii) £m	2009 £m	2010 £m	2011 £m	2012 £m
Group revenue from continuing operations (i) (iii)	20,872	21,963	22,423	22,824	**23,942**
Operating profit from continuing operations before exceptional items and certain re-measurements:					
British Gas	712	1,011	1,216	1,005	**1,093**
Centrica Energy	881	525	771	1,023	**1,230**
Centrica Storage	195	168	169	75	**89**
Direct Energy	215	153	234	312	**331**
Adjusted operating profit – operating profit before exceptional items, certain re-measurements and impact of fair value uplifts from Strategic Investments	2,003	1,857	2,390	2,415	**2,743**
Share of joint ventures' and associates' interest and taxation	(3)	(11)	(78)	(102)	**(85)**
Other	(8)	(5)	–	–	**–**
Depreciation of fair value uplifts to property, plant and equipment (iv)	–	(27)	(118)	(105)	**(96)**
	1,992	1,814	2,194	2,208	**2,562**
Operating (loss)/profit from discontinued operations:					
European operations (v)	(52)	105	(2)	13	**–**
Exceptional items and certain re-measurements after taxation	(1,048)	(288)	726	(844)	**(77)**
(Loss)/profit attributable to equity holders of the parent	(137)	844	1,935	421	**1,273**
	Pence	Pence	Pence	Pence	**Pence**
(Loss)/earnings per ordinary share (ii)	(3.3)	16.5	37.6	8.2	**24.6**
Adjusted earnings per ordinary share (ii) (vi)	21.7	21.7	25.2	25.8	**27.1**
Dividend per share declared in respect of the year (vii)	12.2	12.8	14.3	15.4	**16.4**

Assets and liabilities

31 December	2008 (restated) (ii) (viii) (ix) £m	2009 (restated) (ix) £m	2010 (restated) (ix) £m	2011 (restated) (ix) £m	2012 £m
Goodwill and other intangible assets	2,181	2,822	3,454	3,739	**4,122**
Other non-current assets	6,341	9,650	9,815	10,234	**11,690**
Net current assets/(liabilities)	2,163	330	283	(674)	**(352)**
Non-current liabilities	(6,313)	(8,675)	(7,820)	(7,699)	**(9,533)**
Net assets of disposal groups held for sale	–	128	87	–	**–**
Net assets	4,372	4,255	5,819	5,600	**5,927**
Debt, net of cash, cash equivalents and securities:					
Net debt (ix)	(389)	(3,055)	(3,195)	(3,292)	**(4,047)**

Cash flows

Year ended 31 December	2008 (restated) (x) £m	2009 (restated) (x) £m	2010 (restated) (x) £m	2011 £m	2012 £m
Cash flow from operating activities before exceptional payments (x)	279	2,430	2,651	2,531	**3,086**
Payments relating to exceptional charges	(74)	(203)	(223)	(194)	**(266)**
Net cash flow from investing activities (x)	(1,030)	(4,100)	(1,584)	(1,400)	**(2,558)**
Cash flow before cash flow from financing activities	(825)	(1,873)	844	937	**262**

(i) Group revenue and cost of sales have been restated to report gas sales revenue of Centrica Storage net of cost of sales to better reflect the nature of the transactions.
(ii) Restated to capitalise borrowing costs on the adoption of IAS 23 (Amendment) and to reflect the change in British Gas Services Limited's revenue recognition policy.
(iii) Restated to present the European Energy segment, with the exception of the Group's operations in Germany, as a discontinued operation. The operating profit of the Group's operations in Germany is reported within Centrica Energy. Also restated to include the operating profit of joint ventures and associates pre-interest and tax.
(iv) The depreciation of British Energy fair value uplifts is shown net of taxation.
(v) Discontinued in 2009.
(vi) Adjusted earnings per ordinary share excludes depreciation of fair value uplifts to PP&E from Strategic Investments after taxation and certain re-measurements and exceptional items.
(vii) Figures for 2008 have been adjusted to reflect the bonus element of a Rights Issue undertaken during 2008.
(viii) Restated to classify the non-current portions of derivative financial instruments from current assets and liabilities to non-current assets and liabilities.
(ix) To align with management reporting, net debt has been restated to include mark-to-market values on derivative financial instruments used to hedge offsetting changes in borrowings.
(x) The 2008-2010 comparatives have been restated for a change in presentation of emission certificate/allowance cash flows.

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF CENTRICA PLC

We have audited the Group Financial Statements of Centrica plc for the year ended 31 December 2011 which comprise the Group Income Statement, the Group Statement of Comprehensive Income, the Group Statement of Changes in Equity, the Group Balance Sheet, the Group Cash Flow Statement and the related notes and supplementary information. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRS) as adopted by the European Union (EU).

RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITORS

As explained more fully in the Directors' Responsibility Statement set out on page 51, the Directors are responsible for the preparation of the Group Financial Statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the Group Financial Statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the Company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

SCOPE OF THE AUDIT OF THE FINANCIAL STATEMENTS

An audit involves obtaining evidence about the amounts and disclosures in the Financial Statements sufficient to give reasonable assurance that the Financial Statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Group's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Directors; and the overall presentation of the Financial Statements. In addition, we read all the financial and non-financial information in the Annual Report and Accounts to identify material inconsistencies with the audited Financial Statements. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

OPINION ON FINANCIAL STATEMENTS

In our opinion the Group Financial Statements:

- give a true and fair view of the state of the Group's affairs as at 31 December 2011 and of its profit and cash flows for the year then ended;
- have been properly prepared in accordance with IFRS as adopted by the EU; and
- have been prepared in accordance with the requirements of the Companies Act 2006 and Article 4 of the IAS Regulation.

OPINION ON OTHER MATTERS PRESCRIBED BY THE COMPANIES ACT 2006

In our opinion the information given in the Directors' Report for the financial year for which the Group Financial Statements are prepared is consistent with the Group Financial Statements.

MATTERS ON WHICH WE ARE REQUIRED TO REPORT BY EXCEPTION

We have nothing to report in respect of the following:

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- certain disclosures of Directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

Under the Listing Rules we are required to review:

- the Directors' statement, set out on page 51 in relation to going concern;
- the part of the Corporate Governance Statement relating to the Company's compliance with the nine provisions of the UK Corporate Governance Code specified for our review; and
- certain elements of the report to shareholders by the Board on Directors' remuneration.

OTHER MATTER

We have reported separately on the parent Company Financial Statements of Centrica plc for the year ended 31 December 2011 and on the information in the Directors' Remuneration Report that is described as having been audited.

John Maitland
Senior Statutory Auditor
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
London
23 February 2012

Financial Statements

GROUP INCOME STATEMENT

Year ended 31 December	Notes	2011 Business performance £m	2011 Exceptional items and certain re-measurements £m	2011 Results for the year £m	2010 Business performance £m	2010 Exceptional items and certain re-measurements £m	2010 Results for the year £m
Group revenue	4	**22,824**	**–**	**22,824**	22,423	–	22,423
Cost of sales before exceptional items and certain re-measurements	5	**(17,959)**	**–**	**(17,959)**	(17,595)	–	(17,595)
Exceptional items	7	**–**	**(221)**	**(221)**	–	(102)	(102)
Re-measurement of energy contracts	7	**–**	**(437)**	**(437)**	–	1,177	1,177
Cost of sales	5	**(17,959)**	**(658)**	**(18,617)**	(17,595)	1,075	(16,520)
Gross profit		**4,865**	**(658)**	**4,207**	4,828	1,075	5,903
Operating costs before exceptional items	5	**(2,750)**	**–**	**(2,750)**	(2,641)	–	(2,641)
Exceptional items	7	**–**	**(110)**	**(110)**	–	(181)	(181)
Operating costs	5	**(2,750)**	**(110)**	**(2,860)**	(2,641)	(181)	(2,822)
Share of profits/(losses) in joint ventures and associates, net of interest and taxation	7, 16	**93**	**(26)**	**67**	7	(14)	(7)
Group operating profit	4	**2,208**	**(794)**	**1,414**	2,194	880	3,074
Interest income	8	**212**	**–**	**212**	214	–	214
Interest expense	8	**(358)**	**–**	**(358)**	(479)	–	(479)
Net interest expense		**(146)**	**–**	**(146)**	(265)	–	(265)
Profit from continuing operations before taxation		**2,062**	**(794)**	**1,268**	1,929	880	2,809
Taxation on profit from continuing operations	9	**(810)**	**(16)**	**(826)**	(708)	(221)	(929)
Profit from continuing operations after taxation		**1,252**	**(810)**	**442**	1,221	659	1,880
Profit/(loss) from discontinued operations	7	**13**	**22**	**35**	(8)	67	59
(Loss)/profit on disposal of discontinued operations	7, 31	**–**	**(56)**	**(56)**	3	–	3
Discontinued operations		**13**	**(34)**	**(21)**	(5)	67	62
Profit for the year		**1,265**	**(844)**	**421**	1,216	726	1,942
Attributable to:							
Equity holders of the parent		**1,265**	**(844)**	**421**	1,209	726	1,935
Non-controlling interests		**–**	**–**	**–**	7	–	7
		1,265	**(844)**	**421**	1,216	726	1,942

Earnings per ordinary share	Notes	2011 Pence	2010 Pence
From continuing and discontinued operations:			
Basic	11	**8.2**	37.6
Diluted	11	**8.1**	37.3
From continuing operations:			
Basic	11	**8.6**	36.4
Diluted	11	**8.5**	36.1
Interim dividend paid per ordinary share	10	**4.29**	3.84
Final dividend proposed per ordinary share	10	**11.11**	10.46

The notes on pages 70 to 122 form part of these Financial Statements.

Financial Statements

GROUP STATEMENT OF COMPREHENSIVE INCOME

Year ended 31 December	Notes	2011 £m	2010 £m
Profit for the year		**421**	1,942
Other comprehensive income/(losses):			
Transfer of available-for-sale reserve to income statement	27	**23**	–
Losses on revaluation of available-for-sale securities	27	**(4)**	(4)
Taxation on revaluation of available-for-sale securities	27	**(2)**	(1)
		17	(5)
Unrealised (losses)/gains on cash flow hedges	27	**(99)**	10
Transferred to income and expense on cash flow hedges	27	**42**	236
Transferred to assets and liabilities on cash flow hedges	27	**2**	19
Recycling of foreign exchange gains on cash flow hedges on disposal of business	27	**–**	9
Exchange differences on cash flow hedges	27	**(3)**	(8)
Taxation on cash flow hedges	27	**23**	(79)
		(35)	187
Exchange differences on translation of foreign operations	27	**(12)**	70
Recycling of foreign exchange loss on disposal of business	27	**(3)**	(1)
Taxation on related exchange differences	27	**–**	14
		(15)	83
Net actuarial gains/(losses) on defined benefit pension schemes	27	**198**	(9)
Exchange loss on translation of actuarial reserve	27	**–**	(1)
Taxation on net actuarial gains/(losses) on defined benefit pension schemes	27	**(59)**	(2)
		139	(12)
Share of joint ventures/associates actuarial (loss)/gain (post tax)	16	**(24)**	14
Share of joint ventures/associates cash flow hedge reserve (loss)/gain (post tax)	16	**(1)**	1
		(25)	15
Other comprehensive income net of taxation		**81**	268
Total comprehensive income for the year		**502**	2,210

GROUP STATEMENT OF CHANGES IN EQUITY

	Attributable to equity holders of the parent							
	Share capital (note 26) £m	Share premium £m	Retained earnings £m	Accumulated other comprehensive income/(loss) (note 27) £m	Other equity (note 28) £m	**Total £m**	Non-controlling interests £m	**Total equity £m**
1 January 2010	317	778	3,103	(587)	581	4,192	63	4,255
Total comprehensive income	–	–	1,935	268	–	2,203	7	2,210
Employee share schemes	1	55	16	–	(3)	69	–	69
Liquidation of subsidiaries	–	–	–	–	–	–	(70)	(70)
Dividends	–	–	(668)	–	–	(668)	–	(668)
Taxation	–	–	–	–	20	20	–	20
Exchange adjustments	–	–	–	–	3	3	–	3
31 December 2010	318	833	4,386	(319)	601	5,819	–	5,819
Total comprehensive income	–	–	421	81	–	**502**	–	**502**
Employee share schemes	1	41	5	–	10	**57**	–	**57**
Dividends	–	–	(762)	–	–	**(762)**	–	**(762)**
Purchase of non-controlling interest	–	–	(7)	–	–	**(7)**	–	**(7)**
Taxation	–	–	–	–	(8)	**(8)**	–	**(8)**
Exchange adjustments	–	–	–	–	(1)	**(1)**	–	**(1)**
31 December 2011	**319**	**874**	**4,043**	**(238)**	**602**	**5,600**	**–**	**5,600**

The notes on pages 70 to 122 form part of these Financial Statements.

Financial Statements

GROUP BALANCE SHEET

31 December	Notes	2011 £m	2010 £m
Non-current assets			
Goodwill	14	**2,518**	2,370
Other intangible assets	14	**1,221**	1,084
Property, plant and equipment	15	**6,412**	6,398
Interests in joint ventures and associates	16	**2,620**	2,507
Deferred tax assets	22	**235**	238
Trade and other receivables	18	**74**	97
Derivative financial instruments	19	**290**	341
Securities	12	**190**	234
Retirement benefit assets	29	**413**	–
		13,973	13,269
Current assets			
Inventories	17	**442**	344
Current tax assets		**81**	81
Trade and other receivables	18	**4,212**	4,187
Derivative financial instruments	19	**315**	449
Securities	12	**28**	23
Cash and cash equivalents	12	**518**	467
		5,596	5,551
Assets of disposal groups classified as held for sale	31	**–**	455
Total assets		**19,569**	19,275
Current liabilities			
Trade and other payables	21	**(4,094)**	(4,059)
Current tax liabilities		**(226)**	(182)
Bank overdrafts, loans and other borrowings	12	**(502)**	(77)
Derivative financial instruments	19	**(1,140)**	(755)
Provisions for other liabilities and charges	23	**(308)**	(195)
		(6,270)	(5,268)
Net current (liabilities)/assets		**(674)**	283
Non-current liabilities			
Trade and other payables	21	**(33)**	(56)
Bank overdrafts, loans and other borrowings	12	**(3,669)**	(3,959)
Derivative financial instruments	19	**(505)**	(648)
Deferred tax liabilities	22	**(1,506)**	(1,367)
Provisions for other liabilities and charges	23	**(1,903)**	(1,551)
Retirement benefit obligations	29	**(83)**	(239)
		(7,699)	(7,820)
Liabilities of disposal groups classified as held for sale	31	**–**	(368)
Net assets		**5,600**	5,819
Equity			
Share capital	26	**319**	318
Share premium		**874**	833
Retained earnings		**4,043**	4,386
Accumulated other comprehensive loss	27	**(238)**	(319)
Other equity	28	**602**	601
Total shareholders' equity		**5,600**	5,819

The Financial Statements on pages 66 to 122 were approved and authorised for issue by the Board of Directors on 23 February 2012 and were signed below on its behalf by:

Sam Laidlaw
Chief Executive

Nick Luff
Group Finance Director

The notes on pages 70 to 122 form part of these Financial Statements.

GROUP CASH FLOW STATEMENT

Year ended 31 December	Notes	2011 £m	2010 (restated) (i) £m
Cash generated from continuing operations	13	**3,229**	3,190
Income taxes paid		**(430)**	(412)
Net petroleum revenue tax paid		**(262)**	(128)
Interest received		**20**	5
Interest paid		**(3)**	(11)
Payments relating to exceptional charges		**(194)**	(223)
Net cash flow from continuing operating activities		**2,360**	2,421
Net cash flow from discontinued operating activities		**(23)**	7
Net cash flow from operating activities		**2,337**	2,428
Purchase of businesses net of cash and cash equivalents acquired	30	**(394)**	(606)
Sale of businesses net of cash and cash equivalents disposed of	31	**78**	9
Purchase of intangible assets	4,14	**(299)**	(406)
Purchase of property, plant and equipment	4,15	**(765)**	(547)
Disposal of property, plant and equipment and intangible assets		**6**	47
Investments in joint ventures and associates	16	**(236)**	(149)
Dividends received from joint ventures and associates	16	**147**	83
Repayments of loans to, and disposal of investments in, joint ventures and associates	16	**10**	26
Interest received		**6**	19
Net sale/(purchase) of securities	13	**48**	(56)
Net cash flow from continuing investing activities		**(1,399)**	(1,580)
Net cash flow from discontinued investing activities		**(1)**	(4)
Net cash flow from investing activities		**(1,400)**	(1,584)
Issue of ordinary share capital	26	**23**	31
Purchase of treasury shares		**(6)**	(9)
Financing interest received		**9**	–
Financing interest paid		**(202)**	(292)
Cash inflow from additional debt		**114**	267
Cash outflow from payment of capital element of finance leases		**(25)**	(23)
Cash outflow from repayment of other debt		**(30)**	(928)
Net cash flow from increase/(reduction) in debt	13	**59**	(684)
Realised net foreign exchange loss on cash settlement of derivative contracts		**(28)**	(55)
Equity dividends paid	10	**(762)**	(668)
Net cash flow from continuing financing activities		**(907)**	(1,677)
Net increase/(decrease) in cash and cash equivalents		**30**	(833)
Cash and cash equivalents at 1 January		**451**	1,285
Effect of foreign exchange rate changes		**(2)**	(1)
Cash and cash equivalents at 31 December		**479**	451
Included in the following lines of the Balance Sheet:			
Cash and cash equivalents	12	**518**	467
Bank overdrafts, loans and other borrowings		**(39)**	(19)
Assets of disposal groups classified as held for sale	31	**–**	3
		479	451

(i) The 2010 comparatives have been restated for a change in presentation of emission certificate/allowance cash flows, see note 1(d).

The notes on pages 70 to 122 form part of these Financial Statements.

NOTES TO THE FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT NEW ACCOUNTING POLICIES AND REPORTING CHANGES

The principal accounting policies applied in the preparation of these consolidated Financial Statements are set out below and in the supplementary information (note S2).

Basis of preparation

The consolidated Financial Statements have been prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union (EU) and therefore comply with Article 4 of the EU IAS Regulation and the Companies Act 2006.

The consolidated Financial Statements have been prepared on the historical cost basis, except for derivative financial instruments, available-for-sale financial assets, financial instruments designated as at fair value through profit or loss on initial recognition, and the assets of the Group pension schemes that have been measured at fair value; and the liabilities of the Group pension schemes that are measured using the projected unit credit valuation method. The carrying values of recognised assets and liabilities that are hedged items in fair value hedges, and are otherwise carried at cost, are adjusted to record changes in the fair values attributable to the risks that are being hedged.

The preparation of Financial Statements in conformity with IFRS as adopted by the EU requires the use of certain critical accounting estimates. It requires management to exercise its judgement in the processes of applying the Group's accounting policies. The areas involving a higher degree of judgement, complexity or areas where assumptions and estimates are significant to the consolidated Financial Statements are described in notes 2 and 3.

(a) Standards, amendments and interpretations effective in 2011

There are no IFRSs or IFRIC interpretations that are effective for the first time for the current financial year that have had a material impact on the Group.

(b) Standards, amendments and interpretations that are not yet effective and that have not been early adopted by the Group

At the date of authorisation of these Financial Statements, a number of standards, amendments to existing standards and interpretations have been issued but are not yet effective. The Group has not early adopted any of these. The standards and amendments to standards that could have an impact on the Group's future financial statements are: IFRS 9, 10, 11, 12, 13 and amendments to IAS 19. The Group is currently assessing the impact these may have.

(c) Change to operating segments

The Upstream UK operating structure is now presented in two segments, Gas and Power. These new segments are each based on the prior year segments of Upstream gas and oil and Power generation respectively. The remaining segments of Industrial and commercial and Proprietary energy trading have been allocated between the new Gas and Power segments. The new structure is consistent with how the Group reports to the Chief Operating Decision Maker defined in IFRS 8. Comparatives have been restated accordingly.

(d) Change to cash flow presentation in relation to emissions certificates/allowances

Cash flows in relation to the purchase of emissions certificates/allowances have previously been classified within investing cash flows, as emissions certificates/allowances are accounted for as intangible assets. The Group continues to account for emissions certificates/allowances as intangible assets in the Group Balance Sheet but the associated cash flows have now been included within working capital movements in operating cash flows in the Group Cash Flow Statement as this presentation better reflects the nature of the cash flows. In 2011, the cash outflow amounts to £216 million (2010: £255 million). Comparatives have been restated accordingly.

2. CENTRICA SPECIFIC ACCOUNTING MEASURES

Use of adjusted profit measures

The Directors believe that reporting adjusted profit and adjusted earnings per share measures provides additional useful information on business performance and underlying trends. These measures are used for internal performance purposes. The adjusted measures in this report are not defined terms under IFRS and may not be comparable with similarly titled measures reported by other companies.

The measure of operating profit used by management to evaluate segment performance is adjusted operating profit. Adjusted operating profit is defined as operating profit before:

- exceptional items
- certain re-measurements
- depreciation resulting from fair value uplifts to property, plant and equipment (PP&E) on the acquisition of Strategic Investments

but including:

- the Group's share of the results from joint ventures and associates before interest and taxation.

Note 4 contains an analysis of adjusted operating profit by segment and a reconciliation of adjusted operating profit to operating profit after exceptional items and certain re-measurements.

Adjusted earnings is defined as earnings before:

- exceptional items net of taxation
- certain re-measurements net of taxation and
- depreciation of fair value uplifts to PP&E on the acquisition of Strategic Investments, net of taxation.

A reconciliation of earnings is provided in note 11.

The Directors have determined that for Strategic Investments it is important to separately identify the earnings impact of increased depreciation arising from the acquisition-date fair value uplifts made to PP&E over their useful economic lives. As a result of the nature of fair value assessments in the energy industry, the value attributed to strategic assets is a subjective judgement based on a wide range of complex variables at a point in time. The subsequent depreciation of the fair value uplifts bears little relationship to current market conditions, operational performance or underlying cash generation. Management therefore reports and monitors the operational performance of Strategic Investments before the impact of depreciation on fair value uplifts to PP&E and the segmental results are presented on a consistent basis.

The Group has two Strategic Investments for which reported profits have been adjusted due to the impact of fair value uplifts. These Strategic Investments relate to the 2009 acquisitions of

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

2. CENTRICA SPECIFIC ACCOUNTING MEASURES CONTINUED

Venture Production plc ('Venture') the operating results of which are included within the Upstream UK – Gas segment and the acquisition of the 20% interest in Lake Acquisitions Limited ('British Energy'), which owned the British Energy Group, the results of which are included within the Upstream UK – Power segment.

(i) Venture

Significant adjustments have been made to the acquired PP&E to report the acquired oil and gas field interests at their acquisition-date fair values which are subsequently depreciated through the Group Income Statement over their respective useful economic lives using the unit of production method.

Whilst the impact of unwinding the PP&E at their acquisition-date fair values is included in overall reported profit for the year, the Directors have reversed the earnings impact of the increased depreciation and related taxation resulting from fair value uplifts to the acquired oil and gas interests in order to arrive at adjusted profit from continuing operations after taxation.

(ii) British Energy

The 20% interest in British Energy is accounted for as an investment in an associate using the equity method. Hence, the Group reports its share of the associate's profit or loss, which is net of interest and taxation, within the Group Income Statement.

The most significant fair value adjustments arising on the acquisition of the 20% investment in British Energy relate to the fair value uplifts made to the British Energy nuclear power stations to report the PP&E at their acquisition-date fair values and fair value uplifts made to British Energy's energy procurement contracts and energy sales contracts to report these at their acquisition-date fair values.

Whilst the impact of increased depreciation and related taxation through unwinding the fair value uplifts to the nuclear power stations is included in the share of associate's post-acquisition result included in overall reported Group profit for the year, the Directors have reversed these impacts in arriving at adjusted profit from continuing operations for the year. The impact of unwinding the acquisition-date fair values attributable to the acquired energy procurement and energy sales contracts is included within certain re-measurements.

Exceptional items and certain re-measurements

The Group reflects its underlying financial results in the 'business performance' column of the Group Income Statement. To be able to provide readers with this clear and consistent presentation, the effects of 'certain re-measurements' of financial instruments, and 'exceptional items', are reported separately in a different column in the Income Statement.

Certain re-measurements predominantly relate to fair value movements on a number of contracts (derivative instruments) entered into as part of the Group's energy procurement or sales activities. Primarily because these contracts include terms that permit net settlement, the rules within IAS 39 require the contracts to be individually fair valued. These individual, unrealised fair value movements do not reflect the underlying performance of the business because they are economically related to our Upstream assets or Downstream demand, which are not fair valued. Therefore, these certain re-measurements are reported separately.

Exceptional items are those items which are of a non-recurring nature and, in the judgement of the Directors, need to be disclosed separately by virtue of their nature, size or incidence. Again, to ensure the business performance column reflects the underlying results of the Group, these exceptional items are also reported in a separate column in the Group Income Statement. Items which may be considered exceptional in nature include disposals of businesses, business restructurings, significant onerous contract charges, and asset write-downs.

See note S2 for a more detailed explanation of the accounting treatment for exceptional items and certain re-measurements.

3. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY

(a) Critical judgements in applying the Group's accounting policies

The Group's accounting policies as set out in note S2 and Notes to the Financial Statements include descriptions of judgements management has made in applying the Group's accounting policies. Areas of judgement that have the most significant effect on the amounts recognised in the Financial Statements (apart from those involving estimations which are dealt with below) include the following:

- the presentation of selected items as exceptional, see notes 2, 7 and S2;
- the use of adjusted profit and adjusted earnings per share measures, see notes 2, 4 and 11;
- the classification of energy procurement contracts as derivative financial instruments and presentation as certain re-measurements, see notes 2, 7 and 19.

In addition to those described above, management has made the following key judgements in applying the Group's accounting policies that have the most significant effect on the Group's Financial Statements.

Wind farm partial disposals

In the past few years, the Group has disposed of 50% of the equity voting capital (and 50% of the shareholder loans where relevant) in wind farm owning companies (for example, GLID Wind Farms TopCo Limited ('GLID') and Lincs Wind Farm Limited ('Lincs')).

As part of these disposals, the Group contracted to purchase a large percentage of the output produced by the wind farms under arm's length, 15-year, offtake agreements. The Group also contracted to provide management, operational and transitional support services to these companies as directed by their boards (and shareholders). Shareholders' agreements were put in place which included a number of reserved matters and provide for joint management of the major decisions of the companies.

Accordingly, the Directors have judged that the disposal of equity voting share capital (and shareholder loans) was a loss of control over the financial and operating policies of the companies. Therefore, the remaining investments are equity accounted as investments in joint ventures (see note 16). The Directors have also judged that the 15-year offtake agreements are not leasing arrangements. This is because the Group is not purchasing substantially all of the economic output of the wind farms. These contracts are considered to be outside the scope of IAS 39 apart from the embedded derivatives arising from the pricing terms which are marked to market separately.

Leases – third-party power station tolling arrangements

The Group has two long-term power station tolling contracts: (i) Spalding in the UK and (ii) Rijnmond in the Netherlands. The arrangements provide Centrica with the right to nominate 100%

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

3. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY CONTINUED

of the plant output for the duration of the contracts in return for a mix of capacity payments and operating payments based on plant availability.

The Spalding contract runs until 2021 and Centrica holds an option to extend the tolling arrangement for a further eight years, exercisable by 30 September 2020. If extended, Centrica is granted an option to purchase the station at the end of this further period. The Directors have judged that the arrangement should be accounted for as a finance lease as the lease term is judged to be substantially all of the economic life of the power station and the present value of the minimum lease payments at inception date of the arrangement amounted to substantially all of the fair value of the power station at that time. Details of the interest charges, finance lease creditor and finance lease asset are included in notes 8, 12 and 15 respectively.

The Rijnmond contract runs until 2030 and Centrica does not have the right to extend the agreement or any option to purchase the plant. The Directors have judged that the arrangement should be accounted for as an operating lease as the lease term is not judged to be substantially all of the economic life of the power station and the present value of the minimum lease payments at inception date of the arrangement did not amount to substantially all of the fair value of the power station at that time. Details of the operating lease disclosures are included in note 34.

Business combinations and acquisitions – purchase price allocations

Business combinations and acquisitions of associates and joint ventures require a fair value exercise to be undertaken to allocate the purchase price (cost) to the fair value of the acquired identifiable assets, liabilities and contingent liabilities.

As a result of the nature of fair value assessments in the energy industry this purchase price allocation exercise requires subjective judgements based on a wide range of complex variables at a point in time. Management uses all available information to make the fair value determinations. Business combinations are set out in note 30.

EU Emissions Trading Scheme

In the absence of specific guidance under IFRS, the Group has adopted an accounting policy which recognises carbon dioxide emissions liabilities when the level of emissions exceeds the level of allowances granted by the Government in the period. The liability is measured at the cost of purchased allowances up to the level of purchased allowances held, and then at market price of allowances ruling at the balance sheet date. Movements in the liability are reflected within operating profit. Forward contracts for sales and purchases of allowances are measured at fair value. The Directors have judged that this accounting policy most appropriately reflects the economic impact of the scheme on the Group.

(b) Key sources of estimation uncertainty

The key assumptions concerning the future, and other key sources of estimation uncertainty at the balance sheet date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year, are discussed below.

Revenue recognition – unread gas and electricity meters

Revenue for energy supply activities includes an assessment of energy supplied to customers between the date of the last meter reading and the year end (unread). Unread gas and electricity comprises both billed and unbilled revenue. It is estimated through the billing systems, using historical consumption patterns, on a customer by customer basis, taking into account weather patterns, load forecasts and the differences between actual meter reads being returned and system estimates. Actual meter reads continue to be compared to system estimates between the balance sheet date and the finalisation of the accounts. An assessment is also made of any factors that are likely to materially affect the ultimate economic benefits which will flow to the Group, including bill cancellation and re-bill rates. To the extent that the economic benefits are not expected to flow to the Group, the value of that revenue is not recognised. The judgements applied, and the assumptions underpinning these judgements, are considered to be appropriate. However, a change in these assumptions would have an impact on the amount of revenue recognised.

Industry reconciliation process – cost of sales

Industry reconciliation procedures are required as differences arise between the estimated quantity of gas and electricity the Group deems to have supplied and billed customers, and the estimated quantity industry system operators deem the individual suppliers, including the Group, to have supplied to customers. Difference in deemed supply is referred to as imbalance. The reconciliation procedures can result in either a higher or lower value of industry deemed supply than has been estimated as being supplied to customers by the Group, but in practice tends to result in a higher value of deemed supply. The Group then reviews the difference to ascertain whether there is evidence that its estimate of amounts supplied to customers is inaccurate or whether the difference arises from other causes. The Group's share of the resulting imbalance is included within commodity costs charged to cost of sales. Management estimates the level of recovery of imbalance which will be achieved either through subsequent customer billing or through developing industry settlement procedures.

Decommissioning costs

The estimated cost of decommissioning at the end of the producing lives of fields (including storage assets) is reviewed periodically and is based on proven and probable reserves, price levels and technology at the balance sheet date. Provision is made for the estimated cost of decommissioning at the balance sheet date. The payment dates of total expected future decommissioning costs are uncertain and dependent on the lives of the facilities, but are currently anticipated to be incurred until 2055, with the majority of the costs expected to be paid between 2020 and 2030.

Significant judgements and estimates are also made about the costs of decommissioning British Energy's nuclear power stations and the costs of waste management and spent fuel. These estimates impact the carrying value of our investment. Various arrangements and indemnities are in place with the Secretary of State with respect to these costs, as explained in note S2.

Gas and liquids reserves

The volume of proven and probable ('2P') gas and liquids reserves is an estimate that affects the unit of production, depreciation of producing gas and liquids PP&E as well as being a significant estimate affecting decommissioning and impairment calculations. The factors impacting gas and liquids estimates, the process for estimating reserve quantities and reserve recognition are described on page 129.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

3. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY CONTINUED

The impact of a change in estimated 2P reserves is dealt with prospectively by depreciating the remaining book value of producing assets over the expected future production. If 2P reserves estimates are revised downwards, earnings could be affected by higher depreciation expense or an immediate write-down (impairment) of the asset's book value.

Determination of fair values – energy derivatives

Fair values of energy derivatives are estimated by reference in part to published price quotations in active markets and in part by using valuation techniques. More detail on the assumptions used in determining fair valuations is provided in note 24.

Impairment of long-lived assets

The Group has several material long-lived assets that are assessed or tested for impairment at each reporting date in accordance with the Group's accounting policy as described in note S2. The Group make judgements and estimates in considering whether the carrying amounts of these assets or cash generating units (CGUs) are recoverable. The key assets that are subjected to impairment tests are upstream gas and oil assets, power generation assets, storage facility assets, nuclear investment (investment in associate) and goodwill.

Upstream gas and oil assets

The recoverable amount of the Group's gas and oil assets is determined by discounting the post-tax cash flows expected to be generated by the assets over their lives. The cash flows are derived from projected production profiles of each field, based predominantly on expected 2P reserves and take into account forward prices for gas and liquids over the relevant period. Where forward market prices are not available, prices are determined based on internal model inputs. The recoverable amount also takes into account assumptions market participants would use in estimating fair value.

Power generation assets

The recoverable amount of the Group's power generation assets is calculated by discounting the pre-tax cash flows expected to be generated by the assets and is dependent on views of forecast power generation, forecast power, gas and carbon prices (where applicable) and the timing and extent of capital expenditure. Where forward market prices are not available, prices are determined based on internal model inputs. The current year impairment charge in relation to UK gas-fired power stations assumes overcapacity in the UK power generation market post 2018 will diminish and normal returns will be achievable on our most efficient assets. Should the overcapacity not diminish, there is a risk of further impairment to assets with a total net book value of £664 million.

Storage facility assets

The recoverable amount of our planned storage facilities is calculated by discounting the post-tax cash flows expected to be generated by the assets based on predictions of seasonal gas price differentials and shorter term price volatilities less any related capital and operating expenditure. This is then compared to the book value. Should the business cases not support the planned investments, this risks a loss of pre-development costs incurred to date, as detailed in notes 14 and 15.

Nuclear investment

The recoverable amount of the Nuclear investment is based on the value of the existing British Energy nuclear fleet and the value of Nuclear New Build (NNB). The existing fleet value is calculated by discounting post-tax cash flows derived from the stations based on forecast power generation and power prices, whilst taking account of planned outages and the possibility of life extensions. The NNB value is similarly dependent on power prices and generation but also on build cost, decommissioning assessments and government support for nuclear. Should the business case not support the new nuclear investment, this would risk a loss of pre-development costs invested to date, as detailed in note 16.

Goodwill

Goodwill does not generate independent cash flows and accordingly is allocated at inception to specific CGUs or groups of CGUs for impairment testing purposes. The recoverable amounts of these CGUs are derived from estimates of future cash flows (as described in the asset classes above). The goodwill impairment tests are also subject to these key estimates.

Further detail on impairments arising and the assumptions used in determining the recoverable amounts is provided in notes 14 and 15.

Credit provisions for trade and other receivables

The methodology for determining provisions for credit losses on trade and other receivables and the level of such provisions is set out in note 18. Although the provisions recognised are considered appropriate, the use of different assumptions or changes in economic conditions could lead to changes in the provisions and therefore impact profit or loss.

Pensions and other post–employment benefits

The cost of providing benefits under defined benefit schemes is determined separately for each of the Group's schemes under the projected unit credit actuarial valuation method. Actuarial gains and losses are recognised in full in the period in which they occur. The key assumptions used for the actuarial valuation are based on the Group's best estimate of the variables that will determine the ultimate cost of providing post-employment benefits, on which further detail is provided in notes 29 and S6.

Provisions for onerous contracts

The Group has entered into a number of commodity procurement and capacity contracts related to specific assets in the ordinary course of its business. Where the unavoidable costs of meeting the obligations under these contracts exceed the associated, expected future net revenues, an onerous contract provision is recognised. The calculation of these provisions will involve the use of estimates. The key onerous provisions are as follows:

Rijnmond power station operating lease

The onerous provision is calculated using net revenue estimates related to power, gas and carbon forward prices less the tolling costs. The contract runs until 2030 and so there is currently no liquid market for these commodities for much of this period.

European gas transportation capacity contracts

The onerous provision is calculated using capacity costs incurred under the contracts, less any predicted income. The current year charge assumes that all contracts are onerous for the period to 2018 but that post-2018 the remaining capacities could still be necessary to secure supplies of gas into the UK. Therefore no provision has been recognised relating to this latter period.

North American wind farm power purchase agreements

The onerous nature of the power purchase agreements is measured using estimates relating to wind forecasts, forward curves for energy prices, balancing costs and renewable energy certificates for which there is not a liquid market for the full term of all the contracts.

Further detail of these provisions is provided in note 7.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

4. SEGMENTAL ANALYSIS

The Group's results are discussed in the Business Review (page 5 to 40). For a description of the products and services from which each reportable segment derives its revenues, see note S5. The Group's segmental results are as follows:

Year ended 31 December	2011			2010 (restated) (ii)		
(a) Revenue	Gross segment revenue £m	Less inter-segment revenue (i) £m	Group revenue £m	Gross segment revenue £m	Less inter-segment revenue (i) £m	Group revenue £m
Continuing operations:						
Residential energy supply	**8,113**	**(3)**	**8,110**	8,359	(4)	8,355
Residential services	**1,504**	**–**	**1,504**	1,464	–	1,464
Business energy supply and services	**2,702**	**(1)**	**2,701**	2,907	(1)	2,906
Downstream UK	**12,319**	**(4)**	**12,315**	12,730	(5)	12,725
Gas (ii)	**3,571**	**(521)**	**3,050**	2,490	(431)	2,059
Power (ii)	**1,588**	**(179)**	**1,409**	1,519	(13)	1,506
Upstream UK	**5,159**	**(700)**	**4,459**	4,009	(444)	3,565
Storage UK	**184**	**(20)**	**164**	267	(35)	232
Residential energy supply	**2,416**	**–**	**2,416**	2,502	–	2,502
Business energy supply	**2,748**	**–**	**2,748**	2,682	–	2,682
Residential and business services	**520**	**–**	**520**	485	–	485
Upstream and wholesale energy	**433**	**(231)**	**202**	328	(96)	232
North America	**6,117**	**(231)**	**5,886**	5,997	(96)	5,901
	23,779	**(955)**	**22,824**	23,003	(580)	22,423
Discontinued operations:						
European Energy (note 31)	**167**	**–**	**167**	590	–	590

(i) Inter-segment revenue is subject to year on year fluctuations due to the change in the mix of internal and external energy sales by Upstream UK.
(ii) The Industrial and commercial and Proprietary energy trading businesses have been reallocated into the new Power and Gas segments. See note 1(c).

The Group operates in the following geographical areas:

Year ended 31 December	Revenue (based on location of customer) 2011 £m	2010 (restated) (i) £m
Continuing operations:		
UK	**15,760**	15,811
USA	**3,787**	3,729
Canada	**2,100**	2,173
Rest of the world	**1,177**	710
	22,824	22,423

(i) During the year a system upgrade has enabled a more detailed geographic analysis of assets. Prior year figures have been restated accordingly.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

4. SEGMENTAL ANALYSIS CONTINUED

Year ended 31 December

(b) Operating profit	2011 £m	2010 (restated) (i) £m
Continuing operations:		
Residential energy supply	**522**	742
Residential services	**264**	241
Business energy supply and services	**219**	233
Downstream UK	**1,005**	1,216
Gas (i) (ii)	**769**	566
Power (i) (ii)	**254**	205
Upstream UK	**1,023**	771
Storage UK	**75**	169
Residential energy supply	**161**	177
Business energy supply	**110**	88
Residential and business services	**28**	15
Upstream and wholesale energy	**13**	(46)
North America	**312**	234
Adjusted operating profit – segment operating profit before exceptional items, certain re-measurements and impact of fair value uplifts from Strategic Investments (iii)	**2,415**	2,390
Share of joint ventures/associates' interest and taxation	**(102)**	(78)
Depreciation of fair value uplifts to property, plant and equipment – Venture (ii)	**(64)**	(60)
Depreciation of fair value uplifts to property, plant and equipment (net of taxation) – associates – British Energy (ii)	**(41)**	(58)
	2,208	2,194
Exceptional items (note 7)	**(331)**	(283)
Certain re-measurements included within gross profit (note 7)	**(437)**	1,177
Certain re-measurements of associates' energy contracts (net of taxation) (note 7)	**(26)**	(14)
Operating profit after exceptional items and certain re-measurements	**1,414**	3,074
Discontinued operations:		
European Energy (note 31) (iv)	**13**	(5)

(i) The Industrial and commercial and Proprietary energy trading businesses have been reallocated into the new Power and Gas segments. See note 1(c).
(ii) See note 2 and note 11 for explanation of the depreciation on fair value uplifts to PP&E on acquiring Strategic Investments.
(iii) Includes results of equity-accounted interests before interest and taxation.
(iv) Represents profit/(loss) after taxation and before exceptional items and certain re-measurements of Oxxio B.V. up to the date of disposal. This is the measure of results of discontinued operations that is reported regularly to the Group's Executive Committee.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

4. SEGMENTAL ANALYSIS CONTINUED

Year ended 31 December	Share of results of joint ventures and associates before interest and taxation		Depreciation and impairments of property, plant and equipment (i)		Amortisation, write-downs and impairments of intangibles	
(c) Included within adjusted operating profit	**2011 £m**	2010 (restated) (iii) £m	**2011 £m**	2010 (restated) (iii) £m	**2011 £m**	2010 (restated) (iii) £m
Continuing operations:						
Residential energy supply	**–**	–	**8**	6	**23**	38
Residential services	**–**	–	**18**	9	**6**	1
Business energy supply and services	**–**	–	**2**	2	**7**	7
Downstream UK	**–**	–	**28**	17	**36**	46
Gas (i) (ii) (iii)	**(1)**	3	**503**	487	**52**	91
Power (i) (iii) (iv)	**237**	140	**112**	120	**4**	1
Upstream UK	**236**	143	**615**	607	**56**	92
Storage UK	**–**	–	**30**	26	**–**	–
Residential energy supply	**–**	–	**1**	–	**9**	5
Business energy supply	**–**	–	**1**	1	**4**	4
Residential and business services	**–**	–	**3**	2	**6**	5
Upstream and wholesale energy (ii)	**–**	–	**89**	88	**4**	3
North America	**–**	–	**94**	91	**23**	17
Other (v)	**–**	–	**19**	15	**25**	19
	236	143	**786**	756	**140**	174

(i) Depreciation of PP&E is stated before depreciation of fair value uplifts for Strategic Investments.
(ii) During 2011, £46 million of write downs relating to exploration and evaluation assets were incurred in Upstream UK (2010: £81 million in Upstream UK and £2 million in Upstream North America), as described in note 14.
(iii) The Industrial and commercial and Proprietary energy trading businesses have been reallocated into the new Power and Gas segments. See note 1(c).
(iv) Share of results of joint ventures and associates is before interest, certain re-measurements, depreciation of fair value uplifts to PP&E on Strategic Investments and taxation.
(v) Other comprises depreciation of PP&E and amortisation and write-downs of intangibles on Corporate Centre assets which are charged out to other Group segments.

(d) Assets and liabilities

The Group operates in the following geographical areas:

31 December	Non-current assets (based on location of assets) (i)	
	2011 £m	2010 (restated) (ii) £m
Continuing operations:		
UK	**9,146**	8,955
Canada	**1,349**	1,381
USA	**1,064**	820
Rest of the world	**1,212**	1,203
	12,771	12,359

(i) Non-current assets include goodwill, other intangible assets, PP&E and interest in joint ventures and associates.
(ii) During the year a system upgrade has enabled a more detailed geographic analysis of assets. Comparatives have been restated accordingly.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

4. SEGMENTAL ANALYSIS CONTINUED

31 December	Net segment assets/(liabilities)		Average capital employed Year ended 31 December	
(d) Assets and liabilities continued	**2011 £m**	2010 (restated) (i) £m	**2011 £m**	2010 (restated) (i) £m
Residential energy supply	**125**	27	**151**	195
Residential services	**254**	225	**258**	95
Business energy supply and services	**558**	516	**569**	552
Downstream UK	**937**	768	**978**	842
Gas (i)	**2,427**	2,894	**1,500**	1,240
Power (i)	**3,534**	3,677	**3,335**	3,446
Upstream UK	**5,961**	6,571	**4,835**	4,686
Storage UK	**517**	347	**221**	206
Residential energy supply	**925**	731	**715**	709
Business energy supply	**459**	441	**315**	288
Residential and business services	**377**	400	**366**	323
Upstream and wholesale energy	**733**	784	**677**	659
North America	**2,494**	2,356	**2,073**	1,979
	9,909	10,042	**8,107**	7,713
Unallocated current and deferred tax balances	**186**	217		
Derivative financial instruments held for energy procurement (ii)	**(1,214)**	(715)		
Bank overdrafts and loans, securities and treasury derivatives	**(3,868)**	(3,716)		
Retirement benefit assets/(obligations)	**330**	(239)		
Corporate centre assets and discontinued operations (iii)	**257**	230		
Non-operating liabilities	**(4,309)**	(4,223)		
	5,600	5,819		

(i) The Industrial and commercial and Proprietary energy trading businesses have been reallocated into the new Power and Gas segments. See note 1(c).
(ii) Includes balances held by joint ventures/associates.
(iii) During 2010 assets and liabilities of discontinued operations were classified as held for sale.

Capital employed represents the investment required to operate each of the Group's segments. Capital employed is used by the Group to calculate the return on capital employed for each of the Group's segments as part of the Group's managing for value concept. Additional value is created when the return on capital employed exceeds the cost of capital. Net segment assets of the Group can be reconciled to the Group's capital employed as follows:

	2011 £m	2010 £m
Net segment assets at 31 December	**9,909**	10,042
Deduct:		
Intra-Group balances	**56**	26
Pre-productive assets	**(2,287)**	(1,659)
Margin call debtor	**(188)**	(161)
Cash at bank, in transit and in hand excluding certain restricted cash	**(44)**	(117)
Effect of averaging	**661**	(418)
Average capital employed for year ended 31 December	**8,107**	7,713

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

4. SEGMENTAL ANALYSIS CONTINUED

(e) Capital expenditure

Year ended 31 December	Capital expenditure on property, plant and equipment (note 15) 2011 £m	2010 (restated) (i) £m	Capital expenditure on intangible assets other than goodwill (note 14) 2011 £m	2010 (restated) (i) (ii) £m
Continuing operations:				
Residential energy supply	**48**	15	**240**	256
Residential services	**6**	6	**22**	15
Business energy supply and services	**3**	1	**75**	68
Downstream UK	**57**	22	**337**	339
Gas (i)	**488**	383	**97**	230
Power (i)	**89**	82	**6**	28
Upstream UK	**577**	465	**103**	258
Storage UK	**59**	33	**–**	–
Residential energy supply	**–**	–	**4**	2
Business energy supply	**1**	–	**18**	10
Residential and business services	**2**	2	**1**	5
Upstream and wholesale energy	**36**	20	**8**	10
North America	**39**	22	**31**	27
Other	**26**	16	**49**	29
Capital expenditure on continuing operations	**758**	558	**520**	653
(Decrease)/increase in prepayments related to capital expenditure	**(15)**	18	**–**	6
Capitalised borrowing costs	**(46)**	(37)	**–**	–
Decrease/(increase) in trade payables related to capital expenditure	**68**	8	**(5)**	2
Purchases of emissions allowances and renewable obligations certificates (ii)	**–**	–	**(216)**	(255)
Net cash outflow	**765**	547	**299**	406

(i) The Industrial and commercial and Proprietary energy trading businesses have been reallocated into the new Power and Gas segments. See note 1(c).
(ii) The 2010 comparatives have been restated for a change in presentation of emission certificate/allowance cash flows, see note 1(d).

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

5. COSTS OF CONTINUING OPERATIONS

Analysis of costs by nature	2011 £m	2010 £m
Transportation, distribution and metering costs	**(3,718)**	(3,627)
Commodity costs	**(11,208)**	(11,295)
Depreciation, amortisation and write-downs	**(757)**	(770)
Employee costs	**(672)**	(565)
Other direct costs relating to the upstream businesses	**(389)**	(273)
Other direct costs relating to the downstream businesses	**(1,215)**	(1,065)
Total cost of sales before exceptional items and certain re-measurements	**(17,959)**	(17,595)
Exceptional items and certain re-measurements (note 7)	**(658)**	1,075
Total cost of sales	**(18,617)**	(16,520)
Depreciation, amortisation and write-downs	**(233)**	(224)
Employee costs	**(1,188)**	(1,068)
Exploration costs expensed	**(36)**	(7)
Impairment of trade receivables (note 18)	**(222)**	(269)
Foreign exchange gains	**–**	1
Other costs associated with upstream businesses	**(175)**	(137)
Other costs associated with downstream businesses	**(896)**	(937)
Total operating costs before exceptional items and certain re-measurements	**(2,750)**	(2,641)
Exceptional items and certain re-measurements (note 7)	**(110)**	(181)
Total operating costs	**(2,860)**	(2,822)

6. DIRECTORS AND EMPLOYEES

(a) Employee costs [(i)]	2011 £m	2010 £m
Wages and salaries	**(1,562)**	(1,345)
Social security costs	**(137)**	(115)
Pension and other post-employment benefits costs	**(129)**	(134)
Share scheme costs	**(40)**	(48)
	(1,868)	(1,642)
Capitalised employee costs	**8**	9
Employee costs recognised in the Group Income Statement	**(1,860)**	(1,633)

(i) Details of Directors' remuneration, share-based payments and pension entitlements in the Remuneration Report on pages 52 to 63 form part of these Financial Statements. Details of employee share-based payments are given in note 32. Details of the remuneration of key management personnel are given in note 35.

(b) Average number of employees during the year	2011 Number	2010 Number
Downstream UK	**31,278**	27,298
Upstream UK	**1,658**	1,556
Storage UK	**290**	255
North America	**6,206**	5,534
European operations (note 31)	**–**	327
	39,432	34,970

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

7. EXCEPTIONAL ITEMS AND CERTAIN RE-MEASUREMENTS

(a) Exceptional items for the year ended 31 December

	2011 £m	2010 £m
Continuing operations:		
Provision for European onerous capacity contracts (i)	**(221)**	–
Provision for North American and UK onerous commodity contracts	**–**	(102)
Exceptional items from continuing operations included within gross profit	**(221)**	(102)
Impairments:		
Impairment of UK generation assets (ii)	**(226)**	(68)
Impairment of North American and UK exploration and production assets	**–**	(95)
	(226)	(163)
Downstream UK contract migration (iii)	**(63)**	(43)
Restructuring charges (iv)	**(154)**	–
Profit on disposal of investments	**–**	25
Pension curtailment (note 29)	**333**	–
	(110)	(181)
Exceptional items from continuing operations included within Group operating profit	**(331)**	(283)
Taxation on exceptional items (note 9)	**69**	118
Effect of change in UK supplementary tax charge (note 9)	**(204)**	–
Net exceptional items from continuing operations after taxation	**(466)**	(165)
Discontinued operations:		
Loss on disposal of Oxxio B.V. after taxation (note 31)	**(56)**	–
Total exceptional items after taxation	**(522)**	(165)

(b) Certain re-measurements for the year ended 31 December

	2011 £m	2010 £m
Continuing operations:		
Certain re-measurements recognised in relation to energy contracts:		
Net gains arising on delivery of contracts (v)	**200**	1,023
Net (losses)/gains arising on market price movements and new contracts (vi)	**(632)**	130
Net (losses)/gains arising on positions in relation to cross-border transportation or capacity contracts	**(5)**	24
Net re-measurements from continuing operations included within gross profit	**(437)**	1,177
Net losses arising on re-measurement of associates' energy contracts (net of taxation) (vii)	**(26)**	(14)
Net re-measurements included within Group operating profit	**(463)**	1,163
Taxation on certain re-measurements (note 9)	**119**	(339)
Net re-measurements from continuing operations after taxation	**(344)**	824
Discontinued operations:		
Net re-measurements on energy contracts of discontinued operations after taxation (note 31)	**22**	67
Total re-measurements after taxation	**(322)**	891

(i) As a result of the decision to withdraw from Europe the Group recorded onerous contract charges of £111 million for a number of European gas transportation capacity contracts and a further £110 million for the fixed price Rijnmond tolling contract due to the impact of low market spark spreads.
(ii) Impairment charges have been recognised on a number of UK generation assets (including PP&E and inventory) as a result of low spark spreads, which led to the impairment of Killingholme, proposed closure of Barry and Kings Lynn and the operational reconfiguration of Brigg, Peterborough and Roosecote.
(iii) Exceptional charges have been recorded following the termination in December 2010 and subsequent migration of a significant supplier contract.
(iv) Relates to a Group-wide cost reduction programme leading to staff redundancies. See Business Review for more details.
(v) As energy is delivered or consumed from previously contracted positions the related fair value recognised in the opening balance sheet (representing the discounted difference between forward energy prices at the opening balance sheet date and the contract price of energy to be delivered) is charged or credited to the Income Statement.
(vi) Represents fair value (losses)/gains arising from the change in fair value of future contracted sales and purchase contracts as a result of changes in forward energy prices between reporting dates (or date of inception and the reporting date, where later).
(vii) Includes fair value unwinds relating to the recognition of energy procurement contracts and energy sales contracts at their acquisition-date fair values.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

8. NET INTEREST

Year ended 31 December	Interest expense £m 2011	Interest income £m 2011	Total £m 2011	Interest expense £m 2010	Interest income £m 2010	Total £m 2010
Continuing operations:						
Cost of servicing net debt:						
Interest income	**–**	**37**	**37**	–	30	30
Interest expense on bonds, bank loans and overdrafts (i)	**(176)**	**–**	**(176)**	(284)	–	(284)
Interest expense on finance leases	**(19)**	**–**	**(19)**	(21)	–	(21)
	(195)	**37**	**(158)**	(305)	30	(275)
(Losses)/gains on revaluation:						
(Losses)/gains on fair value hedges	**(83)**	**72**	**(11)**	(47)	47	–
Fair value (losses)/gains on other derivatives (ii)	**(71)**	**35**	**(36)**	(121)	9	(112)
Fair value gains on other securities measured at fair value	**–**	**14**	**14**	–	10	10
Net foreign exchange translation of monetary assets and liabilities (iii)	**–**	**19**	**19**	–	85	85
	(154)	**140**	**(14)**	(168)	151	(17)
Notional interest arising from discounting and other interest (iv)	**(55)**	**35**	**(20)**	(43)	33	(10)
	(404)	**212**	**(192)**	(516)	214	(302)
Capitalised borrowing costs (v)	**46**	**–**	**46**	37	–	37
Interest (expense)/income	**(358)**	**212**	**(146)**	(479)	214	(265)

(i) During December 2010 Centrica reduced its outstanding bond debt principal by £151 million and €383 million.
(ii) Primarily reflects changes in the fair value of derivatives used to hedge the foreign exchange exposure associated with inter-company loans denominated in foreign currencies.
(iii) Primarily reflects foreign exchange gains on loans denominated in foreign currencies.
(iv) Other interest includes interest received for cash collateral balances and interest on supplier early payment arrangements.
(v) Borrowing costs have been capitalised using an average rate of 4.94% (2010: 4.78%).

9. TAXATION

(a) Analysis of tax charge for the year	Business performance £m 2011	Exceptional items and certain re-measurements £m 2011	Results for the year £m 2011	Business performance £m 2010	Exceptional items and certain re-measurements £m 2010	Results for the year £m 2010
Current tax						
UK corporation tax	**(529)**	**69**	**(460)**	(464)	23	(441)
UK petroleum revenue tax	**(220)**	**–**	**(220)**	(223)	–	(223)
Foreign tax	**(107)**	**10**	**(97)**	(15)	(6)	(21)
Adjustments in respect of prior years	**23**	**–**	**23**	171	–	171
Total current tax	**(833)**	**79**	**(754)**	(531)	17	(514)
Deferred tax						
Current year	**(40)**	**90**	**50**	(81)	(235)	(316)
UK petroleum revenue tax	**46**	**–**	**46**	7	–	7
Foreign deferred tax	**(24)**	**17**	**(7)**	(39)	7	(32)
Change in tax rates	**30**	**(201)**	**(171)**	15	(1)	14
Adjustments in respect of prior years	**11**	**(1)**	**10**	(79)	(9)	(88)
Total deferred tax	**23**	**(95)**	**(72)**	(177)	(238)	(415)
Total tax on profit from continuing operations (i)	**(810)**	**(16)**	**(826)**	(708)	(221)	(929)

(i) Total tax on profit from continuing operations excludes taxation on the Group's share of profits in joint ventures and associates.

Tax on items taken directly to equity is disclosed in notes 27 and 28. The Group earns its profits primarily in the UK, therefore the tax rate used for tax on profit from ordinary activities is the standard rate for UK corporation tax, which from 1 April 2011 was 26% (2010: 28%), with the exception of upstream profits, which were taxed at a UK corporation tax rate of 30% (2010: 30%) plus a supplementary charge. From 29 March 2011, the supplementary charge was increased to 32% (2010: 20%). Also announced in March 2011, was an intention to restrict from 2012, the rate of tax relief on decommissioning costs from the current 62% to 50%. If enacted, a one-off charge of approximately £60 million will arise from revaluing the related deferred tax provisions.

Certain upstream assets also bear petroleum revenue tax at 50% (2010: 50%). Taxation for other jurisdictions is calculated at the rates prevailing in those respective jurisdictions.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

9. TAXATION CONTINUED

The UK Government has announced its intention to propose Parliament reduce the main rate of UK corporation tax to 23% by 1 April 2014. At 31 December 2011 a reduction in the rate to 25% had been substantively enacted so the relevant UK deferred tax assets and liabilities included in these Financial Statements have been based on that rate. The effect of the additional proposed reduction in the UK corporation tax rate by 2014 would be to decrease the net deferred tax liability by £11 million.

(b) Factors affecting the tax charge for the year

The differences between the total tax shown above and the amount calculated by applying the standard rate of UK corporation tax to the profit before tax are as follows:

			2011			2010
	Business performance £m	Exceptional items and certain re-measurements £m	Results for the year £m	Business performance £m	Exceptional items and certain re-measurements £m	Results for the year £m
Profit from continuing operations before tax	**2,062**	**(794)**	**1,268**	1,929	880	2,809
Less: share of profits in joint ventures and associates, net of interest and taxation	**(93)**	**26**	**(67)**	(7)	14	7
Group profit from continuing operations before tax	**1,969**	**(768)**	**1,201**	1,922	894	2,816
Tax on profit from continuing operations at standard UK corporation tax rate of 26.5% (2010: 28%)	**(522)**	**204**	**(318)**	(538)	(250)	(788)
Effects of:						
Net expenses not deductible for tax purposes	**(20)**	**–**	**(20)**	(42)	15	(27)
Movement in unrecognised deferred tax assets	**(28)**	**(31)**	**(59)**	(8)	1	(7)
UK petroleum revenue tax rates	**(128)**	**–**	**(128)**	(152)	–	(152)
Overseas tax rates	**(24)**	**15**	**(9)**	(2)	(4)	(6)
Additional charges applicable to upstream profits	**(152)**	**(2)**	**(154)**	(73)	27	(46)
Changes to tax rates	**30**	**(201)**	**(171)**	15	(1)	14
Adjustments in respect of prior years	**34**	**(1)**	**33**	92	(9)	83
Taxation on profit from continuing operations	**(810)**	**(16)**	**(826)**	(708)	(221)	(929)

(c) Factors that may affect future tax charges

Production of gas and oil within the UK continental shelf is subject to several taxes: corporation tax at 30% (2010: 30%) on profits of gas and oil production, a supplementary charge at 32% (2010: 20%) on profits of gas and oil production (adjusted for financing costs) and petroleum revenue tax (PRT) at 50% (2010: 50%) on income generated from certain gas and oil production (net of certain costs).

PRT is a deductible expense for the purposes of corporation tax and the supplementary charge. The effective rate of tax suffered on profits of UK gas production therefore falls between 62% and 81% (2010: 50% and 75%). To the extent that the Group's profits are earned from UK gas and oil production, its effective tax rate will remain above the current UK statutory rate of 26% (2010: 28%).

Income earned in territories outside the UK, notably in the USA and Norway, is generally subject to higher effective rates of tax than the current UK statutory rate. In the medium term, particularly given additional investments being made in Norway, the Group's effective tax rate is expected to remain above the UK statutory rate.

10. DIVIDENDS

			2011			2010
	£m	Pence per share	Date of payment	£m	Pence per share	Date of payment
Prior year final dividend	**540**	**10.46**	**15 Jun 2011**	470	9.14	16 Jun 2010
Interim dividend	**222**	**4.29**	**16 Nov 2011**	198	3.84	17 Nov 2010
	762			668		

The Directors propose a final dividend of 11.11 pence per ordinary share (totalling £575 million) for the year ended 31 December 2011. The dividend will be submitted for formal approval at the Annual General Meeting to be held on 11 May 2012 and, subject to approval, will be paid on 13 June 2012 to those shareholders registered on 27 April 2012.

11. EARNINGS PER ORDINARY SHARE

Basic earnings per ordinary share has been calculated by dividing the earnings attributable to equity holders of the Company for the year of £421 million (2010: £1,935 million) by the weighted average number of ordinary shares in issue during the year of 5,159 million (2010: 5,146 million). The number of shares excludes seven million ordinary shares (2010: six million), being the weighted average number of the Company's own shares held in the employee share trust which are treated as treasury shares. The Directors believe that the presentation of adjusted basic earnings per ordinary share, being the basic earnings per ordinary share adjusted for certain re-measurements, exceptional items and the impact of Strategic Investments, assists with understanding the underlying performance of the Group, as explained in note 2.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

11. EARNINGS PER ORDINARY SHARE CONTINUED

The reconciliation of basic to adjusted basic earnings per ordinary share is as follows:

Year ended 31 December		2011		2010
(a) Continuing and discontinued operations	**£m**	**Pence per ordinary share**	£m	Pence per ordinary share
Earnings – basic	**421**	**8.2**	1,935	37.6
Net exceptional items after taxation (notes 2 and 7)	**522**	**10.1**	165	3.2
Certain re-measurement losses/(gains) after taxation (notes 2 and 7)	**322**	**6.2**	(891)	(17.3)
Depreciation of fair value uplifts to property, plant and equipment from Strategic Investments, after taxation	**68**	**1.3**	88	1.7
Earnings – adjusted basic	**1,333**	**25.8**	1,297	25.2
Earnings – diluted	**421**	**8.1**	1,935	37.3
Earnings – adjusted diluted	**1,333**	**25.6**	1,297	25.0

Strategic Investments

During 2009, the Group acquired a 20% interest in British Energy and the entire share capital of Venture. As explained in note 2, the depreciation relating to fair value uplifts of the acquired Venture PP&E and associated taxation is excluded in arriving at adjusted earnings for the year, which amounted to £64 million (2010: £60 million) depreciation and a taxation credit of £37 million (2010: £30 million) in the period. Additionally, the impact of depreciation arising on fair value uplifts attributed to the British Energy nuclear power stations and related taxation included within the Group's share of the post-taxation results of the associate is excluded in arriving at adjusted earnings for the period, which amounted to £41 million (2010: £58 million) net of taxation.

Year ended 31 December		2011		2010
(b) Continuing operations	**£m**	**Pence per ordinary share**	£m	Pence per ordinary share
Earnings – basic	**442**	**8.6**	1,873	36.4
Net exceptional items after taxation (notes 2 and 7)	**466**	**9.0**	165	3.2
Certain re-measurement losses/(gains) after taxation (notes 2 and 7)	**344**	**6.7**	(824)	(16.0)
Depreciation of fair value uplifts to property, plant and equipment from Strategic Investments, after taxation	**68**	**1.3**	88	1.7
Earnings – adjusted basic	**1,320**	**25.6**	1,302	25.3
Earnings – diluted	**442**	**8.5**	1,873	36.1
Earnings – adjusted diluted	**1,320**	**25.4**	1,302	25.1

Year ended 31 December		2011		2010
(c) Discontinued operations	**£m**	**Pence per ordinary share**	£m	Pence per ordinary share
(Loss)/earnings – basic and diluted	**(21)**	**(0.4)**	62	1.2

Certain re-measurements (notes 2 and 7) included within operating profit and discontinued operations comprise re-measurements arising on energy procurement activities and re-measurements of proprietary trades in relation to cross-border transportation or capacity contracts. All other re-measurements are included within results before exceptional items and certain re-measurements.

In addition to basic and adjusted basic earnings per ordinary share, information is presented for diluted and adjusted diluted earnings per ordinary share. Under this presentation, no adjustments are made to the reported earnings for either 2011 or 2010, however the weighted average number of shares used as the denominator is adjusted for potentially dilutive ordinary shares.

(d) Weighted average number of shares	**2011 Million shares**	2010 Million shares
Weighted average number of shares used in the calculation of basic earnings per ordinary share	**5,159**	5,146
Dilutive impact of share-based payment schemes	**44**	45
Weighted average number of shares used in the calculation of diluted earnings per ordinary share	**5,203**	5,191

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NOTES TO THE FINANCIAL STATEMENTS CONTINUED

12. SOURCES OF FINANCE

The Group funds its business using a combination of debt and shareholders' equity.

31 December	2011 £m	2010 £m
Net debt	**3,435**	3,312
Shareholders' equity	**5,600**	5,819
Capital	**9,035**	9,131

The Group seeks to maintain an efficient capital structure with a balance of debt and equity. Debt levels are restricted to limit the risk of financial distress and, in particular, to maintain strong credit ratings. The Group's credit ratings are important for several reasons, to:

- maintain a low cost of debt;
- limit collateral requirements in energy trading, hedging and decommissioning security arrangements; and
- ensure the Group is an attractive counterparty to energy producers and long term customers.

At 31 December 2011, the Group's long-term credit rating was A3 stable outlook for Moody's Investor Services Limited and A– stable outlook for Standard & Poor's Credit Market Services Europe Limited. These ratings did not change during 2011.

The Group monitors its current and projected capital position on a regular basis, considering a medium-term view of three to five years, and different stress case scenarios, including the impact of changes in the Group's credit ratings and significant movements in commodity prices. A number of financial ratios are monitored, including those used by the credit rating agencies, such as debt to cash flow ratios and EBITDA to gross interest expense. At 31 December 2011, the ratio of the Group's net debt to EBITDA was 1.1 (2010: 1.0). EBITDA to gross interest expense for the year ended 31 December 2011 was 8.7 (2010: 6.7).

British Gas Insurance Limited (BGIL) is required under FSA regulations to hold a minimum capital amount and has complied with this requirement in 2011 (and 2010). For the remainder of the Group, the level of debt that can be raised is restricted by the Company's Articles of Association. Net debt is limited to the greater of £5.0 billion and a gearing ratio of three times adjusted capital and reserves. Based on adjusted capital and reserves as at 31 December 2011 of £5.6 billion, the limit for net debt was £16.8 billion. The Group funds its debt principally through issuing bonds. In addition the Group also maintains substantial committed facilities from banks (see note 25), but generally uses these to provide backup liquidity and does not typically draw on them.

(a) Net debt summary

	2011 £m	2010 £m
Cash at bank, in transit and in hand	**94**	114
Short-term deposits	**424**	353
Cash and cash equivalents (i)	**518**	467
Securities – current (ii)	**28**	23
Securities – non-current (ii)	**190**	234
Current and non-current borrowings	**(4,171)**	(4,036)
Net debt at the end of the year	**(3,435)**	(3,312)

(i) Cash and cash equivalents includes £262 million (2010: £206 million) mostly held by the Group's insurance subsidiary undertakings that is not readily available to be used for other purposes within the Group.
(ii) Securities balances include £91 million of available for sale financial assets (2010: £93 million).

(b) Borrowings summary

	Coupon rate %	Principal m	2011 Current £m	2011 Non-current £m	2011 Total £m	2010 Current £m	2010 Non-current £m	2010 Total £m
Bank overdrafts and loans			**69**	**198**	**267**	52	225	277
Bonds (by maturity date):								
2 November 2012	5.875	£284	**291**	**–**	**291**	–	296	296
27 February 2013	1.045	¥3,000	**–**	**26**	**26**	–	25	25
9 December 2013	7.125	€367	**–**	**317**	**317**	–	326	326
4 November 2014	Floating	$100	**–**	**64**	**64**	–	64	64
10 December 2014	5.125	£315	**–**	**335**	**335**	–	329	329
31 March 2015	Floating	$70	**–**	**45**	**45**	–	45	45
24 October 2016	5.500	£300	**–**	**336**	**336**	–	320	320
19 September 2018	7.000	£400	**–**	**473**	**473**	–	444	444
10 March 2022	6.375	£500	**–**	**527**	**527**	–	527	527
4 September 2026	6.400	£200	**–**	**224**	**224**	–	209	209
16 April 2027	5.900	$70	**–**	**45**	**45**	–	45	45
19 September 2033	7.000	£770	**–**	**777**	**777**	–	777	777
			291	**3,169**	**3,460**	–	3,407	3,407
Commercial paper			**114**	**–**	**114**	–	–	–
Obligations under finance leases			**28**	**302**	**330**	25	327	352
			502	**3,669**	**4,171**	77	3,959	4,036

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

13. NOTES TO THE GROUP CASH FLOW STATEMENT

(a) Reconciliation of Group operating profit to cash generated from continuing operations

	2011 £m	2010 (restated) (i) £m
Continuing operations		
Group operating profit including share of result of joint ventures and associates	**1,414**	3,074
Less share of (profit)/loss of joint ventures and associates	**(67)**	7
Group operating profit before share of results of joint ventures and associates	**1,347**	3,081
Add back/(deduct):		
Amortisation and write-down of intangible assets	**140**	176
Depreciation and write-down of property, plant and equipment	**1,055**	973
Recycling of write-down of available-for-sale financial assets (ii)	**23**	4
Loss/(profit) on sale of businesses, property, plant and equipment and other intangible assets	**5**	(22)
Increase in provisions	**395**	159
Net pension curtailment (gain)/loss	**(332)**	14
Pension service cost	**118**	115
Pension contributions	**(130)**	(441)
Employee share scheme costs	**40**	48
Re-measurement of energy contracts (iii)	**404**	(1,097)
Operating cash flows before movements in working capital	**3,065**	3,010
(Increase)/decrease in inventories	**(79)**	31
Decrease in trade and other receivables (iv)	**201**	162
Increase/(decrease) in trade and other payables (i) (iv)	**42**	(13)
Cash generated from continuing operations	**3,229**	3,190

(i) The 2010 comparatives have been restated for a change in presentation of emission certificate/allowance cash flows, see note 1(d).
(ii) The 2010 comparative of £4 million is impairment of joint ventures and associates.
(iii) Adds back unrealised losses/(gains) arising from re-measurement of energy contracts.
(iv) Includes net outflow of £26 million of cash collateral in 2011 (2010: net inflow of £466 million).

(b) Reconciliation of net increase in cash and cash equivalents to movement in net debt

	2011 £m	2010 £m
Net increase/(decrease) in cash and cash equivalents	**30**	(833)
Increase in cash and cash equivalents of disposal groups classified as held for sale	**–**	16
	30	(817)
Add back/(deduct):		
Net (sale)/purchase of securities	**(48)**	56
Cash inflow from additional debt	**(114)**	(267)
Cash outflow from payment of capital element of finance leases	**25**	23
Cash outflow from repayment of other debt	**30**	928
	(77)	(77)
Revaluation of:		
Securities	**10**	7
Loans and other borrowings	**(59)**	(40)
	(126)	(110)
Increase in interest payable on loans and other borrowings	**(2)**	(2)
Acquisitions	**(3)**	–
Disposals	**–**	(56)
Exchange adjustments	**8**	(8)
Movement in net debt	**(123)**	(176)
Net debt at 1 January	**(3,312)**	(3,136)
Net debt at the end of the year	**(3,435)**	(3,312)

(c) Exploration and evaluation cash flows

Included within the £299 million (2010: £406 million) purchase of intangible assets in investing activities is £85 million (2010: £224 million) relating to exploration and evaluation of oil and gas assets.

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NOTES TO THE FINANCIAL STATEMENTS CONTINUED

13. NOTES TO THE GROUP CASH FLOW STATEMENT CONTINUED

(d) Relationship between current tax charge and taxes paid

	UK £m	North America £m	Other £m	2011 £m	2010 £m
Current tax charge:					
Corporation tax	438	55	41	**534**	291
Petroleum revenue tax	220	–	–	**220**	223
	658	**55**	**41**	**754**	514
Taxes paid:					
Corporation tax	389	42	(1)	**430**	412
Petroleum revenue tax	262	–	–	**262**	128
	651	**42**	**(1)**	**692**	540

Differences between current tax charged and taxes paid arose principally due to the following factors:

- Corporation tax is generally paid, based on estimated profits, partly during the year and partly in the following year. Fluctuations in profits from year to year may therefore give rise to divergence between the charge for the current year and taxes paid; and
- Petroleum revenue tax payments are based on income realised in the preceding period, with subsequent adjustments to reflect actual profits. Variations in production from period to period may therefore lead to temporary differences between tax charged and tax paid.

14. GOODWILL AND OTHER INTANGIBLE ASSETS

(a) Carrying amounts

	2011						2010					
	Goodwill £m	Application software (i) £m	EUAs and ROCs £m	Exploration and evaluation expenditure £m	Other (ii) £m	Total £m	Goodwill £m	Application software (i) £m	EUAs and ROCs £m	Exploration and evaluation expenditure £m	Other (ii) £m	Total £m
Cost												
1 January	2,378	796	186	376	231	**3,967**	2,094	633	188	193	188	3,296
Additions	–	219	216	85	–	**520**	–	177	242	225	–	644
Acquisitions (note 30)	153	4	–	–	129	**286**	219	4	–	42	43	308
Disposals	–	(66)	–	(6)	–	**(72)**	–	(31)	–	(6)	(1)	(38)
Surrenders	–	–	(280)	–	–	**(280)**	–	–	(245)	–	–	(245)
Write-downs	–	–	–	(46)	–	**(46)**	–	–	–	(83)	–	(83)
Transfers (iii)	–	–	–	(100)	(12)	**(112)**	–	2	1	–	–	3
Exchange adjustments	(5)	6	–	(3)	3	**1**	65	11	–	5	1	82
31 December	**2,526**	**959**	**122**	**306**	**351**	**4,264**	2,378	796	186	376	231	3,967
Accumulated amortisation and impairment												
1 January	8	401	16	–	88	**513**	6	352	37	–	79	474
Amortisation	–	74	–	–	14	**88**	–	64	–	–	7	71
Impairments	–	–	3	–	3	**6**	2	4	15	–	1	22
Disposals	–	(66)	–	–	–	**(66)**	–	(29)	–	–	(1)	(30)
Surrenders	–	–	(15)	–	–	**(15)**	–	–	(36)	–	–	(36)
Exchange adjustments	–	(2)	–	–	1	**(1)**	–	10	–	–	2	12
31 December	**8**	**407**	**4**	**–**	**106**	**525**	8	401	16	–	88	513
NBV at 31 December	**2,518**	**552**	**118**	**306**	**245**	**3,739**	2,370	395	170	376	143	3,454

(i) Application software includes assets under construction with a cost of £334 million (2010: £221 million).
(ii) Other mainly includes customer relationships and brands.
(iii) Includes transfers to/from other balance sheet captions, such as intangible to tangible (note 15), and from assets held for sale.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

14. GOODWILL AND OTHER INTANGIBLE ASSETS CONTINUED

(b) Carrying amount of goodwill and intangible assets with indefinite useful lives allocated to CGUs

Goodwill acquired through business combinations and indefinite-lived intangible assets have been allocated for impairment testing purposes to individual or groups of CGUs each representing the lowest level within the Group at which the goodwill or indefinite-lived intangible asset is monitored for internal management purposes as follows:

CGU	Principal acquisitions to which goodwill and intangibles with indefinite useful lives relates	2011 Carrying amount of goodwill £m	2011 Carrying amount of indefinite-lived intangible asset (i) £m	2011 Total £m	2010 Carrying amount of goodwill £m	2010 Carrying amount of indefinite-lived intangible asset (i) £m	2010 Total £m
Downstream UK – Business energy supply and services	Enron Direct/Electricity Direct	**133**	**–**	**133**	133	–	133
Downstream UK – Residential services – Dyno-Rod	Dyno-Rod	**17**	**57**	**74**	17	57	74
Upstream UK – Upstream gas and oil	Newfield/Heimdal/Venture/ Trinidad and Tobago	**997**	**–**	**997**	999	–	999
North America – Residential energy supply	Direct Energy/ATCO/ CPL/WTU/FCP (ii)	**761**	**–**	**761**	643	–	643
North America – Business energy supply	Direct Energy/ATCO/ Strategic Energy	**212**	**–**	**212**	203	–	203
North America – Residential and business services	Enbridge Services/Residential Services Group/Clockwork (ii)	**289**	**9**	**298**	286	9	295
Other	Various (iii)	**109**	**1**	**110**	89	1	90
		2,518	**67**	**2,585**	2,370	67	2,437

(i) The indefinite-lived assets mainly relate to Mr Sparky and Benjamin Franklin brands, acquired as part of the Clockwork business combination and the Dyno-Rod brand.
(ii) Carrying amount of goodwill also contains goodwill from other Direct Energy acquisitions which are not significant compared with the aggregate carrying value of goodwill reported within the CGU.
(iii) Goodwill balances allocated across multiple CGUs. The amount of goodwill allocated to each CGU is not significant compared with the aggregate carrying value of goodwill reported within the Group. This balance also includes £33 million for gas storage.

(c) Key assumptions used

Value in use calculations have been used to determine recoverable amounts for all of the goodwill and indefinite-lived intangible asset balances, with the exception of the impairment test for the Upstream UK – Upstream gas and oil CGU, where fair value less costs to sell has been used as the basis for determining recoverable amount.

Value in use (VIU)

The VIU calculations use pre-tax cash flow projections based on the Group's Board-approved three-year business plans. The Group's business plans are based on past experience, and adjusted to reflect market trends, economic conditions, key risks, the implementation of strategic objectives and changes in commodity prices, as appropriate. Commodity prices used in the planning process are based in part on observable market data and in part on internal estimates. The extent to which the commodity prices used in the business plans are based on observable market data is determined by the extent to which the market for the underlying commodity is judged to be active. Note 24 provides additional detail on the active period of each of the commodity markets in which the Group operates.

(i) Growth rates and discount rates

Cash flows beyond the three-year plan period have been extrapolated using long-term growth rates in the market where the CGU operates. Long-term growth rates are determined using a blend of publicly available historical data and long-term growth rate forecasts published by external analysts. Cash flows are discounted using a discount rate specific to each CGU. Discount rates reflect the current market assessments of the time value of money and are based on the estimated cost of capital of each CGU. Additionally, risks specific to the cash flows of the CGUs are reflected within cash flow forecasts. Each CGU's weighted average cost of capital is then adjusted to reflect the impact of tax in order to calculate an equivalent pre-tax discount rate. Long-term growth rates and pre-tax discount rates used in the VIU calculations for each of the Group's CGUs are provided in the table below:

	Downstream UK – Business energy supply and services	Downstream UK – Residential services	North America – Residential energy supply	North America – Business energy supply	North America – Residential and business services
Growth rate to perpetuity	**2.0%**	**2.0%**	**2.1%**	**2.1%**	**2.1%**
Pre-tax discount rate	**7.5%**	**7.5%**	**8.5%**	**8.5%**	**8.5%**

(ii) Inflation rates

Inflation rates used in the three-year business plan were based on a blend of a number of publicly available inflation forecasts for the UK, Canada and the US. Inflation rates used for the value in use calculations were as follows: UK: 2.0%, Canada: 2.1% and the US: 2.6%.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

14. GOODWILL AND OTHER INTANGIBLE ASSETS CONTINUED

(iii) Key operating assumptions by CGUs using VIU

The key operating assumptions across all CGUs are Gross Margin, Revenues and Operating Costs. Each of these assumptions is tailored to the specific CGU using management's knowledge of the environment.

CGU	Gross margin	Revenues	Operating costs
Downstream UK – Business energy supply and services	**Existing customers:** based on contractual terms. **New customers and renewals:** based on gross margins achieved in the period leading up to date of the business plan. Both adjusted for current market conditions and transportation cost inflation.	**Market share:** percentage immediately prior to business plan. **Adjusted for:** growth forecasts which are based on sales and marketing activity and recent customer acquisitions. Gas and electricity revenues based on forward market prices.	**Wages:** projected headcount in line with expected activity. Salary increases based on inflation expectations. **Credit losses:** historical assumptions regarding provisions have been updated to reflect the current UK environment.
Downstream UK – Residential services – Dyno-Rod	**Future sales:** based on percentages achieved in the period up to the approval of the business plan.	**Market share:** percentage immediately prior to business plan. **Adjusted for:** change in growth rates to reflect the current economic environment in the UK.	**Wages:** projected headcount in line with expected efficiency program.
North America – Residential energy supply	**Existing customers:** based on contractual terms. **New customers and renewals:** based on gross margins achieved in the period leading up to date of the business plan. **Adjusted for:** competitor data. Regulated gross margin percentages are based on regulatory applications submitted to the Alberta Utilities Commission in Canada.	**Market share:** average percentage immediately prior to business plan. **Adjusted for**: expectations of growth or decline to reflect regulatory or competitive differences. This includes a decline in Ontario revenues as a result of the challenging regulatory environment.	**Wages:** projected headcount in line with expected activity. Salary increases based on inflation expectations. **Future developments**: slight reduction in costs to reflect planned business processes efficiencies. **Customer acquisition**: based on experience of costs required to support acquisition, renewal and other servicing activities.
North America – Business energy supply	**Existing customers:** based on contractual terms. **New customers and renewals**: based on gross margins achieved historically.	**Market share:** based on historical growth trends and planned sales activities by individual market sector. **Adjusted for:** prices based on contractual terms for fixed price contracts and forward market curves for both gas and electricity in Canada and the US.	**Wages:** projected headcount in line with expected activity. Salary increases based on inflation expectations. **Future developments:** reduction in costs to reflect expected savings.
North America – Residential and business services	**New customers and renewals**: based on gross margins achieved in the period leading up to date of the business plan. **Adjusted for:** current economic conditions including lower Canadian consumer confidence and weak housing markets in Canada and the US.	**Market share:** based on historical growth trends by individual market sector. **Adjusted for:** new product offerings and continued penetration into new markets.	**Wages:** projected headcount in line with expected activity. Salary increases based on inflation expectations. **Credit losses:** historical assumptions regarding provisions have been updated to reflect the current North American environment.

Fair value less costs to sell (FVLCS)

FVLCS is used as the basis for determining the recoverable amount of goodwill allocated to Upstream UK – gas and oil. This methodology is deemed to be more appropriate as it is based on the post-tax cash flows arising from Upstream UK – gas and oil as a whole. This is consistent with the approach taken by management to evaluate the economic value of the underlying assets.

Discount rate and cash-flow assumptions, Upstream UK – Upstream gas and oil

FVLCS is determined by discounting the post-tax cash flows expected to be generated by the gas production and development assets, net of associated selling costs, taking into account those assumptions that market participants would use in estimating fair value. Post-tax cash flows are derived from projected production profiles of each field, taking into account forward prices for gas and liquids over the relevant period. Where forward market prices are not available, prices are determined based on internal model inputs. Note 24 provides additional detail on the active period of each of the commodity markets in which the Group operates. The date of cessation of production depends on the interaction of a number of variables, such as the recoverable quantities of hydrocarbons, production costs, the contractual duration of the licence area and the selling price of the gas and liquids produced. As each field has specific reservoir characteristics and economic circumstances, the post-tax cash flows for each field are computed using individual economic models. Post-tax cash flows used in the FVLCS calculation for the first three years are based on the Group's Board-approved three-year business plans and, thereafter, are based on long-term production and cash flow forecasts.

The future post-tax cash flows are discounted using a post-tax nominal discount rate of 8.5% to determine the FVLCS. The discount rate and inflation rate used in the FVLCS calculation are determined in the same manner as the rates used in the VIU calculations described above, with the exception of the adjustment required to determine an equivalent pre-tax discount rate.

(d) Summary of results

For all of the above CGUs the recoverable amounts exceeded their carrying values at the impairment test date. Reasonably possible changes in the key assumptions listed above would not cause the recoverable amounts of the goodwill balances to be equal to or less than the carrying amounts.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

15. PROPERTY, PLANT AND EQUIPMENT

(a) Carrying amounts	2011 Land and buildings (i) £m	2011 Plant, equipment and vehicles (ii) (iii) £m	2011 Power generation (ii) (iii) (iv) £m	2011 Gas storage and production (ii) (iii) (iv) £m	2011 Total £m	2010 Land and buildings (i) £m	2010 Plant, equipment and vehicles (ii) (iii) £m	2010 Power generation (ii) (iii) (iv) £m	2010 Gas storage and production (ii) (iii) (iv) £m	2010 Total £m
Cost										
1 January	26	369	2,229	9,852	**12,476**	23	389	2,144	8,649	11,205
Additions	–	85	98	529	**712**	2	27	87	401	517
Capitalised borrowing costs (note 8)	–	–	–	46	**46**	–	–	–	37	37
Acquisitions (note 30)	–	10	–	33	**43**	1	5	–	458	464
Prior year acquisition adjustments	–	–	–	–	**–**	–	–	–	(61)	(61)
Disposals	–	(44)	(12)	(2)	**(58)**	–	(67)	(14)	(13)	(94)
Transfers (v)	–	–	5	100	**105**	–	4	–	9	13
Decommissioning liability revisions (note 23)	–	–	(4)	200	**196**	–	–	1	261	262
Exchange adjustments	–	(3)	2	(50)	**(51)**	–	11	11	111	133
31 December	**26**	**417**	**2,318**	**10,708**	**13,469**	26	369	2,229	9,852	12,476
Accumulated depreciation and impairment										
1 January	12	178	743	5,145	**6,078**	11	203	545	4,387	5,146
Charge for the year	1	52	127	654	**834**	1	34	143	638	816
Impairments	–	–	205	16	**221**	–	–	64	93	157
Disposals	–	(39)	(12)	(2)	**(53)**	–	(66)	(11)	(11)	(88)
Exchange adjustments	–	(1)	1	(23)	**(23)**	–	7	2	38	47
31 December	**13**	**190**	**1,064**	**5,790**	**7,057**	12	178	743	5,145	6,078
NBV at 31 December	**13**	**227**	**1,254**	**4,918**	**6,412**	14	191	1,486	4,707	6,398

(i) The NBV of land and buildings comprises freeholds £8 million, long leaseholds £1 million and short leaseholds £4 million (2010: £8 million, £1 million and £5 million respectively).

(ii) Assets in the course of construction are included within the following categories: plant, equipment and vehicles £61 million, power generation £45 million, gas production £996 million and gas storage £156 million (2010: £75 million, £30 million, £781 million and £113 million respectively).

(iii) Assets held under finance leases included in totals above:

	2011 Plant, equipment and vehicles £m	2011 Power generation £m	2011 Gas storage and production £m	2011 Total £m	2010 Plant, equipment and vehicles £m	2010 Power generation £m	2010 Gas storage and production £m	2010 Total £m
Cost at 1 January	2	469	415	**886**	2	469	415	886
Additions	4	–	–	**4**	–	–	–	–
Cost at 31 December	**6**	**469**	**415**	**890**	2	469	415	886
Aggregate depreciation at 1 January	1	173	375	**549**	1	146	365	512
Charge for the year	2	28	5	**35**	–	27	10	37
Aggregate depreciation at 31 December	**3**	**201**	**380**	**584**	1	173	375	549
NBV at 31 December	**3**	**268**	**35**	**306**	1	296	40	337

(iv) The NBV of decommissioning assets included within power generation and gas storage and production assets was £907 million (2010: £804 million).

(v) Transfers to/from other balance sheet accounts, including transfers to inventory or transfers from intangible assets for exploration licences once a field is being developed.

The net book value of assets to which title was restricted at 31 December 2011 was £306 million (2010: £337 million), of which £268 million (2010: £296 million) relate to the Spalding power station finance lease asset. The carrying value of assets pledged as security for liabilities as at 31 December 2011 was £300 million (2010: £300 million).

(b) Impairments for tangible assets

During 2011, impairment charges were recorded as follows:

Upstream UK – Power: £205 million charge within exceptional items (note 7), for the Killingholme, Kings Lynn, Peterborough and Barry power stations, as a result of low spark spreads. The recoverable amount has been determined using value in use calculations, with future cash flows discounted using a pre-tax discount rate of 7.5% (2010: 7.6%). Cash inflows are based on forecast production profiles and forward market prices for power for the active period of the market and internal models thereafter. Cash outflows are based on planned operating and capital expenditure.

Upstream UK – Gas: £13 million charge resulting from impairment of an upstream field.

Storage UK: £3 million charge resulting from a write-off of capitalised costs in relation to a potential storage project.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

16. INTERESTS IN JOINT VENTURES AND ASSOCIATES

(a) Interest in joint ventures and associates

	2011 Investments in joint ventures and associates £m	2011 Shareholder loans £m	2011 **Total £m**	2010 Investments in joint ventures and associates £m	2010 Shareholder loans £m	2010 Total £m
1 January	2,343	164	**2,507**	2,356	66	2,422
Additions	113	115	**228**	66	124	190
Decrease in shareholder loans	–	(10)	**(10)**	–	(26)	(26)
Share of profits/(losses) for the year	67	–	**67**	(7)	–	(7)
Share of reserve movements	(25)	–	**(25)**	15	–	15
Dividends	(147)	–	**(147)**	(83)	–	(83)
Impairments	–	–	**–**	(4)	–	(4)
31 December	**2,351**	**269**	**2,620**	2,343	164	2,507

(b) Share of joint ventures' and associates' assets and liabilities

The Group's share of joint ventures' and associates' gross assets and gross liabilities at 31 December 2011 principally comprised of its interests in the following entities (all reported in Upstream UK – Power segment):

- Wind farms – Braes of Doune Wind Farm (Scotland) Limited, Barrow Offshore Wind Limited, GLID Wind Farms TopCo Limited(i) and Lincs Wind Farm Limited
- Nuclear – Lake Acquisitions Limited (British Energy) and NNB Holding Company Limited

	Joint ventures Wind farms £m	Associates Nuclear £m	Other (ii) £m	2011 **Total £m**	2010 Total £m
Share of non-current assets	590	3,744	50	**4,384**	4,169
Share of current assets	52	622	2	**676**	698
	642	4,366	52	**5,060**	4,867
Share of current liabilities	(112)	(203)	–	**(315)**	(270)
Share of non-current liabilities	(422)	(1,950)	(13)	**(2,385)**	(2,250)
	(534)	(2,153)	(13)	**(2,700)**	(2,520)
Restricted interest on shareholder loan (iii)	(9)	–	–	**(9)**	(4)
Share of net assets of joint ventures and associates (iv)	99	2,213	39	**2,351**	2,343
Shareholder loans	252	–	17	**269**	164
Interests in joint ventures and associates	**351**	**2,213**	**56**	**2,620**	2,507
Net (debt)/cash included in share of net assets	(376)	105	(12)	**(283)**	(205)

(i) As part of a finance arrangement entered into by GLID Wind Farms TopCo Limited, the Group's shares in GLID Wind Farms TopCo Limited are pledged to a third party. The pledge will only come into force should GLID Wind Farms TopCo Limited default on any of its obligations under the finance arrangement.
(ii) Other includes joint ventures of North Sea Infrastructure Partners Limited, Bacton Storage Company Limited and Secure Electrans Limited.
(iii) The Group restricts the amount of interest receivable on the shareholder loan from Lincs Wind Farm Limited to 50% of the interest capitalised by the joint venture.
(iv) Includes £158 million of assets and £21 million of liabilities of NNB Holding Company Limited (2010: £106 million of assets and £21 million of liabilities).

(c) Share of profits/(losses) in joint ventures and associates

	Joint ventures Wind farms £m	Associates Nuclear £m	Other £m	2011 **Total £m**	2010 Total £m
Income	62	532	–	**594**	468
Expenses excluding certain re-measurements (i)	(26)	(417)	(1)	**(444)**	(422)
Certain re-measurements	–	(33)	–	**(33)**	(31)
	36	82	(1)	**117**	15
Interest paid	(17)	(37)	(4)	**(58)**	(55)
Taxation excluding certain re-measurements (i)	(4)	7	(2)	**1**	16
Taxation on certain re-measurements	–	7	–	**7**	17
Share of post-taxation results of joint ventures and associates	15	59	(7)	**67**	(7)

(i) Includes £86 million (2010: £97 million) relating to depreciation of fair value uplifts to PP&E on acquiring the British Energy investments. The associated tax impact is £45 million credit (2010: £39 million).

British Energy

During November 2009 the Group acquired a 20% interest in British Energy for £2,255 million and NNB Holding Company Limited for £32 million. The Group's share of profit arising from its investment in British Energy for the year to 31 December 2011 as set out in the table above includes the effect of unwinding the fair value adjustments. As explained in note 2 the depreciation, net of taxation, arising

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

16. INTERESTS IN JOINT VENTURES AND ASSOCIATES CONTINUED

on fair value uplifts attributed to the nuclear power stations is reversed in arriving at adjusted profit for the period as shown in the reconciliation table below and as set out in notes 4 and 11.

(d) Reconciliation of share of profits/(losses) in joint ventures and associates to share of adjusted profits/(losses) in joint ventures and associates

	Joint ventures	Associates		2011	2010
	Wind farms £m	Nuclear £m	Other £m	**Total £m**	Total £m
Share of post-taxation results of joint ventures and associates	15	59	(7)	**67**	(7)
Certain re-measurements (net of taxation)	–	26	–	**26**	14
Depreciation – British Energy (net of taxation) (i)	–	41	–	**41**	58
Interest paid	17	37	4	**58**	55
Taxation (excluding certain re-measurements and British Energy depreciation)	4	38	2	**44**	23
Share of adjusted results of joint ventures and associates	36	201	(1)	**236**	143

(i) Relates to depreciation of fair value uplifts to PP&E on acquiring the British Energy investments.

17. INVENTORIES

	2011 £m	2010 £m
Gas in storage and transportation	**243**	120
Other raw materials and consumables	**106**	106
Finished goods and goods for resale	**93**	118
	442	344

The Group consumed £1,229 million of inventories (2010: £1,117 million) during the year. £21 million of inventory write downs in the year relate to power generation spare parts, see note 7.

18. TRADE AND OTHER RECEIVABLES

		2011		2010
	Current £m	**Non-current £m**	Current £m	Non-current £m
Financial assets:				
Trade receivables	**2,066**	**3**	1,995	8
Accrued energy income	**1,709**	**–**	1,813	–
Other accrued income	**193**	**–**	202	–
Cash collateral pledged	**223**	**–**	173	–
Other receivables	**351**	**8**	307	12
	4,542	**11**	4,490	20
Less: Provision for credit losses	**(599)**	**–**	(641)	–
	3,943	**11**	3,849	20
Non-financial assets: Prepayments and other receivables	**269**	**63**	338	77
	4,212	**74**	4,187	97

Trade and other receivables include financial assets representing the contractual right to receive cash or other financial assets from residential customers, business customers and treasury, trading and energy procurement counterparties as follows:

		2011		2010
	Current £m	**Non-current £m**	Current £m	Non-current £m
Financial assets by class:				
Residential customers	**2,042**	**4**	2,001	9
Business customers	**1,562**	**7**	1,643	11
Treasury, trading and energy procurement counterparties	**938**	**–**	846	–
	4,542	**11**	4,490	20
Less: Provision for credit losses	**(599)**	**–**	(641)	–
	3,943	**11**	3,849	20

Receivables from residential and business customers are generally considered to be fully performing until such time as the payment that is due remains outstanding past the contractual due date. Contractual due dates range from being due upon receipt to due in 30 days.

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NOTES TO THE FINANCIAL STATEMENTS CONTINUED

18. TRADE AND OTHER RECEIVABLES CONTINUED

At 31 December 2011, there were £24 million (2010: £25 million) of receivables, net of provisions for credit losses, from residential customers and £22 million (2010: £22 million) from treasury, trading and energy procurement counterparties that were individually impaired. Receivables from residential customers are generally reviewed for impairment on an individual basis once a customer discontinues their relationship with the Group.

The provision for credit losses is based on an incurred loss model and is determined by application of expected default and loss factors, determined by historical loss experience and current sampling to the various balances receivable from residential and business customers on a portfolio basis, in addition to provisions taken against individual accounts. Balances are written off when recoverability is assessed as being remote. Movements in the provision for credit losses by class are as follows:

				2011				2010
	Residential customers £m	Business customers £m	Treasury, trading and energy procurement counterparties £m	**Total £m**	Residential customers £m	Business customers £m	Treasury, trading and energy procurement counterparties £m	Total £m
1 January	(375)	(253)	(13)	**(641)**	(362)	(180)	(12)	(554)
Impairment of trade receivables	(120)	(102)	–	**(222)**	(142)	(124)	(1)	(267)
Receivables written off	146	129	–	**275**	132	53	1	186
Acquisitions	(11)	–	–	**(11)**	(1)	(1)	–	(2)
Exchange adjustments	–	–	–	**–**	(2)	(1)	(1)	(4)
31 December	**(360)**	**(226)**	**(13)**	**(599)**	(375)	(253)	(13)	(641)

The impairment charge in trade receivables is stated net of credits for the release of specific provisions made in previous years, which are no longer required. These relate primarily to residential customers in the UK. During the year the Group took possession of £32 million of customer deposits when customers defaulted on their accounts receivable balance. At 31 December 2011 the Group held £50 million (2010: £56 million) of customer deposits for the purposes of mitigating the credit risk associated with receivables from residential and business customers.

19. DERIVATIVE FINANCIAL INSTRUMENTS

Derivative financial instruments are held for the following purposes and accounted for accordingly:

Purpose	Accounting treatment
Proprietary energy trading and treasury management	Carried at fair value with changes in fair value recognised in the Group's results for the year before exceptional items and certain re-measurements (i)
Energy procurement	Carried at fair value, with changes in the fair value reflected in certain re-measurements (ii)

(i) With the exception of certain energy derivatives related to cross-border transportation and capacity contracts (note S2)
(ii) Energy contracts designated at fair value through profit and loss include certain energy contracts that the Group has, at its option, designated at fair value through profit and loss under IAS 39 because the energy contract contains one or more embedded derivatives that significantly modify the cash flows under the contract (note S2).

In cases where a derivative qualifies for hedge accounting, derivatives are classified as fair value hedges, cash flow hedges or hedges of a net investment in a foreign operation. Notes 20 and S2 provide further detail on the Group's hedge accounting.

The carrying values of derivative financial instruments by product type for accounting purposes are as follows:

		2011		2010
	Assets £m	**Liabilities £m**	Assets £m	Liabilities £m
Derivative financial instruments – held for trading under IAS 39:				
Energy derivatives – for procurement	**332**	**(1,390)**	538	(1,022)
Energy derivatives – for proprietary trading	**61**	**(14)**	47	(31)
Interest rate derivatives	**22**	**(79)**	3	(16)
Foreign exchange derivatives	**23**	**(37)**	53	(100)
Energy derivative contracts designated at fair value through profit and loss	**7**	**(46)**	1	(143)
Derivative financial instruments in hedge accounting relationships:				
Energy derivatives	**–**	**(65)**	25	(86)
Interest rate derivatives	**157**	**(7)**	105	–
Foreign exchange derivatives	**3**	**(7)**	18	(5)
Total derivative financial instruments	**605**	**(1,645)**	790	(1,403)
Included within:				
Derivative financial instruments – current	**315**	**(1,140)**	449	(755)
Derivative financial instruments – non-current	**290**	**(505)**	341	(648)

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

19. DERIVATIVE FINANCIAL INSTRUMENTS CONTINUED

The contracts included within energy derivatives are subject to a wide range of detailed specific terms but comprise the following general components, analysed on a net carrying value basis:

	2011 £m	2010 £m
Short-term forward market purchases and sales of gas and electricity:		
UK and Europe	**(458)**	24
North America	**(406)**	(451)
Structured gas purchase contracts	**(91)**	89
Structured gas sales contracts	**(120)**	(176)
Other	**(40)**	(157)
Net total	**(1,115)**	(671)

Net (losses)/gains on derivative financial instruments due to re-measurement	2011 Income Statement £m	2011 Equity £m	2010 Income Statement £m	2010 Equity £m
Financial assets and liabilities measured at fair value:				
Derivative financial instruments – held for proprietary energy trading	**30**	**–**	(51)	–
Derivative financial instruments – held for trading under IAS 39	**(576)**	**–**	1,099	–
Energy contracts designated at fair value through profit and loss	**104**	**–**	36	–
Derivative financial instruments in hedge accounting relationships	**52**	**(56)**	39	260
	(390)	**(56)**	1,123	260

20. HEDGE ACCOUNTING

For the purposes of hedge accounting, hedges are classified as either fair value hedges, cash flow hedges or hedges of net investments in foreign operations. Note S2 details the Group's accounting policies in relation to derivatives qualifying for hedge accounting under IAS 39. The fair values of derivative and primary financial instruments in hedge accounting relationships at 31 December were as follows:

	2011 Assets £m	2011 Liabilities £m	2010 Assets £m	2010 Liabilities £m
Fair value hedges	**153**	**–**	105	–
Cash flow hedges	**7**	**(79)**	43	(91)

Fair value hedges

The Group's fair value hedges consist of interest rate swaps, cross-currency interest rate swaps and forward rate agreements used to protect against changes in the fair value of fixed-rate, long-term debt due to movements in market interest rates. For qualifying fair value hedges, all changes in the fair value of the hedging instrument and in the fair value of the hedged item in relation to the risk being hedged are recognised as income within net interest expense.

Gains or losses arising on fair value hedges at 31 December were as follows:

Gains/(losses)	2011 £m	2010 £m
On hedging instruments	**49**	41
On hedged items attributable to the hedged risk	**(60)**	(41)
	(11)	–

Cash flow hedges

The Group's cash flow hedges consist primarily of:

- physical and financial gas and power purchase contracts used to protect against the variability in future cash flows associated with highly probable forecast purchases of gas and power due to movements in market commodity prices;
- forward foreign exchange contracts used to protect against the variability of functional currency denominated cash flows associated with non-functional currency denominated highly probable forecast transactions; and
- interest rate swaps, cross-currency interest rate swaps and forward rate agreements used to protect against the variability in cash flows associated with floating-rate borrowings due to movements in market interest rates.

Gains and losses are initially recognised in the cash flow hedging reserve in other comprehensive income and are transferred to the Income Statement when the forecast cash flows affect the Income Statement. Note 27 details movements in the cash flow hedging reserve. The ineffective portion of gains and losses on cash flow hedging are recognised immediately in the Income Statement. During 2011, the Group recognised a £3 million gain (2010: £2 million loss) due to cash flow hedge ineffectiveness.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

20. HEDGE ACCOUNTING CONTINUED

Net investment hedges

Historically the Group engaged in net investment hedging (NIH) whereby it would obtain foreign currency debt issued in the same currency as the net investment. In 2009 the Group ceased NIH however the opening balance of the foreign currency translation reserve includes exchange translation differences on borrowings and derivatives classified as NIH under the requirements of IAS 39. These balances will be recycled to the Group Income Statement on disposal of the foreign operation.

21. TRADE AND OTHER PAYABLES

	2011		2010	
	Current £m	**Non-current £m**	Current £m	Non-current £m
Financial liabilities:				
Trade payables	**988**	**–**	1,063	–
Deferred income	**449**	**–**	293	–
Capital creditors	**108**	**–**	169	–
Other payables	**388**	**2**	368	–
Accruals:				
Commodity costs	**719**	**–**	846	–
Transportation, distribution and metering costs	**177**	**–**	163	–
Operating and other accruals	**778**	**–**	676	–
	1,674	**–**	1,685	–
	3,607	**2**	3,578	–
Non-financial liabilities:				
Other payables and accruals	**359**	**11**	329	29
Deferred income	**128**	**20**	152	27
	4,094	**33**	4,059	56

22. DEFERRED TAX LIABILITIES AND ASSETS

The following are the major deferred tax liabilities and assets recognised by the Group and movements thereon during the current and prior reporting periods:

	Accelerated tax depreciation (corporation tax) £m	Other timing differences including losses carried forward £m	Marked to market £m	Net deferred petroleum revenue tax (i) £m	Retirement benefit obligation and other provisions £m	**Total £m**
1 January 2010	(1,829)	417	611	(2)	158	(645)
Change to tax rates	8	4	(1)	–	3	14
Credit/(charge) to income	179	(184)	(331)	(1)	(92)	(429)
Credit/(charge) to equity	–	33	(79)	–	(2)	(48)
Acquisition of subsidiary	(55)	–	–	–	–	(55)
Adjustments to fair value of prior year acquisitions	16	4	–	2	–	22
Exchange and other adjustments	(12)	2	15	7	–	12
31 December 2010	(1,693)	276	215	6	67	**(1,129)**
Change to tax rates	(227)	60	1	–	(5)	**(171)**
(Charge)/credit to income	(103)	156	113	17	(84)	**99**
(Charge)/credit to equity	–	(10)	23	–	(59)	**(46)**
Acquisition of subsidiaries	(3)	–	–	–	–	**(3)**
Exchange and other adjustments	(1)	(23)	3	–	–	**(21)**
31 December 2011	**(2,027)**	**459**	**355**	**23**	**(81)**	**(1,271)**

(i) Petroleum revenue taxation is deductible for corporation tax purposes, hence the deferred petroleum revenue tax amounts include the effect of deferred corporation tax.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

22. DEFERRED TAX LIABILITIES AND ASSETS CONTINUED

Certain deferred tax assets and liabilities have been offset where there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income taxes relate to the same fiscal authority. The following is an analysis of the gross deferred tax balances and associated offsetting balances for financial reporting purposes:

	Assets 2011 £m	Assets 2010 £m	Liabilities 2011 £m	Liabilities 2010 £m
Gross deferred tax balances crystallising within one year	**187**	100	**(354)**	(325)
Gross deferred tax balances crystallising after one year	**993**	973	**(2,097)**	(1,877)
	1,180	1,073	**(2,451)**	(2,202)
Offsetting deferred tax balances	**(945)**	(835)	**945**	835
Net deferred tax balances (after offsetting for financial reporting purposes)	**235**	238	**(1,506)**	(1,367)

At the balance sheet date the Group had certain deductible temporary differences of £454 million (2010: £191 million) available for utilisation against future profits. No deferred tax asset has been recognised in respect of these temporary differences, due to the unpredictability of future profit streams. A significant proportion of these assets may be carried forward indefinitely. At the balance sheet date, no temporary differences existed in respect of the Group's overseas investments (2010: £87 million). The deferred tax liability arising on these temporary differences is estimated to be £nil (2010: £3 million).

23. PROVISIONS FOR OTHER LIABILITIES AND CHARGES

Current provisions for other liabilities and charges	1 January 2011 £m	Acquisitions and disposals £m	Charged in the year £m	Unused and reversed in the year £m	Transferred from non-current £m	Utilised £m	**31 December 2011 £m**
Restructuring costs (i) (ii)	15	–	162	(6)	3	(27)	**147**
Decommissioning costs (iii)	2	–	1	(3)	52	(27)	**25**
Purchase contract loss provision (iv)	124	–	50	(5)	29	(113)	**85**
Other (v)	54	–	63	(6)	5	(65)	**51**
	195	**–**	**276**	**(20)**	**89**	**(232)**	**308**

Non-current provisions for other liabilities and charges	1 January 2011 £m	Acquisitions and disposals £m	Charged in the year £m	Unused and reversed in the year £m	Revisions and additions £m	Transferred to current £m	Exchange adjustments £m	**31 December 2011 £m**
Restructuring costs (i) (ii)	19	–	1	–	–	(3)	–	**17**
Decommissioning costs (iii)	1,401	6	48	–	196	(52)	(8)	**1,591**
Purchase contract loss provision (iv)	71	–	177	–	–	(29)	(2)	**217**
Other (v)	60	–	24	–	–	(5)	(1)	**78**
	1,551	**6**	**250**	**–**	**196**	**(89)**	**(11)**	**1,903**

Included within the above liabilities are the following financial liabilities:

	2011 Current £m	2011 Non-current £m	2010 Current £m	2010 Non-current £m
Financial liabilities:				
Restructuring costs (i) (ii)	**144**	**15**	34	17
Other (v)	**74**	**151**	34	45
	218	**166**	68	62

(i) The brought forward restructuring provisions relate to significant restructuring programmes undertaken to achieve cost reductions across the Group. Included within the closing provision are costs related to surplus properties of £24 million (2010: £28 million) estimated with reference to the expected cost to be incurred to the point of lease termination, including costs for dilapidations and sub-letting. The provisions are expected to be utilised by 2022.
(ii) The amounts charged in the year mainly relate to the exceptional restructuring costs (see note 7). The provisions are expected to be utilised by 2013.
(iii) Provision has been made for the estimated net present cost of decommissioning gas production and storage facilities at the end of their useful lives. The estimate has been based on 2P reserves, price levels and technology at the balance sheet date. The timing of decommissioning payments is dependent on the lives of the facilities but is expected to occur by 2055, with the majority of the provision being utilised between 2020 and 2030. The charge to income includes £40 million of notional interest (2010: £25 million).
(iv) The purchase contract loss provision relates to a number of European gas transportation contracts, the Rijnmond tolling contract and North American wind farm power purchase agreements (see note 7). The majority of the provisions are expected to be utilised by 2018.
(v) Other provisions include UK contract migration costs, National Insurance payable in respect of Long Term Incentive Scheme liabilities, costs for certain long term take-or-pay contracts renegotiated by the Group in prior years and outstanding litigation for a number of items (none of which are individually significant). The provisions are expected to be utilised by 2016.

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NOTES TO THE FINANCIAL STATEMENTS CONTINUED

24. FAIR VALUE OF FINANCIAL INSTRUMENTS

The fair value of a financial instrument is the amount at which the financial instrument could be exchanged in an arm's length transaction between knowledgeable and willing parties under no compulsion to act. The Group has documented internal policies for determining fair value, including methodologies used to establish valuation adjustments required for credit risk.

Financial liabilities	Notes	2011 Carrying value £m	2011 Fair value £m	2010 Carrying value £m	2010 Fair value £m
Financial liabilities measured at amortised cost:					
Trade and other payables	21	**(3,609)**	**(3,609)**	(3,578)	(3,578)
Bank overdrafts, loans and other borrowings:					
Bank overdrafts and loans	12	**(267)**	**(274)**	(277)	(241)
Bonds	12	**(3,460)**	**(3,891)**	(3,407)	(3,693)
Commercial paper	12	**(114)**	**(114)**	–	–
Obligations under finance leases	12	**(330)**	**(328)**	(352)	(364)
Provisions	23	**(384)**	**(384)**	(130)	(130)
		(8,164)	**(8,600)**	(7,744)	(8,006)
Financial liabilities at fair value: Derivative financial instruments	19	**(1,645)**	**(1,645)**	(1,403)	(1,403)

Financial assets

The carrying values of the Group's financial assets (disclosed in notes 12, 18 and 19) are equal to the fair values of those assets.

Bank overdrafts, loans and other borrowings

The fair values of bonds are based on quoted market prices. The fair values of bank loans have been determined by discounting cash flows with reference to relevant market rates of interest. The fair values of overdrafts and commercial paper are assumed to equal their book values due to the short-term nature of these amounts. The fair values of obligations under finance leases have been determined by discounting contractual cash flows with reference to the Group's cost of borrowing.

Other financial instruments

Due to their nature and/or short-term maturity, the fair values of trade and other receivables, cash and cash equivalents, trade and other payables and provisions are estimated to approximate their carrying values.

Derivative financial instruments and energy contracts designated at fair value through profit and loss

The fair values of foreign exchange and interest rate derivatives are determined by reference to closing market rates at the balance sheet date. The fair values of energy derivatives are determined using valuation techniques based in part on observable market data and in part on internal estimates not currently supported by observable market data. The extent to which fair values of energy derivatives are based on observable market data is determined by the extent to which the market for the underlying commodity is judged to be active.

The Group has judged each of the markets in which it operates as active for the purposes of accounting as follows:

Active period of markets	Gas	Power	Coal	Emissions	Oil
UK (years)	**2**	**2**	**3**	**2**	**3**
North America (years)	**5**	**Up to 5**	**n/a**	**Up to 5**	**n/a**

The fair values of energy contracts within the scope of IAS 39 that settle inside the active period of the market are based on quoted market prices and expected volumes, discounted at an average rate of 1% per annum (2010: 1%). The fair values of derivative financial instruments in North America and Europe are based primarily on quoted market prices. In the UK, however, certain energy contracts extend beyond the active period of the market. The fair values of energy contracts that extend beyond the active period of the market are determined by reference in part to published price quotations in active markets and in part by using valuation techniques based on commodity prices derived using assumptions that are based on internal market expectations and expected volumes, discounted using an average discount rate of 2% per annum for 2011.

Where the fair value at initial recognition for such contracts differs from the transaction price, a day-one gain or loss will arise. Such gains and losses are deferred and amortised to the Income Statement based on volumes purchased or delivered over the contractual period until such time as observable market data becomes available (see note S2 for further detail). The amount that has yet to be recognised in the Income Statement relating to the difference between the fair value at initial recognition (the transaction price) and the amount that would have arisen had valuation techniques used for subsequent measurement been applied at initial recognition, less subsequent releases, is as follows:

Net deferred (gains)/losses	2011 £m	2010 £m
1 January	**(109)**	(86)
Net losses/(gains) deferred on new transactions	**7**	(2)
Recognised in the Income Statement during the year	**43**	(21)
31 December	**(59)**	(109)

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

24. FAIR VALUE OF FINANCIAL INSTRUMENTS CONTINUED

Fair value hierarchy

Financial assets and financial liabilities measured at fair value are classified into one of three categories:

	2011 Level 1 £m	2011 Level 2 £m	2011 Level 3 £m	2011 Total £m	2010 Level 1 £m	2010 Level 2 £m	2010 Level 3 £m	2010 Total £m
Financial assets								
Derivative financial instruments:								
Energy derivatives	40	318	42	**400**	–	492	119	611
Interest rate derivatives	–	179	–	**179**	–	108	–	108
Foreign exchange derivatives	–	26	–	**26**	–	71	–	71
Treasury gilts designated at fair value through profit and loss	128	–	–	**128**	164	–	–	164
Debt instruments	69	–	3	**72**	64	–	1	65
Equity instruments	11	–	7	**18**	17	–	11	28
Total financial assets	**248**	**523**	**52**	**823**	245	671	131	1,047
Financial liabilities								
Derivative financial instruments:								
Energy derivatives	(169)	(1,140)	(206)	**(1,515)**	(113)	(849)	(320)	(1,282)
Interest rate derivatives	–	(86)	–	**(86)**	–	(16)	–	(16)
Foreign exchange derivatives	–	(44)	–	**(44)**	–	(105)	–	(105)
Total financial liabilities	**(169)**	**(1,270)**	**(206)**	**(1,645)**	(113)	(970)	(320)	(1,403)

There were no significant transfers out of Level 1 into Level 2 and out of Level 2 into Level 1 during 2011 and 2010.

The reconciliation of the Level 3 fair value measurements during the year is as follows:

	2011 Financial asset £m	2011 Financial liability £m	2010 Financial asset £m	2010 Financial liability £m
Level 3 financial instruments				
1 January	**131**	**(320)**	75	(490)
Total realised and unrealised (losses)/gains:				
Recognised in income statement	**(45)**	**68**	60	(72)
Gains recognised in other comprehensive income	**–**	**(3)**	2	–
Purchases, sales, issuances and settlements (net)	**–**	**–**	38	77
Transfers from Level 3 to Level 2	**(34)**	**49**	(44)	165
31 December	**52**	**(206)**	131	(320)
Total (losses)/gains for the year for Level 3 financial instruments held at the end of the reporting period (i)	**(21)**	**65**	74	(86)

(i) £21 million losses (2010: £72 million gains) for the year for Level 3 financial assets held at the end of the reporting year were recognised within certain re-measurements and no gains or losses (2010: £2 million) were recognised in other comprehensive income. £68 million gains (2010: £86 million losses) for the year for Level 3 financial liabilities held at the end of the reporting year were recognised within certain re-measurements and £3 million losses (2010: £nil) were recognised in other comprehensive income.

The impacts of reasonably possible changes to assumed gas, power, coal, emissions and oil prices on the net fair value of the Group's fair value measurements categorised as Level 3 are as follows:

Energy price	2011 Reasonably possible change in variable	2010 Reasonably possible change in variable
UK gas (p/therm)	**+/–9**	+/–11
UK power (£/MWh)	**+/–6**	+/–5
UK coal (US$/tonne)	**+/–13**	+/–21
UK emissions (€/tonne)	**+/–2**	+/–2
UK oil (US$/bbl)	**+/–20**	+/–18

Increase/(decrease) in fair value	2011 £m	2010 £m
UK energy prices – increase/(decrease)	**52/(38)**	9/12

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

24. FAIR VALUE OF FINANCIAL INSTRUMENTS CONTINUED

The impacts disclosed above result from changing the assumptions used for fair valuing energy contracts in relation to gas, power, emissions, coal and oil prices to reasonably possible alternative assumptions at the balance sheet date. The fair value impacts only concern those contracts entered into which are within the scope of IAS 39 and are marked-to-market based on valuation models using assumptions that are not currently observable in an active market. The sensitivity analysis provided is hypothetical only and should be used with caution, as the impacts provided are not necessarily indicative of the actual impacts that would be experienced because the Group's actual exposure to market rates is constantly changing as the Group's portfolio of energy contracts changes. Changes in fair values based on a variation in a market variable cannot be extrapolated as the relationship between the change in market variable and the change in fair value will not always be linear. This can be seen in the results from the above 2010 sensitivity analysis. Due to the interaction of various contract price floors and ceilings and optionality in purchase/sales volumes, both scenarios lead to an increase in the total fair value of the Level 3 assets and liabilities.

25. FINANCIAL RISK MANAGEMENT

The Group's normal operating, investing and financing activities expose it to a variety of financial risks. The processes for managing these risks are set out in note S3. The information in this note sets out financial metrics related to these risks.

Transactional and translational currency risks

It is the Group's policy to hedge material transactional exposures using forward contracts to fix the functional currency value of non-functional currency cash flows, except where there is an economic hedge inherent in the transaction. At 31 December 2011, there were no material unhedged non-functional currency monetary assets or liabilities, firm commitments or probable forecast transactions (2010: £nil), other than transactions which have an inherent economic hedge and foreign currency borrowings used to hedge translational exposures.

The Group manages translational currency risk taking into consideration the cash impact of any hedging activity as well as the risk to the net asset numbers in the Group's Financial Statements. The translation hedging programme including the potential cash impact is monitored by the GFRMC.

The impacts of reasonably possible changes in foreign currency rates relative to pounds sterling on profit and equity, both after taxation, based on the assumptions set out in note S3 are as follows:

			2011			2010
Foreign exchange rates and incremental profit/(loss)	**Reasonably possible change in variable %**	**Impact on profit £m**	**Impact on equity £m**	Reasonably possible change in variable %	Impact on profit £m	Impact on equity £m
US dollar	**+/–10**	**14/(23)**	**(17)/20**	+/–10	(75)/94	20/(18)
Canadian dollar	**+/–10**	**(18)/20**	**(54)/66**	+/–10	(20)/20	52/(43)
Euro	**+/–10**	**33/(20)**	**19/(23)**	+/–10	(28)/33	(5)/7

Interest rate risk

The impacts of reasonably possible changes in interest rates on profit and equity, both after taxation, based on the assumptions set out in note S3 are as follows:

			2011			2010
Interest rates and incremental profit/(loss)	**Reasonably possible change in variable %**	**Impact on profit £m**	**Impact on equity £m**	Reasonably possible change in variable %	Impact on profit £m	Impact on equity £m
UK interest rates	**+/–1.0**	**6/(4)**	**27/(33)**	+/–1.0	14/(12)	14/(18)
US interest rates	**+/–1.0**	**2/(4)**	**–/–**	+/–1.0	2/(6)	–/–
Euro interest rates	**+/–1.0**	**(4)/5**	**–/–**	+/–1.0	(7)/5	–/–

Commodity price risk

The impacts of reasonably possible changes in commodity prices on profit and equity, both after taxation, based on the assumptions set out in note S3 are as follows:

		2011		2010
Energy prices	**Base price (i)**	**Reasonably possible change in variable**	Base price (i)	Reasonably possible change in variable
UK gas (p/therm)	**59**	**+/– 9**	59	+/–11
UK power (£/MWh)	**47**	**+/– 6**	51	+/–5
UK coal (US$/tonne)	**117**	**+/– 13**	121	+/–21
UK emissions (€/tonne)	**8**	**+/– 2**	14	+/–2
UK oil (US$/bbl)	**101**	**+/– 20**	95	+/–18
North American gas (USc/therm)	**42**	**+/– 6**	52	+/–9
North American power (US$/MWh)	**43**	**+/– 4**	48	+/–4

(i) The base price represents the average forward market price over the duration of the active market curve used in the sensitivity analysis provided.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

25. FINANCIAL RISK MANAGEMENT CONTINUED

Incremental profit/(loss)	2011 Impact on profit £m	2011 Impact on equity £m	2010 Impact on profit £m	2010 Impact on equity £m
UK energy prices (combined) – increase/(decrease)	**245/(235)**	**24/(24)**	98/(79)	32/(32)
North American energy prices (combined) – increase/(decrease)	**56/(56)**	**–/–**	25/(25)	7/(7)

Liquidity risk

The Group has a number of treasury and risk policies to monitor and manage liquidity risk. Cash forecasts identifying the Group's liquidity requirements are produced regularly and are stress-tested for different scenarios, including, but not limited to, reasonably possible increases or decreases in commodity prices and the potential cash implications of a credit rating downgrade. The Group seeks to ensure that sufficient financial headroom exists for at least a 12-month period to safeguard the Group's ability to continue as a going concern. It is the Group's policy to maintain committed facilities and/or available surplus cash resources of at least £1,200 million, raise at least 75% of its net debt (excluding non-recourse debt) in the long-term debt market and to maintain an average term to maturity in the recourse long-term debt portfolio greater than five years.

At 31 December 2011, the Group had undrawn committed credit facilities of £3,254 million (2010: £2,873 million) and £518 million (2010: £467 million) of cash and cash equivalents. These facilities include a £500 million facility to aid the purchase of the Statoil gas and oil assets described in note 37. 115% (2010: 121%) of the Group's net debt has been raised in the long-term debt market and the average term to maturity of the long-term debt portfolio was 9.6 years (2010: 10.5 years).

The Group's liquidity is impacted by the cash pledged under margin/collateral agreements; the table below summarises the movements in margin cash:

	2011 £m	2010 £m
Cash pledged as collateral at 1 January	**(173)**	(631)
Net cash (outflow)/inflow	**(26)**	466
Transferred from discontinued operations	**(2)**	–
Acquisition of businesses	**(17)**	–
Foreign exchange	**(1)**	(8)
Cash pledged as collateral at 31 December (i)	**(219)**	(173)

(i) Within discontinued operations there was also a net £8 million cash inflow of collateral in the period (2010: £25 million outflow). The net cash collateral pledged of £219 million is included in trade payables, £4 million, and trade receivables, £223 million (2010: £173 million).

The relatively high level of undrawn committed bank borrowing facilities and available cash resources has enabled the Directors to conclude that the Group has sufficient headroom to continue as a going concern. The statement of going concern is included in the Directors' Report – Governance, on page 51.

Maturity profiles

Maturities of derivative financial instruments, provisions, finance leases and trade and other payables are provided in the following tables (all amounts are undiscounted):

Due for payment	<1 year £m	1 to 2 years £m	2 to 3 years £m	3 to 4 years £m	4 to 5 years £m	>5 years £m
2011						
Energy and interest derivatives in a loss position that will be settled on a net basis	**(326)**	**(85)**	**(17)**	**(3)**	**(2)**	**(24)**
Gross energy procurement contracts carried at fair value	**(16,174)**	**(7,033)**	**(4,396)**	**(3,552)**	**(2,054)**	**(1,077)**
Foreign exchange derivatives that will be settled on a gross basis:						
Outflow	**(2,920)**	**(699)**	**(36)**	**(19)**	**(2)**	**(319)**
Inflow	**2,921**	**656**	**39**	**17**	**–**	**263**
Financial liabilities within provisions	**(218)**	**(40)**	**(30)**	**(22)**	**(45)**	**(29)**
Finance leases: (i)						
Minimum lease payments	**(46)**	**(46)**	**(47)**	**(48)**	**(48)**	**(187)**
Capital elements of leases	**(28)**	**(33)**	**(32)**	**(35)**	**(38)**	**(164)**

(i) Note the difference between the total minimum lease payments and the total capital elements of leases is due to future finance charges.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

25. FINANCIAL RISK MANAGEMENT CONTINUED

Due for payment	<1 year £m	1 to 2 years £m	2 to 3 years £m	3 to 4 years £m	4 to 5 years £m	>5 years £m
2010						
Energy and interest derivatives in a loss position that will be settled on a net basis	(418)	(33)	(112)	2	1	(14)
Gross energy procurement contracts carried at fair value	(12,814)	(5,839)	(3,867)	(2,919)	(2,574)	(2,184)
Foreign exchange derivatives that will be settled on a gross basis:						
Outflow	(2,350)	(548)	(595)	(11)	–	(244)
Inflow	2,335	556	565	15	–	158
Financial liabilities within provisions	(68)	(16)	(5)	(6)	(28)	(7)
Finance leases: (i)						
Minimum lease payments	(45)	(46)	(46)	(47)	(48)	(235)
Capital elements of leases	(25)	(28)	(30)	(32)	(35)	(202)

(i) Note the difference between the total minimum lease payments and the total capital elements of leases is due to future finance charges.

Financial liabilities within trade and other payables on an undiscounted basis	2011 £m	2010 £m
Less than 90 days	**3,356**	3,214
90 to 182 days	**90**	160
183 to 365 days	**161**	204
	3,607	3,578
Greater than 365 days	**2**	–
	3,609	3,578

Credit risk for financial assets

Credit risk from financial asset transactions is generated by the potential for the counterparty to default on its contractual obligations. 2011 was marked by a continuing shortage of available credit in European energy markets due to general economic conditions and the continuing impact of the European Sovereign debt concerns. The Group does not hold any financial instruments issued by any of Portugal, Ireland, Italy, Greece and Spain governments. Further consolidation of energy market participants in key European markets has also impacted overall market activity. Credit markets in North America have followed suit and have been volatile due to ongoing US economy and European Sovereign debt concerns. The Group continues to be vigilant and manage credit risk in accordance with its risk management policy. Details of how credit risk is managed across the asset categories shown below are included in note S3. Credit risk from financial assets is measured by counterparty credit rating as follows:

	2011			2010		
	Derivative financial instruments with positive fair values £m	Receivables from treasury, trading and energy procurement counterparties £m	Cash and cash equivalents £m	Derivative financial instruments with positive fair values £m	Receivables from treasury, trading and energy procurement counterparties £m	Cash and cash equivalents £m
AAA to AA	**5**	**128**	**411**	26	12	363
AA– to A–	**469**	**408**	**106**	647	334	104
BBB+ to BBB–	**23**	**137**	**–**	42	175	–
BB+ to BB–	**20**	**27**	**1**	2	14	–
B or lower	**3**	**1**	**–**	–	–	–
Unrated (i)	**85**	**237**	**–**	73	311	–
	605	**938**	**518**	790	846	467

(i) The unrated counterparty receivables primarily comprise amounts due from subsidiaries of rated entities, exchanges or clearing houses.

Financial assets within trade and other receivables on an undiscounted basis	2011 £m	2010 £m
Less than 30 days	**564**	365
30 to 89 days	**344**	328
Less than 90 days	**908**	693
90 to 182 days	**121**	142
183 to 365 days	**186**	182
Greater than 365 days	**77**	64
	1,292	1,081

For additional information on financial risk management see note S3.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

26. SHARE CAPITAL

Share capital of the Company

	2011 £m	2010 £m
Allotted and fully paid share capital of the Company		
5,173,244,808 ordinary shares of 6 14/81p each (2010: 5,154,005,553)	**319**	318

The movement in the number of allotted and fully paid shares of the Company for the year was as follows:

	2011 Millions	2010 Millions
1 January	**5,154**	5,132
Issued under employee share schemes (i)	**19**	22
31 December	**5,173**	5,154

(i) Ordinary shares were allotted and issued to satisfy the exercise of share options, share incentive schemes, the Direct Energy Employee Share Purchase Plan and the matching element of the Share Incentive Plan as follows:

	2011	2010
Number of shares (millions)	**19**	22
Nominal value (£million)	**1.2**	1.4
Consideration (£million) (net of issue costs of £nil (2010: £nil))	**23**	31
Service consideration (£million)	**19**	25

The closing price of one Centrica ordinary share on 31 December 2011 was 289.30 pence (2010: 331.60 pence). Centrica employee share ownership trusts purchase Centrica ordinary shares from the open market and receive newly issued shares to satisfy future obligations of certain employee share schemes. During the year, the trusts purchased 0.9 million shares (2010: 2.5 million), received 4.9 million newly allotted shares (2010: 4.2 million) and released 7.0 million shares (2010: 4.1 million) to employees on vesting. At 31 December 2011, the trusts held 7.3 million shares (2010: 8.5 million) at a carrying amount of £19 million (2010: £22 million). Until such time as the Company's own shares held by these trusts vest unconditionally, the amount paid for those shares, or the value they were issued at, are held as treasury shares and are deducted from shareholders' equity.

27. ACCUMULATED OTHER COMPREHENSIVE INCOME/(LOSS)

	2011					2010				
	Available-for-sale reserve (AFS) £m	Cash flow hedging reserve £m	Foreign currency translation reserve £m	Actuarial gains and losses reserve £m	**Total £m**	Available-for-sale reserve (AFS) £m	Cash flow hedging reserve £m	Foreign currency translation reserve £m	Actuarial gains and losses reserve £m	Total £m
1 January	(11)	(56)	91	(343)	**(319)**	(6)	(244)	8	(345)	(587)
Exchange differences on translation of foreign operations	–	(3)	(12)	–	**(15)**	–	(8)	70	(1)	61
Recycling of foreign exchange on disposal of business	–	–	(3)	–	**(3)**	–	9	(1)	–	8
Actuarial gains/(losses) (note 29)	–	–	–	198	**198**	–	–	–	(9)	(9)
Revaluation of available-for-sale securities	(4)	–	–	–	**(4)**	(4)	–	–	–	(4)
Transfer of AFS reserve to income statement	23	–	–	–	**23**	–	–	–	–	–
Cash flow hedges:										
Net fair value (losses)/gains	–	(99)	–	–	**(99)**	–	10	–	–	10
Transferred to income and expense (i)	–	42	–	–	**42**	–	236	–	–	236
Transferred to assets and liabilities	–	2	–	–	**2**	–	19	–	–	19
Share of other comprehensive income of joint ventures and associates	–	(1)	–	(24)	**(25)**	–	1	–	14	15
Taxation on above items	(2)	23	–	(59)	**(38)**	(1)	(79)	14	(2)	(68)
31 December	**6**	**(92)**	**76**	**(228)**	**(238)**	(11)	(56)	91	(343)	(319)

(i) Included within gross profit

Foreign currency translation reserve

The foreign currency translation reserve comprises exchange translation differences on foreign currency net investments. Historically the Group has been hedging its foreign investments and so the opening balance of foreign currency translation reserve includes exchange translation differences on borrowings and derivatives classified as net investment hedges under the requirements of IAS 39.

Cash flow hedging reserve

The cash flow hedging reserve comprises fair value movements on instruments designated as cash flow hedges under the requirements of IAS 39. Note 20 provides further detail on cash flow hedging.

Financial Statements

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

27. ACCUMULATED OTHER COMPREHENSIVE INCOME/(LOSS) CONTINUED

The maturity analysis of amounts included in the cash flow hedging reserve, which includes fair value gains and losses in relation to commodity, interest rate and currency hedges, is as follows:

	2011 £m	2010 £m
Within one year	**(57)**	(38)
Between one and five years	**(13)**	(6)
After five years	**(22)**	(12)
	(92)	(56)

The maturity profile reflects the timing of expected transfers from the cash flow hedging reserve to the Income Statement as and when the hedged item affects the Income Statement which is, for the most part, on delivery of physical volumes for energy contracts and the accrual of interest for debt contracts.

28. OTHER EQUITY

	2011					2010				
	Revaluation reserve £m	Treasury shares reserve £m	Share-based payments reserve £m	Merger and capital redemption reserve £m	**Total £m**	Revaluation reserve £m	Treasury shares reserve £m	Share-based payments reserve £m	Merger and capital redemption reserve £m	Total £m
1 January	27	(22)	113	483	**601**	26	(15)	87	483	581
Employee share schemes:										
Increase in treasury shares	–	(19)	–	–	**(19)**	–	(20)	–	–	(20)
Exercise of awards	–	22	(33)	–	**(11)**	–	13	(44)	–	(31)
Value of services provided	–	–	40	–	**40**	–	–	48	–	48
Taxation on above items	–	–	(8)	–	**(8)**	–	–	20	–	20
Exchange adjustments	(1)	–	–	–	**(1)**	1	–	2	–	3
31 December	**26**	**(19)**	**112**	**483**	**602**	27	(22)	113	483	601

For additional explanation of the reserves that are included in the above table, see note S4.

29. PENSIONS

(a) Summary of main defined benefit schemes

Name of scheme	Section	Status	Funding/tax status	Country
Centrica Engineers Pension Scheme	Final salary section Career average section	Closed to new members Open to new members	Funded/tax-registered Funded/tax-registered	UK UK
Centrica Pension Plan	Management section 2008 section	Closed to new members Closed to new members	Funded/tax-registered Funded/tax-registered	UK UK
Centrica Pension Scheme	Final salary section Career average section	Closed to new members Closed to new members	Funded/tax-registered Funded/tax-registered	UK UK
Centrica Unapproved Pension Scheme		Closed to new members	Unfunded/non-registered	UK
Direct Energy Marketing Ltd pension plan		Closed to new members	Funded/tax-registered	Canada

The Centrica Pension Scheme also has a defined contribution section which is open to new members.

The Centrica Engineers Pension Scheme (CEPS), Centrica Pension Plan (CPP) and Centrica Pension Scheme form the majority of the Group's defined benefit obligation and are referred to below as the 'Registered Pension Schemes'.

For additional background information to the Group's pension schemes, see note S6.

(b) 2011 curtailment gain

During the year, the Company announced changes to the terms of the final salary sections of the CEPS and the CPP with the changes taking effect from 1 January 2012 and 1 March 2012 respectively. Employees' annual increases in pensionable pay will be capped to 2% and annual increases in respect of future years' service for pensions in deferment will be the lower of CPI and 2.5%. Following agreement of the changes in October 2011 (for CEPS) and December 2011 (for CPP) with the trade unions and the trustees, the Company has recognised exceptional curtailment gains of £333 million, as disclosed in note 7.

The other final salary defined benefit obligations in the UK are within the Centrica Pension Scheme and the Centrica Unapproved Pension Scheme, which have a combined active membership of approximately 100 employees.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

29. PENSIONS CONTINUED

(c) Accounting assumptions

The accounting assumptions for the Registered Pension Schemes are given below.

Major assumptions used for the actuarial valuation	31 December 2011 %	31 December 2010 %
Rate of increase in employee earnings:		
Subject to cap	**2.0**	n/a
Other	**4.3**	4.7
Rate of increase in pensions in payment	**3.3**	3.7
Rate of increase in deferred pensions:		
In line with CPI capped at 2.5%	**2.3**	n/a
In line with RPI	**3.3**	3.7
Discount rate	**5.4**	5.7

The assumptions relating to longevity underlying the pension liabilities at the balance sheet date have been based on a combination of standard actuarial mortality tables, scheme experience and other relevant data, and include a medium cohort allowance, as published by the Institute and Faculty of Actuaries, with an underpin. The longevity assumptions for members in normal health are as follows:

Life expectancy at age 65 for a member	2011 Male Years	2011 Female Years	2010 Male Years	2010 Female Years
Currently aged 65	**22.7**	**24.0**	22.6	24.0
Currently aged 45	**24.5**	**25.4**	24.4	25.3

At 31 March 2009, the date of the most recent actuarial review, the schemes had approximately 34,900 members and beneficiaries. The other demographic assumptions have been set having regard to the latest trends in scheme experience and other relevant data. The assumptions are reviewed and updated as necessary as part of the periodic actuarial valuation of the pension schemes.

Impact of changing material assumptions	2011 Increase/ decrease in assumption	2011 Indicative effect on scheme liabilities %	2010 Increase/ decrease in assumption	2010 Indicative effect on scheme liabilities %
Rate of increase in employee earnings	**0.25%**	**nil**	0.25%	+/–1
Rate of increase in pensions in payment and deferred pensions	**0.25%**	**+/–5**	0.25%	+/–5
Discount rate	**0.25%**	**–/+6**	0.25%	–/+6
Inflation assumption	**0.25%**	**+/–5**	0.25%	+/–6
Longevity assumption	**1 year**	**+/–2**	1 year	+/–2

The remaining disclosures in this note cover all of the Group's defined benefit schemes.

(d) Amounts included in the Group Balance Sheet

	2011 £m	2010 £m
Fair value of plan assets	**4,670**	4,335
Present value of defined benefit obligation	**(4,340)**	(4,574)
Net asset/(liability) recognised in the Balance Sheet	**330**	(239)
Associated deferred tax (liability)/asset recognised in the Balance Sheet	**(81)**	67
Net pension asset/(liability) after deferred tax	**249**	(172)
Pension asset/(liability) presented in the Balance Sheet as:		
Retirement benefit assets	**413**	–
Retirement benefit liabilities	**(83)**	(239)
Net pension asset/(liability)	**330**	(239)

Financial Statements

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

29. PENSIONS CONTINUED

(e) Movement in the year

	Pension liabilities 2011 £m	Pension liabilities 2010 £m	Pension assets 2011 £m	Pension assets 2010 £m
1 January	**(4,574)**	(4,098)	**4,335**	3,533
Items included in the Group Income Statement:				
Current service cost	**(118)**	(115)	**–**	–
Loss on curtailment	**(1)**	(14)	**–**	–
Exceptional gains on curtailment	**333**	–	**–**	–
Interest on scheme liabilities	**(258)**	(249)	**–**	–
Expected return on scheme assets	**–**	–	**285**	275
Items included in Other Comprehensive Income:				
Actuarial gain/(loss)	**198**	(163)	**–**	154
Exchange adjustments	**1**	(7)	**(1)**	3
Items included in the Group Cash Flow Statement:				
Employer contributions	**–**	–	**130**	441
Other movements:				
Plan participants' contributions	**(29)**	(33)	**29**	33
Benefits paid from schemes	**108**	105	**(108)**	(104)
31 December	**(4,340)**	(4,574)	**4,670**	4,335

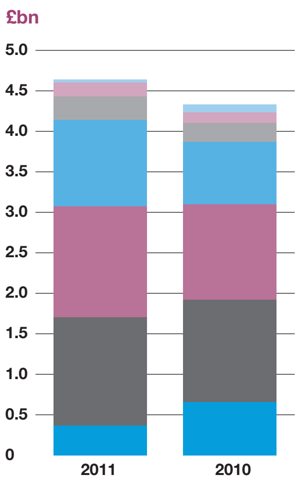
In addition to current service cost on the Group's defined benefit pension schemes, the Group also charged £10 million (2010: £5 million) to operating profit in respect of defined contribution pension schemes.

(f) Analysis of the actuarial gain/(loss) recognised in the Statement of Comprehensive Income

	2011 £m	2010 £m
Actuarial gain (actual return less expected return on pension scheme assets)	**–**	154
Experience gains arising on the scheme liabilities	**57**	74
Changes in assumptions underlying the present value of the schemes' liabilities	**141**	(237)
Actuarial gain/(loss) recognised in accumulated other comprehensive income (before taxation)	**198**	(9)
Cumulative actuarial losses recognised in reserves at 1 January, before adjustment for taxation	**(489)**	(480)
Cumulative actuarial losses recognised in reserves at 31 December, before adjustment for taxation	**(291)**	(489)

(g) Pension schemes assets

The expected long-term rate of return and the market value of plan assets are illustrated below:



	2011 Fair value £m	2011 Expected long-term rate of return per annum %	2010 Fair value £m	2010 Expected long-term rate of return per annum %
UK equities	**400**	**7.5**	659	8.0
Non-UK equities	**1,337**	**7.7**	1,261	8.0
Fixed-interest bonds	**1,370**	**5.3**	1,182	5.5
Inflation-linked assets	**1,067**	**3.9**	773	4.2
High-yield debt	**292**	**6.3**	229	7.5
Property	**168**	**6.8**	134	7.6
Cash pending investment	**36**	**4.6**	97	5.6
	4,670	**6.0**	4,335	6.6

The overall expected rate of return on assets is a weighted average based on the actual plan assets held in each class and the expected returns on separate asset classes, less costs of administering the plan and taxes paid by the plan itself. The returns on separate asset classes are based on the expected median return over a 10-year period (for equities, high-yield debt and property) and appropriate market indices (for fixed-interest bonds and inflation-linked assets). These returns are calculated by the independent company actuary, and adjusted for factors specific to the investment portfolio of the Centrica Combined Common Investment Fund, such as the duration of the assets.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

29. PENSIONS CONTINUED

Included within the Group Balance Sheet within non-current securities are £54 million (2010: £52 million) of investments, held by the Law Debenture Trust on behalf of the Company, as security in respect of the unfunded Centrica Unapproved Pension Scheme. Included within the pension schemes' liabilities above are £34 million (2010: £33 million) relating to this scheme.

(h) Pension scheme contributions

Based on the triennial valuation at 31 March 2009, the Company and the trustees of the Registered Pension Schemes agreed a schedule for deficit payments. An amount of £27 million has been paid in the year to 31 December 2011 and the following further deficit payments will be made: £37 million in 2012 and £57 million per annum from 2013 to 2016. Although there is an accounting surplus in the three Registered Pension Schemes, low government bond yields are likely to result in a deficit at the next triennial valuation scheduled to be prepared for the trustees as at 31 March 2012. It is unlikely, therefore, that the agreed deficit payments will reduce following the triennial valuation and they may increase or be extended. In addition, a charge over the Humber power station has been provided as additional security for the trustees.

The Company also estimates that it will pay £90 million of employer contributions during 2012 at an average rate of 17% of pensionable pay.

(i) Five-year histories

Five-year history of surplus/(deficit)	2011 £m	2010 £m	2009 £m	2008 £m	2007 £m
Plan assets	**4,670**	4,335	3,533	2,642	3,327
Defined benefit obligations	**(4,340)**	(4,574)	(4,098)	(2,755)	(3,230)
Surplus/(deficit)	**330**	(239)	(565)	(113)	97

Five-year history of experience gains and losses	2011	2010	2009	2008	2007
Difference between the expected and actual return on scheme assets:					
Amount (£m)	**–**	154	344	(1,121)	(38)
Percentage of scheme assets	**–**	3.6%	9.7%	42.4%	1.1%
Experience gains/(losses) on scheme liabilities:					
Amount (£m)	**57**	74	(104)	–	(16)
Percentage of the present value of scheme liabilities	**1.3%**	1.6%	2.5%	–	0.5%
Total actuarial gains/(losses) recognised in the Group Statement of Comprehensive Income:					
Amount (£m)	**198**	(9)	(804)	(399)	284
Percentage of the present value of scheme liabilities	**4.6%**	0.2%	19.6%	14.5%	8.8%

30. BUSINESS COMBINATIONS

Fair values of the identifiable assets acquired and liabilities assumed

	First Choice Power £m	Other £m	Total £m
Balance Sheet items			
Intangible assets	84	49	**133**
Property, plant and equipment	2	41	**43**
Other non-current assets	–	9	**9**
Current assets (i)	71	91	**162**
Current liabilities	(44)	(51)	**(95)**
Non-current liabilities	–	(20)	**(20)**
Net assets acquired	**113**	**119**	**232**
Goodwill	93	60	**153**
Total consideration	**206**	**179**	**385**
Consideration comprises:			
Cash consideration	206	173	**379**
Deferred cash consideration	–	6	**6**
Income Statement items			
Revenue recognised since the acquisition date and included within the Group Income Statement	37	159	**196**
Profit recognised since the acquisition date and included within the Group Income Statement	1	–	**1**

(i) Includes a bad debt provision of £11 million, predominantly in relation to First Choice Power trade receivables.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

30. BUSINESS COMBINATIONS CONTINUED

First Choice Power

On 1 November 2011, the Group acquired 100% of the shares in FCP Enterprises Inc ('First Choice Power') for cash consideration of $325 million (£206 million). First Choice Power is a Texas-based independent retail electricity supplier with more than 220,000 residential and small commercial customers. The acquisition is another important step towards growing scale and leadership in North America, and significantly enlarges the business in one of the key US deregulated residential markets. The acquisition is included within the North America – Residential energy supply segment.

Goodwill of $146 million (£93 million) arose, principally attributable to expected cost savings and synergies and is expected to be deductible for tax purposes. Acquisition costs of $0.2 million (£0.1 million) were expensed as operating costs. The fair values disclosed in the table are provisional pending finalisation of the completion accounts process.

Other acquisitions

The Group also acquired the following companies and interests during the year. The goodwill of £60 million is attributable to enhanced geographic presence, cost savings, synergies and growth opportunities, £4 million of which is expected to be deductible for tax purposes. Acquisition costs of £1.5 million were expensed as operating costs. The fair values are provisional unless stated otherwise.

Project	Description of business acquired	Date of control	Consideration (i)	Equity acquired
Wildcat Hills	Additional natural gas and infrastructure interests within the Wildcat Hills area. Increases natural gas reserves to meet North American supply requirements.	31 March 2011	CA$45m (£29m)	Various operating interests. No gain/loss on revaluation of existing interests
Gateway Energy Services Corporation	Independent retail energy supplier focused on residential and commercial customers. Increases customer relationships in US North-East and Mid-Atlantic.	1 May 2011	$108m including $10m deferred (£65m including £6m deferred)	100% of shares
PH Jones Group Limited	Independent provider of central heating services to social housing market. Increases business growth opportunities and helps cut customer carbon and fuel bills.	13 May 2011	£26m	100% of shares
Vectren Retail LLC	Supplier of gas to residential and small business customers. Increases customer relationships in US North-East.	30 December 2011	$84m (£54m)	100% of shares

(i) A small number of other businesses have been acquired for total consideration of £5 million.

Pro forma information

The pro forma consolidated results of the Group, as if the acquisitions had been made at the beginning of the year, would show revenue from continuing operations of £23,305 million (compared to reported revenue of £22,824 million) and profit after taxation of £436 million (compared to reported profit after taxation of £421 million).

This information is not necessarily indicative of the results of the combined Group that would have occurred had the purchases actually been made at the beginning of the year presented, or indicative of the future results of the combined Group.

2010 acquisitions – fair value updates

During the year to 31 December 2011, there have been no significant updates to the fair value entries posted in relation to acquisitions which occurred in 2010.

31. DISPOSALS, DISCONTINUED OPERATIONS AND DISPOSAL GROUPS HELD FOR SALE

The European segment was classified as a discontinued operation during 2009 following the Group's decision to dispose of its 100% interests in Segebel S.A. (Segebel), Centrica Energía S.L. (Centrica Energía) in Spain and Oxxio B.V. (Oxxio) in the Netherlands. The disposal of Segebel was completed in 2009. The sale of Centrica Energía was completed in November 2010.

On 1 June 2011, the Group completed its planned disposal of its European segment with the sale of the trade and assets of Oxxio which resulted in a loss on disposal of £56 million.

	Oxxio £m
Non-current assets (i)	115
Current assets (ii)	287
Current liabilities	(236)
Total net assets disposed	**166**
Total consideration (iii)	111
Net assets disposed	(166)
Foreign exchange recycled from reserves	3
Disposal costs	(4)
Loss on disposal after taxation	**(56)**

(i) Includes PP&E of £35 million and intangible assets and goodwill of £80 million which were included in assets held for sale.
(ii) Includes cash and cash equivalents of £8 million.
(iii) Includes deferred consideration of £25 million.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

32. SHARE-BASED PAYMENTS

(a) Summary of principal share-based payment plans and movements in the number of shares and options outstanding

Employee share schemes are designed to encourage participants to align their objectives with those of shareholders. Centrica operates nine employee share schemes which gave rise to a charge of £40 million (2010: £48 million) which represents 2% (2010: 3%) of employee costs. Over 70% of this share-based payment charge arose from three schemes: Deferred and Matching Share Scheme (DMSS), Long Term Incentive Scheme (LTIS) and Share Award Scheme (SAS). The DMSS and LTIS schemes have been described in the Remuneration Report on pages 55 and 56 respectively, with further details in note S7.

Share Award Scheme (SAS)

Under the SAS, allocations of shares in Centrica plc are made to selected employees at middle management levels, based on recommendation by the Chief Executive and the Group Director, Human Resources. There is no contractual eligibility for SAS and each year's award is made independently from previous awards. Allocations are subject to no performance conditions and vest unconditionally subject to continued employment within the Group (except where permitted by the rules of the scheme) in two stages – half of the award vesting after two years, the other half vesting after three years. On vesting, additional shares are awarded or a cash payment is made to reflect dividends that would have been paid on the allocations during the vesting period. The fair value is therefore considered to be the market value at date of grant.

A reconciliation of total number of shares allocated under these three schemes is as follows:

(Number of shares)	2011 Thousands	2010 Thousands
Balance at start of year	**51,969**	46,880
Granted	**18,245**	17,947
Released [(i)]	**(8,938)**	(7,583)
Forfeited	**(10,183)**	(5,275)
Balance at end of year	**51,093**	51,969

(i) For shares released during the period, the weighted average share price was £3.30 (2010: £2.98).

(b) Fair values and associated details of shares granted under the principal schemes

	2011 DMSS	2011 LTIS	2011 SAS	2010 DMSS	2010 LTIS	2010 SAS
Number of equity instruments granted (in thousands) [(i)]	**4,670**	**10,600**	**3,133**	4,855	10,366	3,187
Weighted average fair value at date of grant	**£2.89**	**£2.57**	**£3.32**	£3.32	£2.42	£2.97
Expected performance lapses	**0%**	**n/a**	**n/a**	0%	n/a	n/a
Vesting period	**4 years**	**3 years**	**2.5 years**	4 years	3 years	2.5 years
Expected volatility [(ii)]	**n/a**	**23%**	**n/a**	n/a	30%	n/a
Expected forfeitures	**6%**	**16%**	**18%**	10%	20%	18%
Risk-free rate [(ii)]	**n/a**	**1.9%**	**n/a**	n/a	1.8%	n/a
Average volatility of FTSE 100	**n/a**	**26%**	**n/a**	n/a	27%	n/a
Average cross-correlation of FTSE 100 [(iii)]	**n/a**	**50%**	**n/a**	n/a	48%	n/a

(i) The number of equity instruments granted under DMSS is the estimate on the first day of the bonus year. This differs from the table in section (a) which states the number of shares legally granted during the year.
(ii) The expected volatility is based on historical volatility over a five year period. The risk-free rate of return is the yield on zero-coupon UK Government bonds of a term consistent with the expected option life.
(iii) The cross-correlation of the FTSE 100 has been obtained from a model which calculates the correlation between Centrica's historical share price and each of the remaining FTSE 100 companies over the period commensurate with the performance period of the awards.

33. AUDITORS' REMUNERATION

	2011 £m	2010 £m
Fees payable to the Company's auditors for the audit of the Company's annual accounts and Group consolidation	**4.3**	3.6
The auditing of other accounts within the Group pursuant to legislation (including that of countries and territories outside the UK)	**1.4**	1.5
Total fees related to audit of parent and subsidiary entities	**5.7**	5.1
Fees payable to the Company's auditors and its associates for other services:		
Audit related assurance services	**0.9**	0.6
Tax advisory services	**0.3**	0.1
Services related to corporate finance transactions entered into or proposed to be entered into by or on behalf of the Company or any of its associates	**0.2**	1.2
All other services	**0.7**	1.6
	7.8	8.6
Fees in respect of pension scheme audits	**0.1**	0.1

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NOTES TO THE FINANCIAL STATEMENTS CONTINUED

33. AUDITORS' REMUNERATION CONTINUED

It is the Group's policy to seek competitive tenders for all major consultancy and advisory projects. Appointments are made taking into account factors including expertise, experience and cost. In addition, the Audit Committee has approved a detailed policy defining the types of work for which the auditors can tender and the approvals required. In the past, the auditors have been engaged on assignments in addition to their statutory audit duties where their expertise and experience with the Group are particularly important, including due diligence reporting and reporting accountant services on acquisitions.

34. COMMITMENTS AND CONTINGENCIES

(a) Commitments

The Group procures commodities through a mixture of production from gas fields, power stations, wind farms and procurement contracts. Procurement contracts include short-term forward market purchases of gas and electricity at fixed and floating prices. They also include gas and electricity contracts indexed to market prices and long-term gas contracts with non-gas indexation. The commitments in relation to commodity purchase contracts disclosed below are stated net of amounts receivable under commodity sales contracts, where there is a right of set-off with the counterparty.

The total volume of gas to be taken under certain long-term structured contracts depends on a number of factors, including the actual reserves of gas that are eventually determined to be extractable on an economic basis. The commitments disclosed below are based on the minimum quantities of gas that the Group is contracted to buy at estimated future prices.

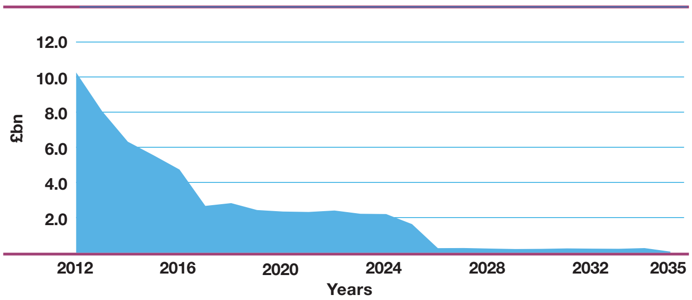
The commitments in this note differ in scope and in basis from the maturity analysis of energy derivatives disclosed in note 25. Whilst the commitments in relation to commodity purchase contracts include all purchase contracts, only certain procurement and sales contracts are within the scope of IAS 39 and included in note 25. In addition, the volumes used in calculating principal values in note 25 are estimated using valuation techniques, rather than being based on minimum contractual quantities and in note 25 there is no offset of amounts receivable under commodity sales contracts where there is a right of set-off with the counterparty.

	2011 £m	2010 restated (i) £m
Commitments in relation to the acquisition of property, plant and equipment:		
Acquisition of Statoil oil and gas assets	**983**	–
Development of York gas field	**82**	–
Other gas field developments	**13**	119
Other capital expenditure	**74**	65
Commitments in relation to the acquisition of intangible assets:		
Renewable obligation certificates to be purchased from joint ventures (ii)	**1,377**	1,145
Renewable obligation certificates to be purchased from other parties	**774**	631
EUAs and CERs	**44**	166
Exploration activity	**122**	80
Other intangible asset purchase commitments	**71**	66
Other commitments:		
Commodity purchase contracts	**58,311**	40,420
LNG capacity	**844**	874
Transportation capacity	**969**	771
Outsourcing of services	**348**	444
Commitments to invest in joint ventures	**234**	319
Other long term commitments	**777**	661
Operating lease commitments:		
Future minimum lease payments under non-cancellable operating leases (iii)	**950**	963

(i) Restated to correct prior year comparatives.
(ii) Renewable obligation certificates are purchased from several joint ventures which produce power from wind energy under long term offtake agreements (up to 15 years). The commitments disclosed above are the gross contractual commitments and do not take into account the Group's economic interest in the joint venture.
(iii) At 31 December the maturity analysis for the total minimum lease payments under non-cancellable operating leases was: <1 year £157 million, 1-2 years £130 million, 2-3 years £88 million, 3-4 years £65 million, 4-5 years £54 million and >5 years £456 million (2010: <1 year £146 million, 1-5 years £331 million and >5 years £486 million).

Commitment profile

The above commitments span many years. For the most significant commitment category, commodity purchase contracts, the graph on the right shows when the £58 billion commitments fall due:



NOTES TO THE FINANCIAL STATEMENTS CONTINUED

34. COMMITMENTS AND CONTINGENCIES CONTINUED

Lease payments recognised as an expense in the year were as follows:

	2011 £m	2010 £m
Minimum lease payments (net of sub-lease receipts)	**126**	101
Contingent rents – renewables (i)	**132**	115

(i) The Group has entered into long-term arrangements with renewable providers to purchase physical power, renewable obligation certificates and levy exemption certificates from renewable sources. Payments made under these contracts are contingent upon actual production and so there is no commitment to a minimum lease payment (2010: £nil). Payments made for physical power are charged to the Income Statement as incurred and disclosed as contingent rents.

(b) Guarantees and indemnities

In connection with the Group's energy trading, transportation and upstream activities, certain Group companies have entered into contracts under which they may be required to prepay, provide credit support or other collateral in the event of a significant deterioration in creditworthiness. The extent of credit support is contingent upon the balance owing to the third party at the point of deterioration.

The Group has provided a number of guarantees and indemnities in respect of decommissioning costs; the most significant two indemnities relate to the decommissioning costs associated with the Morecambe and Statfjord fields. These indemnities are to the previous owners of these fields. Under the licence conditions of the fields, the previous owners will have exposure to the decommissioning costs should these liabilities not be fully discharged by the Group.

The security is to be provided when the estimated future net revenue stream from the associated gas field falls below a predetermined proportion of the estimated decommissioning cost. The nature of the security may take a number of different forms and will remain in force until the costs of such decommissioning have been irrevocably discharged and the relevant legal decommissioning notices in respect of the relevant fields have been revoked.

(c) Contingent liabilities

There are no material contingent liabilities.

35. RELATED PARTY TRANSACTIONS

During the year, the Group entered into the following arms length transactions with related parties who are not members of the Group and had the following associated balances:

	2011				2010			
	Sale of goods and services £m	Purchase of goods and services £m	Amounts owed from £m	Amounts owed to £m	Sale of goods and services £m	Purchase of goods and services £m	Amounts owed from £m	Amounts owed to £m
Joint ventures:								
Wind farms (as defined in note 16)	**25**	**92**	**312**	**46**	–	82	206	37
Associates:								
Nuclear (as defined in note 16)	**278**	**516**	**19**	**65**	278	284	33	53
Other	**–**	**8**	**17**	**–**	–	38	–	2
	303	**616**	**348**	**111**	278	404	239	92

Investment and funding transactions for joint ventures and associates are disclosed in note 16. The terms of the outstanding balances related to trade receivables from related parties are typically 30 to 120 days. The balances are unsecured and will be settled in cash. No provision for bad or doubtful debts owed by related parties was required (2010: £nil).

Key management personnel comprise members of the Board and Executive Committee, a total of 15 individuals at 31 December 2011 (2010: 14). Key management personnel and their families purchase gas, electricity and home services products from the Group for domestic purposes on terms equal to those for other employees of the Group.

Remuneration of key management personnel	2011 £m	2010 £m
Short-term benefits	**7**	10
Post-employment benefits	**2**	1
Share-based payments	**8**	10
	17	21

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

36. FIXED-FEE SERVICE AND INSURANCE CONTRACTS

The fixed-fee service claims and insurance claims notified during the year were £115 million (2010: £259 million) and £356 million (2010: £104 million) respectively and were exactly matched by expenses related to fixed-fee service and insurance contracts. All claims are settled immediately and in full. Due to the short lead time between claims being incurred and claims being rectified, there are no material provisions outstanding at the balance sheet date (2010: £nil).

	2011 £m	2010 £m
Total revenue	**1,167**	1,098
Expenses relating to fixed-fee service and insurance contracts	**904**	851
Deferred income (unearned premium)	**68**	57
Accrued income	**28**	34

The Group considers the adequacy of estimated future cash flows under the contracts to meet expected future costs under the contracts. Any deficiency is charged immediately to the Income Statement. Service requests are sensitive to the reliability of appliances as well as the impact of weather conditions. Each incremental 1% increase in service and insurance requests would impact profit and equity by approximately £9 million (2010: £9 million). The contracts are not exposed to any interest rate risk or significant credit risk and do not contain any embedded derivatives. See note S8 for more information.

37. EVENTS AFTER THE BALANCE SHEET DATE

The Directors propose a final dividend of 11.11 pence per ordinary share (totalling £575 million) for the year ended 31 December 2011. The dividend will be submitted for formal approval at the Annual General Meeting to be held on 11 May 2012 and, subject to approval, will be paid on 13 June 2012 to those shareholders registered on 27 April 2012.

North American acquisitions

On 11 November 2011 Direct Energy announced the purchase of Home Warranty of America, a US nationwide home warranty protection plan company, for $48 million (£31 million). The acquisition involves the purchase of 100% of the shares of the company and it is anticipated this transaction will close in March 2012, pending regulatory approval. The acquisition allows Direct Energy to sell nationwide home protection plans and provides further growth and integration opportunities. A provisional goodwill value of $43 million (£27 million) is expected to arise, 40% of which is expected to be deductible for tax purposes.

On 8 December 2011 Direct Energy announced that it had agreed to acquire a package of natural gas assets located in west central Alberta (Carrot Creek assets) from Encana Corporation for CA$58 million (£37 million) in cash and Direct Energy's existing Entice asset with fair value of CA$48 million (£30 million). The Group obtained control of the business on 10 January 2012. The acquisition allows the Group to grow its North American upstream gas business. No goodwill is expected to arise.

Strategic partnership with Statoil and Norwegian asset acquisition

On 21 November 2011 Centrica Energy announced that it had signed a 10-year gas supply contract with Statoil starting from 2015, an agreement to pay $1,525 million (£983 million) with an additional payment of up to $100 million (£64 million) contingent on future production performance for the acquisition of producing and development assets in the Norwegian North Sea and a strategic agreement for partnership on gas exploration activities. As part of the transaction the relevant parts of Statoil's capacity rights in the gas export system from Norway to the UK and the Continent will be transferred to Centrica. The transaction is expected to complete in May 2012 and will help to deliver UK energy security, develop our strategic relationship with Statoil and further expand Centrica Energy's upstream business.

Statfjord asset acquisition

On 30 January 2012, Centrica Energy announced that it has reached agreement with ConocoPhillips to acquire its non-operated interests in the gas and oil producing Statfjord field and associated satellites for a total cash consideration of $223 million (£142 million). The deal is expected to complete in May 2012. The acquisition further strengthens Centrica's integrated business model and provides another source of gas for our UK customers.

Asset acquisition from Total

On 22 February 2012, Centrica announced an agreement with Total to acquire a portfolio of UK North Sea non-operated producing oil and gas assets for a cash consideration of $388 million (£246 million). The transaction is expected to close on a field by field basis. The earliest closing date is expected to be around July 2012. The acquisition increases the reserves of the Group and provides additional gas to meet supply requirements of our UK customers.

SUPPLEMENTARY INFORMATION

S1. GENERAL INFORMATION

Centrica plc is a Company domiciled and incorporated in the UK. The address of the registered office is given on page 51. The nature of the Group's operations and principal activities are set out in note S5 and in the Directors' Report – Business Review on pages 5 to 40.

The consolidated Financial Statements of Centrica plc are presented in pounds sterling. Operations and transactions conducted in currencies other than pounds sterling are included in the consolidated Financial Statements in accordance with the foreign currencies accounting policy set out in note S2.

S2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Income Statement presentation

The Group's Income Statement and segmental note separately identify the effects of re-measurement of certain financial instruments, and items which are exceptional, in order to provide readers with a clear and consistent presentation of the Group's underlying performance, as described below.

(i) Certain re-measurements

As part of its energy procurement activities, the Group enters into a range of commodity contracts designed to achieve security of energy supply. These contracts comprise both purchases and sales and cover a wide range of volumes, prices and timescales. The majority of the underlying supply comes from high-volume, long-term contracts which are complemented by short-term arrangements. These short-term contracts are entered into for the purpose of balancing energy supplies and customer demand and to optimise the price paid by the Group. Short-term demand can vary significantly as a result of factors such as weather, power generation profiles and short-term movements in market prices.

Many of the energy procurement contracts are held for the purpose of receipt or delivery of commodities in accordance with the Group's purchase, sale or usage requirements and are therefore out of scope of IAS 39. However, a number of contracts are considered to be derivative financial instruments and are required to be fair valued under IAS 39, primarily because their terms include the ability to trade elements of the contracted volumes on a net-settled basis.

The Group has shown the fair value adjustments arising on these contracts separately in the certain re-measurements column. This is because the intention of management is, subject to short-term demand balancing, to use these energy supplies to meet customer demand. Accordingly, management believes the ultimate net charge to cost of sales will be consistent with the price of energy agreed in these contracts and that the fair value adjustments will reverse as the energy is supplied over the life of the contract. This makes the fair value re-measurements very different in nature from costs arising from the physical delivery of energy in the year.

At the balance sheet date the fair value represents the difference between the prices agreed in the respective contracts and the actual or anticipated market price of acquiring the same amount of energy on the open market. The movement in the fair value taken to certain re-measurements in the Income Statement represents the unwinding of the contracted volume delivered or consumed during the year, combined with the change in fair value of future contracted energy as a result of movements in forward energy prices during the year.

As an integrated energy business, the Group also enter into a range of commodity contracts designed to secure the value of its underlying production, generation, storage and transportation assets. The fair value movements on these contracts are also shown separately in the certain re-measurements column. This is because the fair value movements on these contracts are not matched with fair value movements of the underlying assets, since not all the underlying assets are fair valued.

These adjustments represent the significant majority of the items included in certain re-measurements.

In addition to these, however, the Group has identified a number of comparable contractual arrangements where the difference between the price which the Group expects to pay or receive under a contract and the market price is required to be fair valued by IAS 39. These additional items relate to cross-border transportation or transmission capacity, storage capacity and contracts relating to the sale of energy by-products, on which economic value has been created which is not wholly recognised under the requirements of IAS 39. For these arrangements the related fair value adjustments are also included under certain re-measurements.

These arrangements are managed separately from proprietary energy trading activities where trades are entered into speculatively for the purpose of making profits in their own right. These proprietary trades are included in the results before certain re-measurements.

In addition, certain re-measurements include the effects of unwinding the acquisition-date fair values attributable to forward energy procurement and energy sales contracts arising on the acquisition of Strategic Investments, as described in note 2. The Group has shown the effect of unwinding the acquisition-date fair values attributable to forward energy procurement and energy sales contracts for these investments separately as a certain re-measurement as the intention is to use these energy supplies in the normal course of business and management believes the ultimate net charge reflected before the unwind of acquisition-date fair values will be consistent with the price of energy agreed within these contracts. Such presentation is consistent with the internal performance measures used by the Group.

(ii) Exceptional items

As permitted by IAS 1 (Revised), Presentation of Financial Statements, certain items are presented separately. The items that the Group separately presents as exceptional are items which are of a non-recurring nature and, in the judgement of the Directors, need to be disclosed separately by virtue of their nature, size or incidence in order to obtain a clear and consistent presentation of the Group's underlying business performance.

Basis of consolidation

The Group Financial Statements consolidate the Financial Statements of the Company and entities controlled by the Company (its subsidiaries) up to 31 December each year, and incorporate the results of its share of jointly controlled entities and associates using the equity method of accounting.

Control is achieved where the Company has the power to govern the financial and operating policies of an investee entity so as to obtain benefits from its activities.

The results of subsidiaries acquired or disposed of during the year are consolidated from the effective date of acquisition or up to the effective date of disposal, as appropriate. Where necessary, adjustments are made to the Financial Statements of subsidiaries, associates and jointly-controlled entities to bring the accounting policies used into line with those used by the Group.

When the Group ceases to have control or significant influence, any retained interest in the entity is re-measured to its fair value with the change in carrying amount recognised in profit or loss. This fair value becomes the initial carrying amount for the purposes of subsequently accounting for the retained interest as a joint venture, associate or financial asset.

Segmental reporting

The Group's operating segments are reported in a manner consistent with the internal reporting provided to and regularly reviewed by the Group's Executive Committee for the purposes of evaluating segment performance and allocating resources.

Revenue

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be measured reliably. Revenue includes amounts receivable for goods and services provided in the normal course of business, net of discounts, rebates, VAT and other sales-related taxes.

Energy supply: Revenue is recognised on the basis of energy supplied during the year. Revenue for energy supply activities includes an assessment of energy supplied to customers between the date of the last meter reading and the year end (unread). Unread gas and electricity is estimated using historical consumption patterns, taking into account the

SUPPLEMENTARY INFORMATION CONTINUED

S2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES CONTINUED

industry reconciliation process for total gas and total electricity usage by supplier, and is included in accrued energy income within trade and other receivables.

Proprietary energy trading: Revenue comprises both realised (settled) and unrealised (fair value changes) net gains and losses from trading in physical and financial energy contracts.

Fixed-fee service and insurance contracts: Revenue from these contracts is recognised in the Income Statement with regard to the incidence of risk over the life of the contract, reflecting the seasonal propensity of claims to be made under the contracts and the benefits receivable by the customer, which span the life of the contract as a result of emergency maintenance being available throughout the contract term.

Amounts paid in advance greater than recognised revenue are treated as deferred income, with any paid in arrears recognised as accrued income. For one-off services, such as installations, revenue is recognised at the date of service provision.

Storage services: Storage capacity revenues are recognised evenly over the contract period, whilst commodity revenues for the injection and withdrawal of gas are recognised at the point of gas flowing into or out of the storage facilities. Gas purchases and gas sales transactions entered into to optimise the performance of the gas storage facilities are presented net within revenue.

Upstream production: Revenue associated with exploration and production sales (of natural gas, crude oil and condensates) is recognised when title passes to the customer. Revenue from the production of natural gas, oil and condensates in which the Group has an interest with other producers is recognised based on the Group's working interest and the terms of the relevant production sharing arrangements (the entitlement method). Where differences arise between production sold and the Group's share of production, this is accounted for as an overlift or underlift (see separate accounting policy). Purchases and sales entered into to optimise the performance of production facilities are presented net within revenue.

Power generation: Revenue is recognised on the basis of power supplied during the period. Power purchases and sales entered into to optimise the performance of power generation facilities are presented net within revenue.

Interest income: Interest income is accrued on a time basis, by reference to the principal outstanding and at the effective interest rate applicable, which is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset to that asset's net carrying value.

Cost of sales

Energy supply includes the cost of gas and electricity produced and purchased during the year taking into account the industry reconciliation process for total gas and total electricity usage by supplier, and related transportation, distribution, royalty costs and bought-in materials and services.

Fixed-fee service and insurance contracts' cost of sales includes direct labour and related overheads on installation work, repairs and service contracts in the year.

Borrowing costs

Borrowing costs that arise in connection with the acquisition, construction or production of a qualifying asset are capitalised and subsequently amortised in line with the depreciation of the related asset. Borrowing costs are capitalised from the time of acquisition or from the beginning of construction or production until the point at which the qualifying asset is ready for use. Where a specific financing arrangement is in place, the specific borrowing rate for that arrangement is applied. For non-specific financing arrangements, a Group financing rate representative of the weighted average borrowing rate of the Group is used. Borrowing costs not arising in connection with the acquisition, construction or production of a qualifying asset are expensed.

Carbon Emissions Reduction Target programme and Communities Energy Savings Programme

UK-licensed energy suppliers are set a Carbon Emission Reduction Target ('CERT') by the Government which is proportional to the size of their customer base. The current CERT programme runs from April 2008 to December 2012. The CERT targets have been amended from April 2011, to include individual sub-targets related to insulation and non-insulation based carbon reductions. UK licensed energy suppliers and electricity generators are also required to contribute to the Communities Energy Saving Programme ('CESP') by the Government in proportion to the size of their customer base and also the amount of electricity they generate. The current CESP programme runs from October 2009 to December 2012.

The targets and contributions are subject to an annual adjustment throughout the programme period to take account of changes in their energy supplier's customer base and amount of electricity generated. Energy suppliers and generators can meet the target through expenditure on qualifying projects which give rise to carbon savings. The carbon savings can be transferred between suppliers and generators.

The Group charges the cost of the programmes to cost of sales with a provision recognised where there is a deficit of relevant credits held compared to the sub-target obligations accrued and capitalises the costs incurred in deriving carbon savings in excess of the annual targets or contribution as inventory. The inventory balance is valued at the lower of cost and net realisable value and may be used to meet the sub-target obligations in subsequent periods or sold to third parties. The inventory is carried on a first-in, first-out basis. The obligation for the programme period is allocated to reporting periods on a straight-line basis as adjusted by the annual determination process.

Employee share schemes

The Group operates a number of employee share schemes, detailed in the Remuneration Report on pages 52 to 63 and in notes 32 and S7, under which it makes equity-settled share-based payments to certain employees. Equity-settled share-based payments are measured at fair value at the date of grant (excluding the effect of non-market-based vesting conditions). The fair value determined at the grant date is expensed on a straight-line basis together with a corresponding increase in equity over the vesting period, based on the Group's estimate of the number of awards that will vest, and adjusted for the effect of non-market-based vesting conditions.

Fair value is measured using methods appropriate to each of the different schemes as follows:

LTIS: EPS awards after 2005	Market value on the date of grant
LTIS: TSR awards after 2005	A Monte Carlo simulation to predict the total shareholder return performance
SAS and DMSS	Market value on the date of grant

Foreign currencies

The consolidated Financial Statements are presented in pounds sterling, which is the functional currency of the Company and the Group's presentation currency. Each entity in the Group determines its own functional currency and items included in the Financial Statements of each entity are measured using that functional currency. Transactions in foreign currencies are, on initial recognition, recorded at the functional currency rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange ruling at the balance sheet date. All differences are included in the Income Statement for the period with the exception of exchange differences on foreign currency borrowings that provide a hedge against a net investment in a foreign entity. These are taken directly to equity until the disposal or partial disposal of the net investment, at which time they are recognised in the Income Statement.

Non-monetary items that are measured in terms of historical cost in a currency other than the functional currency of the entity concerned are translated using the exchange rates as at the dates of the initial transactions.

SUPPLEMENTARY INFORMATION CONTINUED

S2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES CONTINUED

For the purpose of presenting consolidated Financial Statements, the assets and liabilities of the Group's foreign subsidiary undertakings, jointly controlled entities and associates are translated into pounds sterling at exchange rates prevailing on the balance sheet date. The results of foreign subsidiary undertakings, jointly controlled entities and associates are translated into pounds sterling at average rates of exchange for the relevant period.

Exchange differences arising from the retranslation of the opening net assets and the results are transferred to the Group's foreign currency translation reserve, a separate component of equity, and are reported in the Statement of Comprehensive Income. In the event of the disposal of an undertaking with assets and liabilities denominated in a foreign currency, the cumulative translation difference arising in the foreign currency translation reserve is charged or credited to the Income Statement on disposal.

Exchange differences on foreign currency borrowings, foreign currency swaps and forward exchange contracts used to hedge foreign currency net investments in foreign subsidiary undertakings, jointly controlled entities and associates are taken directly to reserves and are reported in the Statement of Comprehensive Income. All other exchange movements are recognised in the Income Statement for the year.

Business combinations and goodwill

The acquisition of subsidiaries is accounted for using the purchase method. The cost of the acquisition is measured as the cash paid and the aggregate of the fair values, at the date of exchange, of other assets transferred, liabilities incurred or assumed, and equity instruments issued by the Group in exchange for control of the acquiree. The acquiree's identifiable assets, liabilities and contingent liabilities that meet the conditions for recognition under IFRS 3 (Revised), Business Combinations, are recognised at their fair value at the acquisition date, except for non-current assets (or disposal groups) that are classified as held for resale in accordance with IFRS 5, Non-Current Assets Held for Sale and Discontinued Operations, which are recognised and measured at fair value less costs to sell.

Goodwill arising on a business combination represents the excess of the cost of acquisition over the Group's interest in the fair value of the identifiable assets and liabilities of a subsidiary, jointly controlled entity or associate at the date of acquisition. Goodwill is initially recognised as an asset at cost and is subsequently measured at cost less any accumulated impairment losses. If, after reassessment, the Group's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities exceeds the cost of the business combination, the excess is recognised immediately in the Income Statement.

On disposal of a subsidiary, associate or joint venture entity, any amounts of goodwill attributed to that entity is included in the determination of the profit or loss on disposal.

Other intangible assets

Intangible assets acquired separately are measured on initial recognition at cost. Intangible assets include emissions trading schemes, renewable obligation certificates, certain exploration and evaluation expenditures, brands and application software, the accounting policies for which are dealt with separately below. For purchased application software, for example investments in customer relationship management and billing systems, cost includes contractors' charges, materials, directly-attributable labour and directly-attributable overheads.

Capitalisation begins when expenditure for the asset is being incurred and activities necessary to prepare the asset for use are in progress. Capitalisation ceases when substantially all the activities that are necessary to prepare the asset for use are complete. Amortisation commences at the point of commercial deployment. The cost of intangible assets acquired in a business combination is their fair value as at the date of acquisition.

Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses. The useful lives of intangible assets are assessed to be either finite or indefinite. Intangible assets with finite lives are amortised over their useful economic life and assessed for impairment whenever there is an indication that the intangible asset could be impaired. The amortisation period and the amortisation method for an intangible asset are reviewed at least at each financial year end. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset are accounted for on a prospective basis by changing the amortisation period or method, as appropriate, and treated as changes in accounting estimates.

Intangible assets are derecognised on disposal, or when no future economic benefits are expected from their use.

Intangible assets with indefinite useful lives are tested for impairment annually, and whenever there is an indication that the intangible asset could be impaired, either individually or at the CGU level. Such intangibles are not amortised. The useful life of an intangible asset with an indefinite useful life is reviewed annually to determine whether the indefinite life assessment continues to be supportable. If not, the change in the useful life assessment from indefinite to finite is made on a prospective basis.

The amortisation period for the principal categories of intangible assets are as follows:

Application software	up to 10 years
Licences	up to 20 years
Contractual customer relationships	up to 20 years
Strategic identifiable acquired brand	Indefinite

EU Emissions Trading Scheme and renewable obligations certificates

Granted carbon dioxide emissions allowances received in a period are recognised initially at nominal value (nil value). Purchased carbon dioxide emissions allowances are recognised initially at cost (purchase price) within intangible assets. A liability is recognised when the level of emissions exceeds the level of allowances granted. The liability is measured at the cost of purchased allowances up to the level of purchased allowances held, and then at the market price of allowances ruling at the balance sheet date, with movements in the liability recognised in operating profit.

Forward contracts for the purchase or sale of carbon dioxide emissions allowances are measured at fair value with gains and losses arising from changes in fair value recognised in the Income Statement. The intangible asset is surrendered and the liability is utilised at the end of the compliance period to reflect the consumption of economic benefits.

Purchased renewable obligation certificates are recognised initially at cost within intangible assets. A liability for the renewables obligation is recognised based on the level of electricity supplied to customers, and is calculated in accordance with percentages set by the UK Government and the renewable obligation certificate buyout price for that period.

The intangible asset is surrendered and the liability is utilised at the end of the compliance period to reflect the consumption of economic benefits. Any recycling benefit related to the submission of renewable obligation certificates is recognised in the Income Statement when received.

Exploration, evaluation and production assets

Centrica uses the successful efforts method of accounting for exploration and evaluation expenditure. Exploration and evaluation expenditure associated with an exploration well, including acquisition costs related to exploration and evaluation activities, are capitalised initially as intangible assets. Certain expenditures such as geological and geophysical exploration costs are expensed. If the prospects are subsequently determined to be successful on completion of evaluation, the relevant expenditure including licence acquisition costs is transferred to PP&E and are subsequently depreciated on a unit of production basis. If the prospects are subsequently determined to be unsuccessful on completion of evaluation, the associated costs are expensed in the period in which that determination is made.

All field development costs are capitalised as PP&E. Such costs relate to the acquisition and installation of production facilities and include development drilling costs, project-related engineering and other technical services costs. PP&E, including rights and concessions related to

SUPPLEMENTARY INFORMATION CONTINUED

S2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES CONTINUED

production activities, are depreciated from the commencement of production in the fields concerned, using the unit of production method, based on all of the 2P reserves of those fields. Changes in these estimates are dealt with prospectively.

The net carrying value of fields in production and development is compared on a field-by-field basis with the likely discounted future net revenues to be derived from the remaining commercial reserves. An impairment loss is recognised where it is considered that recorded amounts are unlikely to be fully recovered from the net present value of future net revenues. Exploration and production assets are reviewed annually for indicators of impairment.

Interests in joint ventures

Under the equity method, investments in jointly controlled entities are carried at cost plus post-acquisition changes in the Group's share of net assets of the jointly controlled entity, less any impairment in value in individual investments. The Income Statement reflects the Group's share of the results of operations after tax of the jointly controlled entity.

Certain exploration and production activity is conducted through joint ventures, where the venturers have a direct interest in and jointly control the assets of the venture. The results, assets, liabilities and cash flows of these jointly controlled assets are included in the consolidated Financial Statements in proportion to the Group's interest.

Interests in associates

Under the equity method, investments in associates are carried at cost plus post-acquisition changes in the Group's share of the net assets of the associate, less any impairment in value in individual investments. The Income Statement reflects the Group's share of the results of the associate, which is net of interest and taxation and presents this as a single line item in arriving at Group operating profit on the face of the Income Statement.

Property, plant and equipment

PP&E is included in the Balance Sheet at cost, less accumulated depreciation and any provisions for impairment.

The initial cost of an asset comprises its purchase price or construction cost and any costs directly attributable to bringing the asset into operation. The purchase price or construction cost is the aggregate amount paid and the fair value of any other consideration given to acquire the asset.

Subsequent expenditure in respect of items of PP&E such as the replacement of major parts, major inspections or overhauls, are capitalised as part of the cost of the related asset where it is probable that future economic benefits will arise as a result of the expenditure and the cost can be reliably measured. All other subsequent expenditure, including the costs of day-to-day servicing, repairs and maintenance, is expensed as incurred.

Freehold land is not depreciated. Other PP&E, with the exception of upstream production assets (see below), are depreciated on a straight-line basis at rates sufficient to write off the cost, less estimated residual values, of individual assets over their estimated useful lives. The depreciation periods for the principal categories of assets are as follows:

Freehold and leasehold buildings	up to 50 years
Plant	5 to 20 years
Power stations and wind farms	up to 30 years
Equipment and vehicles	3 to 10 years
Storage	up to 40 years

Assets held under finance leases are depreciated over their expected useful economic lives on the same basis as for owned assets, or where shorter, the lease term.

The carrying values of PP&E are reviewed for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable. Residual values and useful lives are reassessed annually and if necessary changes are accounted for prospectively.

Impairment of property, plant and equipment, intangible assets, investments in joint ventures and associates and goodwill

The Group reviews the carrying amounts of PP&E, intangible assets, interests in joint ventures and associates and goodwill annually, or more frequently if events or changes in circumstances indicate that the recoverable amounts may be lower than their carrying amounts. Where an asset does not generate cash flows that are independent from other assets, the Group estimates the recoverable amount of the CGU to which the asset belongs. The recoverable amount is the higher of value in use and fair value less costs to sell. At inception, goodwill is allocated to each of the Group's CGUs or groups of CGUs that expect to benefit from the business combination in which the goodwill arose. If the recoverable amount of an asset (or CGU) is estimated to be less than its carrying amount, the carrying amount of the asset (or CGU) is reduced to its recoverable amount. Any impairment is expensed immediately in the Income Statement. Any goodwill impairment loss is allocated first to reduce the carrying amount of any goodwill allocated to the CGU and then to the other assets of the unit pro rata on the basis of the carrying amount of each asset in the unit.

An impairment loss is reversed only if there has been a change in the estimate used to determine the asset's recoverable amount since the last impairment loss was recognised, with the exception of goodwill impairment which is never reversed. Where an impairment loss subsequently reverses, the carrying amount of the asset (or CGU) is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset (or CGU) in prior years. A reversal of an impairment loss is recognised in the Income Statement immediately. After such a reversal the depreciation or amortisation charge, where relevant, is adjusted in future periods to allocate the asset's revised carrying amount, less any residual value, on a systematic basis over its remaining useful life.

Overlift and underlift

Offtake arrangements for oil and gas produced from jointly owned operations are often such that it is not practical for each participant to receive or sell its precise share of the overall production during the period. This results in short-term imbalances between cumulative production entitlement and cumulative sales, referred to as overlift and underlift.

An overlift payable, or underlift receivable, is recognised at the balance sheet date within Trade and other payables, or Trade and other receivables, respectively and measured at market value, with movements in the period recognised within cost of sales.

Leases

The determination of whether an arrangement is, or contains, a lease is based on the substance of the arrangement and requires an assessment of whether the fulfilment of the arrangement is dependent on the use of a specific asset or assets and whether the arrangement conveys a right to use the asset. Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases. Assets held under finance leases are capitalised and included in PP&E at their fair value, or if lower, at the present value of the minimum lease payments, each determined at the inception of the lease. The obligations relating to finance leases, net of finance charges in respect of future periods, are included within bank loans and other borrowings, with the amount payable within 12 months included in bank overdrafts and loans within current liabilities.

Lease payments are apportioned between finance charges and reduction of the finance lease obligation so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged directly against income.

Payments under operating leases are charged to the Income Statement on a straight-line basis over the term of the relevant lease.

Inventories

Inventories are valued on a weighted-average cost basis, with the exception of CERT inventory, and at the lower of cost and estimated net realisable value after allowance for redundant and slow-moving items.

SUPPLEMENTARY INFORMATION CONTINUED

S2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES CONTINUED

Decommissioning costs

Provision is made for the net present value of the estimated cost of decommissioning gas production facilities at the end of the producing lives of fields, and storage facilities and power stations at the end of the useful life of the facilities, based on price levels and technology at the balance sheet date.

When this provision gives access to future economic benefits, a decommissioning asset is recognised and included as part of the associated PP&E and depreciated accordingly. Changes in these estimates and changes to the discount rates are dealt with prospectively and reflected as an adjustment to the provision and corresponding decommissioning asset included within PP&E. The unwinding of the discount on the provision is included in the Income Statement within interest expense.

Non-current assets and disposal groups held for sale and discontinued operations

Non-current assets (and disposal groups) classified as held for sale are measured at the lower of carrying amount and fair value less costs to sell. No depreciation is charged in respect of non-current assets classified as held for sale.

Non-current assets and disposal groups are classified as held for sale if their carrying amount will be recovered through a sale transaction rather than through continuing use. This condition is regarded as met only when the sale is highly probable and the asset (or disposal group) is available for immediate sale in its present condition. Management must be committed to the sale which should be expected to qualify for recognition as a completed sale within one year from the date of classification.

The profits or losses and cash flows that relate to a major component of the Group or geographical region that has been sold or is classified as held for sale are presented separately from continuing operations as discontinued operations within the Income Statement and Cash Flow Statement.

Pensions and other post-employment benefits

The Group operates a number of defined benefit pension schemes. The cost of providing benefits under the defined benefit schemes is determined separately for each scheme using the projected unit credit actuarial valuation method. Actuarial gains and losses are recognised in full in the period in which they occur. They are recognised in the Statement of Comprehensive Income.

The cost of providing retirement pensions and other benefits is charged to the Income Statement over the periods benefiting from employees' service. Past service cost is recognised immediately to the extent that the benefits are already vested, and otherwise is amortised on a straight-line basis over the average period until the benefits become vested. The difference between the expected return on scheme assets and the change in present value of scheme obligations resulting from the passage of time is recognised in the Income Statement within interest income or interest expense.

The retirement benefit obligation or asset recognised in the Balance Sheet represents the present value of the defined benefit obligation of the schemes as adjusted for unrecognised past service cost, and the fair value of the schemes' assets. The present value of the defined benefit obligation or asset is determined by discounting the estimated future cash outflows using interest rates of high-quality corporate bonds that are denominated in the currency in which the benefits are paid, and that have terms of maturity approximating to the terms of the related pension liability.

Payments to defined contribution retirement benefit schemes are charged as an operating expense as they fall due.

Provisions

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, that can be measured reliably, and it is probable that the Group will be required to settle that obligation. Provisions are measured at the Directors' best estimate of the expenditure required to settle the obligation at the balance sheet date, and are discounted to present value where the effect is material. Where discounting is used, the increase in the provision due to the passage of time is recognised in the Income Statement within interest expense. Onerous contract provisions are recognised where the unavoidable costs of meeting the obligations under a contract exceed the economic benefits expected to be received under it. Contracts to purchase or sell energy are reviewed on a portfolio basis given the fungible nature of energy, whereby it is assumed that the highest priced purchase contract supplies the highest priced sales contract and the lowest priced sales contract is supplied by the lowest priced purchase contract.

Taxation

Current tax, including UK corporation tax, UK petroleum revenue tax and foreign tax is provided at amounts expected to be paid (or recovered) using the tax rates and laws that have been enacted or substantively enacted by the balance sheet date.

Deferred tax is recognised in respect of all temporary differences identified at the balance sheet date, except to the extent that the deferred tax arises from the initial recognition of goodwill (if amortisation of goodwill is not deductible for tax purposes) or the initial recognition of an asset or liability in a transaction which is not a business combination and at the time of the transaction affects neither accounting profit nor taxable profit and loss. Temporary differences are differences between the carrying amount of the Group's assets and liabilities and their tax base.

Deferred tax liabilities may be offset against deferred tax assets within the same taxable entity or qualifying local tax group. Any remaining deferred tax asset is recognised only when, on the basis of all available evidence, it can be regarded as probable that there will be suitable taxable profits, within the same jurisdiction, in the foreseeable future, against which the deductible temporary difference can be utilised.

Deferred tax is provided on temporary differences arising on subsidiaries, jointly controlled entities and associates, except where the timing of the reversal of the temporary difference can be controlled and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred tax is measured at the average tax rates that are expected to apply in the periods in which the asset is realised or liability settled, based on tax rates and laws that have been enacted or substantively enacted by the balance sheet date. Measurement of deferred tax liabilities and assets reflects the tax consequences expected from the manner in which the asset or liability is recovered or settled.

Financial instruments

Financial assets and financial liabilities are recognised in the Group Balance Sheet when the Group becomes a party to the contractual provisions of the instrument. Financial assets are de-recognised when the Group no longer has the rights to cash flows, the risks and rewards of ownership or control of the asset. Financial liabilities are de-recognised when the obligation under the liability is discharged, cancelled or expires.

(a) Trade receivables

Trade receivables are recognised and carried at original invoice amount less an allowance for any uncollectible amounts. Provision is made when there is objective evidence that the Group may not be able to collect the trade receivable. Balances are written off when recoverability is assessed as being remote. If collection is due in one year or less they are classified as current assets. If not they are presented as non-current assets.

(b) Trade payables

Trade payables are recognised at original invoice amount. If payment is due within one year or less they are classified as current liabilities. If not, they are presented as non-current liabilities.

(c) Share capital

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of new shares are shown in equity as a deduction from the proceeds received. Own equity instruments that are reacquired (treasury shares) are deducted from equity. No gain or loss is recognised in the Income Statement on the purchase, sale, issue or cancellation of the Group's own equity instruments.

(d) Cash and cash equivalents

Cash and cash equivalents comprise cash in hand and current balances with banks and similar institutions, which are readily convertible to known

SUPPLEMENTARY INFORMATION CONTINUED

S2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES CONTINUED

amounts of cash and which are subject to insignificant risk of changes in value and have an original maturity of three months or less.

For the purpose of the Group Cash Flow Statement, cash and cash equivalents consist of cash and cash equivalents as defined above, net of outstanding bank overdrafts.

(e) Interest-bearing loans and other borrowings

All interest-bearing loans and other borrowings are initially recognised at fair value net of directly attributable transaction costs. After initial recognition, interest-bearing loans and other borrowings are subsequently measured at amortised cost using the effective interest method, except when they are the hedged item in an effective fair value hedge relationship where the carrying value is also adjusted to reflect the fair value movements associated with the hedged risks. Such fair value movements are recognised in the Income Statement. Amortised cost is calculated by taking into account any issue costs, discount or premium.

(f) Available-for-sale financial assets

Available-for-sale financial assets are those non-derivative financial assets that are designated as available-for-sale, which are recognised initially at fair value within the Balance Sheet. Available-for-sale financial assets are re-measured subsequently at fair value with gains and losses arising from changes in fair value recognised directly in equity and presented in the Statement of Comprehensive Income, until the asset is disposed of or is determined to be impaired, at which time the cumulative gain or loss previously recognised in equity is included in the Income Statement for the period. Accrued interest or dividends arising on available-for-sale financial assets are recognised in the Income Statement.

At each balance sheet date the Group assesses whether there is objective evidence that available-for-sale financial assets are impaired. If any such evidence exists, cumulative losses recognised in equity are removed from equity and recognised in the Income Statement. The cumulative loss removed from equity represents the difference between the acquisition cost and current fair value, less any impairment loss on that financial asset previously recognised in the Income Statement.

Impairment losses recognised in the Income Statement for equity investments classified as available-for-sale are not subsequently reversed through the Income Statement. Impairment losses recognised in the Income Statement for debt instruments classified as available-for-sale are subsequently reversed if an increase in the fair value of the instrument can be objectively related to an event occurring after the recognition of the impairment loss.

(g) Financial assets at fair value through profit or loss

The Group holds investments in gilts which it designates as fair value through profit or loss. Investments are measured at fair value on initial recognition and are re-measured to fair value in each subsequent reporting period. Gains and losses arising from changes in fair value are recognised in the Income Statement within interest income or interest expense.

(h) Derivative financial instruments

The Group routinely enters into sale and purchase transactions for physical delivery of gas, power and oil. A portion of these transactions take the form of contracts that were entered into and continue to be held for the purpose of receipt or delivery of the physical commodity in accordance with the Group's expected sale, purchase or usage requirements, and are not within the scope of IAS 39.

Certain purchase and sales contracts for the physical delivery of gas, power and oil are within the scope of IAS 39 due to the fact that they net settle or contain written options. Such contracts are accounted for as derivatives under IAS 39 and are recognised in the Balance Sheet at fair value. Gains and losses arising from changes in fair value on derivatives that do not qualify for hedge accounting are taken directly to the Income Statement for the year.

The Group uses a range of derivatives for both trading and to hedge exposures to financial risks, such as interest rate, foreign exchange and energy price risks, arising in the normal course of business. The use of derivative financial instruments is governed by the Group's policies approved by the Board of Directors. Further detail on the Group's risk management policies is included within the Directors' Report - Governance on pages 49 to 51 and in note S3.

The accounting treatment for derivatives is dependent on whether they are entered into for trading or hedging purposes. A derivative instrument is considered to be used for hedging purposes when it alters the risk profile of an underlying exposure of the Group in line with the Group's risk management policies and is in accordance with established guidelines, which require the hedging relationship to be documented at its inception, ensure that the derivative is highly effective in achieving its objective, and require that its effectiveness can be reliably measured. The Group also holds derivatives which are not designated as hedges and are held for trading.

All derivatives are recognised at fair value on the date on which the derivative is entered into and are re-measured to fair value at each reporting date. Derivatives are carried as assets when the fair value is positive and as liabilities when the fair value is negative. Derivative assets and derivative liabilities are offset and presented on a net basis only when both a legal right of set-off exists and the intention to net settle the derivative contracts is present.

The Group enters into certain energy derivative contracts covering periods for which observable market data does not exist. The fair value of such derivatives is estimated by reference in part to published price quotations from active markets, to the extent that such observable market data exists, and in part by using valuation techniques, whose inputs include data which is not based on or derived from observable markets. Where the fair value at initial recognition for such contracts differs from the transaction price, a fair value gain or fair value loss will arise. This is referred to as a day-one gain or day-one loss. Such gains and losses are deferred and amortised to the Income Statement based on volumes purchased or delivered over the contractual period until such time observable market data becomes available. When observable market data becomes available, any remaining deferred day-one gains or losses are recognised within the Income Statement. Recognition of the gains or losses resulting from changes in fair value depends on the purpose for issuing or holding the derivative. For derivatives that do not qualify for hedge accounting, any gains or losses arising from changes in fair value are taken directly to the Income Statement and are included within gross profit or interest income and interest expense. Gains and losses arising on derivatives entered into for speculative energy trading purposes are presented on a net basis within revenue.

Embedded derivatives: Derivatives embedded in other financial instruments or other host contracts are treated as separate derivatives when their risks and characteristics are not closely related to those of the host contracts and the host contracts are not carried at fair value, with gains or losses reported in the Income Statement. The closely-related nature of embedded derivatives is reassessed when there is a change in the terms of the contract which significantly modifies the future cash flows under the contract. Where a contract contains one or more embedded derivatives, and providing that the embedded derivative significantly modifies the cash flows under the contract, the option to fair value the entire contract may be taken and the contract will be recognised at fair value with changes in fair value recognised in the Income Statement.

(i) Hedge accounting

For the purposes of hedge accounting, hedges are classified either as fair value hedges, cash flow hedges or hedges of net investments in foreign operations.

Fair value hedges: A derivative is classified as a fair value hedge when it hedges the exposure to changes in the fair value of a recognised asset or liability. Any gain or loss from re-measuring the hedging instrument to fair value is recognised immediately in the Income Statement. Any gain or loss on the hedged item attributable to the hedged risk is adjusted against the carrying amount of the hedged item and recognised in the Income Statement. The Group discontinues fair value hedge accounting if the hedging instrument expires or is sold, terminated or exercised, the hedge no longer qualifies for hedge accounting or the Group revokes the designation. Any adjustment to the carrying amount of a hedged financial instrument for which the effective interest method is used is amortised to the Income Statement. Amortisation

SUPPLEMENTARY INFORMATION CONTINUED

S2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES CONTINUED

may begin as soon as an adjustment exists and shall begin no later than when the hedged item ceases to be adjusted for changes in its fair value attributable to the risk being hedged.

Cash flow hedges: A derivative is classified as a cash flow hedge when it hedges exposure to variability in cash flows that is attributable to a particular risk either associated with a recognised asset, liability or a highly probable forecast transaction. The portion of the gain or loss on the hedging instrument which is effective is recognised directly in equity while any ineffectiveness is recognised in the Income Statement. The gains or losses that are recognised directly in equity are transferred to the Income Statement in the same period in which the highly probable forecast transaction affects income, for example when the future sale of physical gas or physical power actually occurs. Where the hedged item is the cost of a non-financial asset or liability, the amounts taken to equity are transferred to the initial carrying amount of the non-financial asset or liability on its recognition. Hedge accounting is discontinued when the hedging instrument expires or is sold, terminated or exercised without replacement or rollover, no longer qualifies for hedge accounting or the Group revokes the designation.

At that point in time, any cumulative gain or loss on the hedging instrument recognised in equity remains in equity until the highly probable forecast transaction occurs. If the transaction is no longer expected to occur, the cumulative gain or loss recognised in equity is recognised in the Income Statement.

Net investment hedges: Hedges of net investments in foreign operations are accounted for similarly to cash flow hedges. Any gain or loss on the effective portion of the hedge is recognised in equity, any gain or loss on the ineffective portion of the hedge is recognised in the Income Statement. On disposal of the foreign operation, the cumulative value of any gains or losses recognised directly in equity is transferred to the Income Statement.

Nuclear activity

The Group's investments in Lake Acquisitions Limited and NNB Holding Company Limited are accounted for as associates. The following accounting policies are specific to the accounting for the nuclear activity of these associates.

(a) Fuel costs – nuclear front end

Front end fuel costs consist of the costs of procurement of uranium, conversion and enrichment services and fuel element fabrication. All costs are capitalised into inventory and charged to the Income Statement in proportion to the amount of fuel burnt.

(b) Fuel costs – nuclear back end

Advanced Gas-cooled Reactors (AGR)

Spent fuel extracted from the reactors is sent for reprocessing and/or long-term storage and eventual disposal of resulting waste products. Back end fuel costs comprise a loading related cost per tonne of uranium and a rebate/surcharge to this cost dependent on the out-turn market electricity price in the year and are capitalised into inventory and charged to the Income Statement in proportion to the amount of fuel burnt.

Pressurised Water Reactor (PWR)

Back end fuel costs are based on wet storage in station ponds followed by dry storage and subsequent direct disposal of fuel. Back end fuel costs are capitalised into inventory on loading and charged to the Income Statement in proportion to the amount of fuel burnt.

(c) Nuclear property, plant and equipment and depreciation

The depreciation period for the nuclear fleet, which are depreciated on a straight-line basis from the date of the Group acquiring its share in British Energy, are as follows:

Hinkley Point and Hunterston	2016
Dungeness B	2018
Heysham 1 and Hartlepool	2019
Heysham 2 and Torness	2023
Sizewell B	2035

Expenditure on major inspection and overhauls of production plant is depreciated over the period until the next outage which for AGR power stations is two to three years and for the PWR power station is 18 months.

(d) Nuclear Liabilities Fund (NLF) funding arrangements

Under the arrangements in place with the Secretary of State, the NLF will fund, subject to certain exceptions, British Energy's qualifying uncontracted nuclear liabilities and qualifying decommissioning costs.

In part consideration for the assumption of these liabilities by the Secretary of State and the NLF, British Energy agreed to pay fixed decommissioning contributions each year and £150,000 (indexed to RPI) for every tonne of uranium in PWR fuel loaded into the Sizewell B reactor after the date of these arrangements.

(e) NLF and nuclear liabilities receivables

The Government indemnity is provided to indemnify any future shortfall on NLF funding of qualifying uncontracted nuclear liabilities (including PWR back end fuel services) and qualifying nuclear decommissioning costs such that the receivable equals the present value of the associated qualifying nuclear liabilities.

(f) Nuclear liabilities

Nuclear liabilities represent provision for British Energy's liabilities in respect of the costs of waste management of spent fuel and nuclear decommissioning.

(g) Unburnt fuels at shutdown

Due to the nature of the nuclear fuel process there will be quantities of unburnt fuel in the reactors at station closure. The costs relating to this unburnt fuel (final core) are estimated by applying a long-term inflation index to the projected costs, which are then discounted.

S3. FINANCIAL RISK MANAGEMENT

The Group's normal operating, investing and financing activities expose it to a variety of financial risks: market risk (including commodity price risk, volumetric risk, currency risk, interest rate risk and equity price risk), credit risk and liquidity risk. The Group's overall risk management process is designed to identify, manage and mitigate business risk, which includes, among others, financial risk. Further detail on the Group's overall risk management process is included within the Directors' Report – Governance on pages 49 to 51.

Financial risk management is overseen by the Group Financial Risk Management Committee (GFRMC) according to objectives, targets and policies set by the Board. Commodity price risk management is carried out in accordance with individual business unit Financial Risk Management Committees and their respective financial risk management policies, as approved by the GFRMC under delegated authority from the Board. Treasury risk management, including management of currency risk, interest rate risk, equity price risk and liquidity risk is carried out by a central Group Treasury function in accordance with the Group's financing and treasury policy and collateral risk policy, as approved by the Board.

The wholesale credit risks associated with commodity trading and treasury positions are managed in accordance with the Group's credit risk policy. Downstream credit risk management is carried out in accordance with individual business unit credit policies.

Market risk management

Market risk is the risk of loss that results from changes in market prices (commodity prices, foreign exchange rates, interest rates and equity prices). The level of market risk to which the Group is exposed at a point in time varies depending on market conditions, expectations of future price or market rate movements and the composition of the Group's physical asset and contract portfolios.

(a) Commodity price risk management

The Group is exposed to commodity price risk in its upstream assets, energy procurement contracts, downstream and proprietary energy trading activities and uses specific limits to manage the exposure to commodity prices associated with the Group's activities to an acceptable level. Volumetric limits are supported by Profit at Risk (PaR) and Value at Risk (VaR) metrics in the UK and in North America to measure the

SUPPLEMENTARY INFORMATION CONTINUED

S3. FINANCIAL RISK MANAGEMENT CONTINUED

Group's exposure to commodity price risk. Limits are also set on PaR and VaR measurements as a further control over exposure to market prices.

(i) Energy procurement, upstream and downstream activities

The Group's energy procurement, upstream and downstream activities consist of equity gas and liquids production, equity power generation, bilateral procurement and sales contracts, market-traded purchase and sales contracts and derivative positions taken on with the intent of securing gas and power for the Group's downstream customers in the UK and North America from a variety of sources at an optimal cost. The Group actively manages commodity price risk by optimising its asset and contract portfolios and making use of volume flexibility.

The Group is exposed to commodity price risk in its energy procurement, upstream and downstream activities because the cost of procuring gas and electricity to serve its downstream customers varies with wholesale commodity prices. The risk is primarily that market prices for commodities will fluctuate between the time that sales prices are fixed or tariffs are set and the time at which the corresponding procurement cost is fixed, thereby potentially reducing expected margins or making sales unprofitable.

The Group is also exposed to volumetric risk in the form of an uncertain consumption profile arising from a range of factors, including weather, energy consumption changes, customer attrition and economic climate.

In order to manage the exposure to market prices associated with the Group's energy procurement, upstream and downstream activities the Group uses a specific set of limits (including position, volumetric, VaR/PaR) established by the Executive Committee and governed by GFRMC oversight along with business unit market risk policies.

Volumetric limits are supported by PaR and VaR metrics in the UK and in North America to measure the Group's exposure to commodity price risk. Limits are also set on PaR and VaR measurements as a further control over exposure to market prices. PaR measures the estimated potential loss in a position or portfolio of positions associated with the movement of a commodity price for a given confidence level, over the remaining term of the position or contract portfolio. VaR measures the estimated potential loss for a given confidence level over a predetermined holding period. The standard confidence level used is 95%. In addition, stress tests are regularly performed to evaluate the impact of substantial movements in commodity prices.

The Group measures and manages the commodity price risk associated with the Group's entire energy procurement, upstream and downstream portfolio. Only certain of the Group's energy procurement, upstream and downstream contracts constitute financial instruments under IAS 39 (note 24).

As a result, while the Group manages the commodity price risk associated with both financial and non-financial energy procurement, upstream and downstream contracts, it is the notional value of energy contracts being carried at fair value that represents the exposure of the Group's energy procurement, upstream and downstream activities to commodity price risk according to IFRS 7, Financial Instruments: Disclosures. This is because energy contracts that are financial instruments under IAS 39 are accounted for on a fair value basis and changes in fair value immediately impact profit or equity. Conversely, energy contracts that are not financial instruments under IAS 39 are accounted for as executory contracts and changes in fair value do not immediately impact profit or equity, and as such, are not exposed to commodity price risk as defined by IFRS 7. So whilst the PaR or VaR associated with energy procurement and downstream contracts outside the scope of IAS 39 is monitored for internal risk management purposes, only those energy contracts within the scope of IAS 39 are within the scope of the IFRS 7 disclosure requirements.

(ii) Proprietary energy trading

The Group's proprietary energy trading activities consist of physical and financial commodity purchases and sales contracts taken on with the intent of benefiting in the short term from changes in market prices or differences between buying and selling prices. The Group conducts its trading activities in the over-the-counter market and through exchanges in the UK, North America and continental Europe. The Group is exposed to commodity price risk as a result of its proprietary energy trading activities because the value of its trading assets and liabilities will fluctuate with changes in market prices for commodities.

The Group sets volumetric and VaR limits to manage the commodity price risk exposure associated with the Group's proprietary energy trading activities. The VaR used measures the estimated potential loss for a 95% confidence level over a one-day holding period. The holding period used is based on market liquidity and the number of days the Group would expect it to take to close out a trading position. The VaR limits set for proprietary trading activities are relatively small compared to the Group's overall operations and are less than £5 million. The carrying value of energy contracts used in proprietary energy trading activities at 31 December 2011 is disclosed in note 24.

As with any modelled risk measure, there are certain limitations that arise from the assumptions used in the VaR analysis. VaR assumes that the future will behave like the past and that the Group's trading positions can be unwound or hedged within the predetermined holding period. Furthermore, the use of a 95% confidence level, by definition, does not take into account changes in value that might occur beyond this confidence level.

(b) Currency risk management

The Group is exposed to currency risk on foreign currency denominated forecast transactions, firm commitments, monetary assets and liabilities (transactional exposure) and on its net investments in foreign operations (translational exposure).

(i) Transactional currency risk

The Group is exposed to transactional currency risk on transactions denominated in currencies other than the underlying functional currency of the commercial operation transacting. The Group's primary functional currencies are pounds sterling in the UK, Canadian dollars in Canada, US dollars in the US, Norwegian kroner in Norway and euros in the Netherlands. The risk is that the functional currency value of cash flows will vary as a result of movements in exchange rates. Transactional exposure arises from the Group's energy procurement activities in the UK and in Canada, where a proportion of transactions are denominated in euros or US dollars and on certain capital commitments denominated in foreign currencies. In addition, in order to optimise the cost of funding, the Group has, in certain cases, issued foreign currency denominated debt, primarily in US dollars, New Zealand dollars, euros or Japanese yen.

(ii) Translational currency risk

The Group is exposed to translational currency risk as a result of its net investments in North America and Europe. The risk is that the pounds sterling value of the net assets of foreign operations will decrease with changes in foreign exchange rates. The Group's policy is to protect the pounds sterling book value of its net investments in foreign operations, subject to certain parameters monitored by the GFRMC, by holding foreign currency debt, entering into foreign currency derivatives, or a mixture of both.

The Group measures and manages the currency risk associated with all transactional and translational exposures. In contrast, IFRS 7 only requires disclosure of currency risk arising on financial instruments denominated in a currency other than the functional currency of the commercial operation transacting. As a result, for the purposes of IFRS 7, currency risk excludes the Group's net investments in North America and Europe as well as foreign currency denominated forecast transactions and firm commitments. A sensitivity analysis that is intended to illustrate the sensitivity of the Group's financial position and performance to changes in the fair value or future cash flows of foreign currency denominated financial instruments as a result of changes in foreign exchange rates is provided in note 25.

(c) Interest rate risk management

In the normal course of business the Group borrows to finance its operations. The Group is exposed to interest rate risk because the fair value of fixed rate borrowings and the cash flows associated with floating rate borrowings will fluctuate with changes in interest rates. The Group's policy is to manage the interest rate risk on long-term borrowings by ensuring the exposure to floating interest rates remains within a 30% to 70% range, including the impact of interest rate derivatives. A sensitivity analysis that is intended to illustrate the sensitivity of the Group's financial

SUPPLEMENTARY INFORMATION CONTINUED

S3. FINANCIAL RISK MANAGEMENT CONTINUED

position and performance to changes in interest rates is provided in note 25.

(d) Equity price risk management

The Group is exposed to equity price risk because certain available-for-sale financial assets, held by the Law Debenture Trust on behalf of the Company as security in respect of the Centrica Unapproved Pension Scheme, are linked to equity indices (note 29). Investments in equity indices are inherently exposed to less risk than individual equity investments because they represent a naturally diverse portfolio. Note 29 details the Group's other retirement benefit assets and liabilities.

(e) Sensitivity analysis

IFRS 7 requires disclosure of a sensitivity analysis that is intended to illustrate the sensitivity of the Group's financial position and performance to changes in market variables (commodity prices, foreign exchange rates and interest rates) as a result of changes in the fair value or cash flows associated with the Group's financial instruments. The sensitivity analysis provided discloses the effect on profit or loss and equity at 31 December 2011 assuming that a reasonably possible change in the relevant risk variable had occurred at 31 December 2011 and been applied to the risk exposures in existence at that date to show the effects of reasonably possible changes in price on profit or loss and equity to the next annual reporting date. Reasonably possible changes in market variables used in the sensitivity analysis are based on implied volatilities, where available, or historical data for energy prices and foreign exchange rates. Reasonably possible changes in interest rates are based on management judgement and historical experience.

The sensitivity analysis has been prepared based on 31 December 2011 balances and on the basis that the balances, the ratio of fixed to floating rates of debt and derivatives, the proportion of energy contracts that are financial instruments, the proportion of financial instruments in foreign currencies and the hedge designations in place at 31 December 2011 are all constant. Excluded from this analysis are all non-financial assets and liabilities and energy contracts that are not financial instruments under IAS 39. The sensitivity to foreign exchange rates relates only to monetary assets and liabilities denominated in a currency other than the functional currency of the commercial operation transacting, and excludes the translation of the net assets of foreign operations to pounds sterling, but includes the corresponding impact of financial instruments used in net investment hedges.

The sensitivity analysis provided is hypothetical only and should be used with caution as the impacts provided are not necessarily indicative of the actual impacts that would be experienced because the Group's actual exposure to market rates is changing constantly as the Group's portfolio of commodity, debt and foreign currency contracts changes. Changes in fair values or cash flows based on a variation in a market variable cannot be extrapolated because the relationship between the change in market variable and the change in fair value or cash flows may not be linear. In addition, the effect of a change in a particular market variable on fair values or cash flows is calculated without considering inter-relationships between the various market rates or mitigating actions that would be taken by the Group. The sensitivity analysis provided in note 25 excludes the impact of proprietary energy trading assets and liabilities because the VaR associated with the Group's proprietary energy trading activities is less than £5 million.

Credit risk management

Credit risk is the risk of loss associated with a counterparty's inability or failure to discharge its obligations under a contract. The Group is exposed to credit risk in its treasury, trading, energy procurement and downstream activities. The Group continues to take steps to tighten downstream credit policies, including the tightening of credit scores in customer management processes, whilst continuing to manage credit risk in accordance with financial risk management processes.

Note 25 provides further detail of the Group's exposure to credit risk on its financial assets.

(a) Treasury, trading and energy procurement activities

Wholesale counterparty credit exposures are monitored by individual counterparty and by category of credit rating, and are subject to approved limits. The majority of significant exposures are with counterparties rated A–/A3 or better. The Group uses master netting agreements to reduce credit risk and net settles payments with counterparties where net settlement provisions exist. In addition, the Group employs a variety of other methods to mitigate credit risk: margining, various forms of bank and parent company guarantees and letters of credit.

100% of the Group's credit risk associated with its treasury, trading and energy procurement activities is with counterparties in related energy industries or with financial institutions.

IFRS 7 requires disclosure of information about the exposure to credit risk arising from financial instruments only. Only certain of the Group's energy procurement contracts constitute financial instruments under IAS 39 (note 24). As a result, whilst the Group manages the credit risk associated with both financial and non-financial energy procurement contracts, it is the carrying value of financial assets within the scope of IAS 39 (note 24) that represents the maximum exposure to credit risk in accordance with IFRS 7.

(b) Downstream activities

In the case of business customers, credit risk is managed by checking a company's creditworthiness and financial strength both before commencing trade and during the business relationship. For residential customers, creditworthiness is ascertained normally before commencing trade to determine the payment mechanism required to reduce credit risk to an acceptable level. Certain customers will only be accepted on a prepayment basis or with a security deposit. In some cases, an ageing of receivables is monitored and used to manage the exposure to credit risk associated with both business and residential customers. In other cases, credit risk is monitored and managed by grouping customers according to method of payment or profile.

Liquidity risk management and going concern

Liquidity risk is the risk that the Group is unable to meet its financial obligations as they fall due. The Group experiences significant movements in its liquidity position due primarily to the seasonal nature of its business and margin cash arrangements associated with certain wholesale commodity contracts. To mitigate this risk the Group maintains significant committed facilities and holds cash on deposit. The Group's liquidity position has remained strong throughout 2011.

S4. OTHER EQUITY

Merger reserve

During February 1997, BG plc (formerly British Gas plc) demerged certain businesses (grouped together under GB Gas Holdings Limited (GBGH)) to form Centrica plc. Upon demerger, the share capital of GBGH was transferred to Centrica plc and was recorded at the nominal value of shares issued to BG plc shareholders. In accordance with the Companies Act 1985, no premium was recorded on the shares issued. On consolidation, the difference between the nominal value of the Company's shares issued and the amount of share capital and share premium of GBGH at the date of demerger was credited to a merger reserve.

Capital redemption reserve

In accordance with the Companies Act 1985, the Company transferred to the capital redemption reserve an amount equal to the nominal value of shares repurchased and subsequently cancelled (£16 million).

Revaluation reserve

During 2005, the revaluation of the Group's existing interest in Centrica SHB Limited to fair value, following the acquisition by the Group of the remaining 40% stake in the company, was recorded as a revaluation reserve adjustment. The remainder of the revaluation reserve relates to a 2009 revaluation of producing gas and oil assets located in Alberta, Canada, following the acquisition by the Group of additional interests.

Treasury shares reserve

Treasury shares reserve reflects the cost of shares in the Company held in share-based payment plans to meet future obligations to deliver shares to employees on vesting.

Share-based payments reserve

The share-based payments reserve reflects the obligation to deliver shares to employees under the Group's share schemes in return for services provided.

SUPPLEMENTARY INFORMATION CONTINUED

S5. SEGMENTAL ANALYSIS

The measure of profit used by the Centrica Executive Committee is adjusted operating profit. Adjusted operating profit is operating profit before exceptional items and certain re-measurements (refer to note 7), before additional depreciation resulting from any fair value uplifts on Strategic Investments (refer to notes 2 and 11) and including the results from joint ventures and associates which are included before interest and tax. All transactions between segments are on an arm's length basis.

Centrica's operating segments are those used internally by management to run the business and make decisions. Centrica's operating segments are based on products and services provided in each geographical area. The operating segments are also the Group's reportable segments. The types of products and services from which each reportable segment derives its revenues are:

Segment	Description
Downstream UK:	
Residential energy supply	The supply of gas and electricity to residential customers in the UK
Residential services	Installation, repair and maintenance of domestic central heating, plumbing and drains, gas appliances and kitchen appliances, including the provision of fixed-fee maintenance/breakdown service and insurance contracts in the UK
Business energy supply and services	The supply of gas and electricity and provision of energy-related services to business customers in the UK
Upstream UK:	
Gas	Production, processing, trading and optimisation of gas and oil and the development of new fields to grow reserves
Power	Generation, trading and optimisation of power from thermal, nuclear and wind sources
Storage UK	Gas storage in the UK
North America:	
Residential energy supply	The supply of gas and electricity to residential customers in North America
Business energy supply	The supply of gas, electricity and energy-related services to business customers in North America
Residential and business services	Installation and maintenance of Heating, Ventilation and Air Conditioning (HVAC) equipment, water heaters and the provision of breakdown services in North America
Upstream and wholesale energy	Gas production, power generation and procurement and trading activities in the North American wholesale energy markets

S6. PENSIONS

Pension schemes

The Registered Pensions Schemes are subject to independent valuations at least every three years, on the basis of which the qualified actuary certifies the rate of employer contributions which, together with the specified contributions payable by the employees and proceeds from the schemes' assets, are expected to be sufficient to fund the benefits payable under the schemes.

The latest full actuarial valuations were carried out at the following dates: the Registered Pensions Schemes at 31 March 2009, the Unapproved Pension Scheme at 6 April 2011 and the Direct Energy Marketing Limited pension plan at 31 December 2010. These have been updated to 31 December 2011 for the purposes of meeting the requirements of IAS 19. Investments have been valued for this purpose at market value.

Governance

The Registered Pension Schemes are managed by trustee companies whose boards consist of both company-nominated and member-nominated directors. Each scheme holds units in the Centrica Combined Common Investment Fund (CCCIF), which holds the combined assets of the participating schemes. The method of allocation of units is set out in the Trust Deed of the CCCIF. The board of CCCIF Limited is comprised of nine directors: three independent directors, three directors appointed by Centrica plc (including the chairman) and one director appointed by each of the three participating schemes. No direct investments are made in securities issued by Centrica plc or any of its subsidiaries, property leased to or owned by Centrica plc or any of its subsidiaries or securities of any fund manager or any of their associated companies.

Under the terms of the Pensions Act 2004, Centrica plc and each trustee board must agree the funding rate for its defined benefit pension scheme and a recovery plan to fund any deficit against the scheme-specific statutory funding objective. This approach was first adopted for the triennial valuations completed at 31 March 2006 and was again reflected in the 31 March 2009 valuations.

S7. SHARE SCHEMES

Long Term Incentive Scheme (LTIS)

Under the LTIS, allocations of shares in Centrica plc are reserved for employees at senior management level. The number of shares to be released to participants is calculated subject to the Company's total shareholder return (TSR) and earnings per share (EPS) growth during the three years following the grant date. Shares are released to participants immediately following the end of the period in which performance is assessed, however release of shares is subject to continued employment within the Group at the date of release. The vesting of half of each award is made on the basis of TSR performance and is valued using a Monte Carlo simulation model. The vesting of the remaining half of awards is dependent on EPS growth. This is a non-market condition and therefore the fair value of these awards is considered to be the market value at the grant date. The likelihood of achieving the performance conditions is taken into account in calculating the number of awards expected to vest.

Deferred and Matching Share Scheme (DMSS)

Awards under the DMSS are reserved for employees within the senior executive group. Under normal conditions the grant date of the scheme is the first day of each bonus year. This is followed by a vesting period of four years, being the bonus year plus a three-year performance period. The fair value of the award reflects the market value of the shares at the grant date. The scheme comprises three separate elements:

(a) Deferred shares

The scheme automatically requires participants to defer between 20% and 40% of their annual pre-tax bonus into the scheme. The shares are held in trust over the three-year performance period, during which time they cannot be withdrawn. An employee who leaves prior to the vesting date will forfeit their right to the shares (except where permitted by the rules of the scheme). All shares held in trust will be eligible to receive dividends.

(b) Investment shares

The scheme allows participants to elect to invest an additional amount of their annual bonus into the scheme up to a maximum of 50% of their total potential bonus for the year. This 50% limit includes the pre-tax amount automatically deferred each year. The shares may be funded directly from the employee and thus the shares do not attract an IFRS 2 charge. An employee who leaves prior to the vesting date will retain their investment shares.

(c) Matching shares

Deferred and investment shares will be matched with conditional matching shares, which will be released upon the achievement, over a three-year performance period, of three-year Group economic profit performance targets. Group economic profit is calculated by taking adjusted group operating profit (as defined in note 4) after tax and subtracting a charge for capital employed based on the Group's weighted average cost of capital. Further information on the operation of the DMSS and related performance conditions can be found on pages 58 to 60. The likelihood of achieving the performance conditions is taken into account in calculating the number of awards expected to vest. Estimates are made in year one and revised in subsequent years. An employee who leaves prior to the vesting date will forfeit their right to the shares (except where permitted by the rules of the scheme).

S8. FIXED-FEE SERVICE AND INSURANCE CONTRACTS

Fixed-fee service contracts are entered into with home services customers in the UK and home and business services customers in North America. These contracts continue until cancelled by either party to the maintenance element.

SUPPLEMENTARY INFORMATION CONTINUED

S8. FIXED-FEE SERVICE AND INSURANCE CONTRACTS CONTINUED

Insurance contracts are entered into with home service customers in the UK by British Gas Insurance Limited (BGIL), a fully owned subsidiary of Centrica plc, an entity regulated by the Financial Services Authority (FSA) since August 2009. Product offerings include central heating, boiler and controls, plumbing and drains and electrical appliance insurance cover. These contracts are normally for periods of 12-months with the option of renewal.

Fixed-fee service and insurance contracts protect purchasers of these contracts against the risk of breakdown of electrical, plumbing, heating, cooling and household appliances, resulting in the transfer of an element of risk from contract holders to BGIL. Benefits provided to customers vary in accordance with terms and conditions of the contracts entered into, however, generally include repair and/or replacement of the items affected.

The risk and level of service required within these contracts is dependent upon the occurrence of uncertain future events, in particular the number of call-outs, the cost per call-out and the nature of the fault. Accordingly, the timing and amount of future cash outflows related to the contracts is uncertain. The key terms and conditions that affect future cash flows are as follows:

- provision of labour and parts for repairs, dependent on the agreement and associated level of service;
- one safety and maintenance inspection either annually or in every continuous two-year period, as set out in the agreement;
- no limit to the number of call-outs to carry out repair work; and
- caps on certain maintenance and repair costs within fixed-fee service and insurance contracts.

Revenue from fixed-fee service and insurance contracts is recognised with regard to the incidence of risk over the life of the contract, reflecting the seasonal propensity of claims to be made under the contracts and the benefits receivable by the customer, which span the life of the contract as a result of emergency maintenance being available throughout the contract term. Cost of sales relates directly to the engineer workforce employed by Centrica within home services, the cost of which is accounted for over a 12-month period with adjustments made to reflect the seasonality of workload over a given year. The costs of claims under the fixed-fee service and insurance contracts will be the costs of the engineer workforce employed by Centrica within home services. These costs are accounted for over a 12-month period with adjustments made to reflect the seasonality of workload over a given year.

Weather conditions and the seasonality of maintenance can affect the number of call-outs, the cost per call-out and the nature of the fault. BGIL's obligations under the terms of home services fixed-fee service and insurance contracts are based on the number of breakdowns occurring within the contract period. BGIL actively manages the risk exposure of these uncertain events by undertaking the following risk mitigation activities:

- an initial service visit is performed for central heating care and insurance cover. If, at the initial visit, faults that cannot be rectified are identified, the fixed-fee service and insurance contract will be cancelled and no further cover provided;
- an annual or biennial safety and maintenance inspection is performed to ensure all issues are identified prior to them developing into significant maintenance or breakdown issues; and
- caps on certain maintenance and repair work are incorporated into fixed-fee service and insurance contracts to limit liability in areas considered to be higher risk in terms of prevalence and cost to repair.

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SUPPLEMENTARY INFORMATION CONTINUED

S9. PRINCIPAL UNDERTAKINGS

31 December 2011	Country of incorporation/formation	Percentage holding in ordinary shares and net assets	Principal activity
Subsidiary undertakings (i)			
Airtron Inc	USA	100	Home/commercial services
Bastrop Energy Partners LP	USA	100	Power generation
Brae Canada Ltd	Canada	100	Investment company
British Gas Energy Services Limited	England	100	Building services
British Gas Insurance Limited	England	100	Insurance provision
British Gas Services Limited	England	100	Residential services
British Gas Trading Limited	England	100	Energy supply
Centrica Barry Limited	England	100	Power generation
Centrica Brigg Limited	England	100	Power generation
Centrica Energy Limited (ii)	England	100	Wholesale energy trading
Centrica Energy (Trading) Limited (iii)	England	100	Proprietary energy trading
Centrica KL Limited	England	100	Power generation
Centrica KPS Limited	England	100	Power generation
Centrica Langage Limited	England	100	Power generation
Centrica LNG Company Limited	England	100	Energy supply
Centrica North Sea Gas Limited (iv)	Scotland	100	Gas and oil production
Centrica North Sea Oil Limited (v)	Scotland	100	Gas and oil production
Centrica Norway Limited	England	100	Gas and oil exploration and production
Centrica PB Limited	England	100	Power generation
Centrica Production Nederland B.V.	Netherlands	100	Gas and oil exploration and production
Centrica Resources Limited	England	100	Gas and oil exploration and production
Centrica RPS Limited	England	100	Power generation
Centrica SHB Limited	England	100	Power generation
Centrica Storage Limited	England	100	Gas storage
Clockwork Inc (vi)	USA	100	Home services
CPL Retail Energy LP	USA	100	Energy supply
Direct Energy LP	USA	100	Energy supply
Direct Energy Business LLC	USA	100	Energy supply
Direct Energy Marketing Inc	USA	100	Wholesale energy trading
Direct Energy Marketing Limited	Canada	100	Energy supply and home services
Direct Energy Partnership	Canada	100	Energy supply
Direct Energy Resources Partnership	Canada	100	Gas production
Direct Energy Services LLC	USA	100	Energy supply and home services
Direct Energy US Home Services Inc	USA	100	Home/commercial services
Dyno Holdings Limited	England	100	Home services
Energy America LLC	USA	100	Energy supply
FCP Enterprises Inc (vii)	USA	100	Energy supply
Frontera Generation LP	USA	100	Power generation
Gateway Energy Services Corporation (viii)	USA	100	Energy supply
GB Gas Holdings Limited	England	100	Holding company
Hydrocarbon Resources Limited	England	100	Gas production
Paris Generation LP	USA	100	Power generation
Vectren Retail LLC (viii)	USA	100	Energy supply
WTU Retail Energy LP	USA	100	Energy supply

(i) All principal undertakings are held indirectly by the Company. The information is only given for those subsidiaries which in the Directors' opinion principally affect the figures shown in the Financial Statements.
(ii) Previously called Accord Energy Limited.
(iii) Previously called Accord Energy (Trading) Limited.
(iv) Previously called Venture North Sea Gas Limited.
(v) Previously called Venture North Sea Oil Limited.
(vi) Holding company for the Clockwork group of companies.
(vii) Holding company for the First Choice Power group of companies acquired in 2011.
(viii) Acquired in 2011.

The principal joint ventures and associate investments held by the Group are disclosed in note 16.

A full list of related undertakings is included in the Company's Annual Return submitted to the Registrar of Companies.

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF CENTRICA PLC

We have audited the parent Company Financial Statements of Centrica plc for the year ended 31 December 2011 which comprise the Company Balance Sheet and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice).

RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITORS

As explained more fully in the Directors' Responsibility Statement set out on page 51 the Directors are responsible for the preparation of the parent Company Financial Statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the parent Company Financial Statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the Company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

SCOPE OF THE AUDIT OF THE FINANCIAL STATEMENTS

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the parent Company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Directors; and the overall presentation of the Financial Statements. In addition, we read all the financial and non-financial information in the Annual Report and Accounts to identify material inconsistencies with the audited Financial Statements. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

OPINION ON FINANCIAL STATEMENTS

In our opinion the parent Company Financial Statements:

- give a true and fair view of the state of the Company's affairs as at 31 December 2011;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

OPINION ON OTHER MATTERS PRESCRIBED BY THE COMPANIES ACT 2006

In our opinion:

- the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006; and
- the information given in the Directors' Report for the financial year for which the parent Company Financial Statements are prepared is consistent with the parent Company Financial Statements.

MATTERS ON WHICH WE ARE REQUIRED TO REPORT BY EXCEPTION

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept by the parent Company, or returns adequate for our audit have not been received from branches not visited by us; or
- the parent Company Financial Statements and the part of the Directors' Remuneration Report to be audited are not in agreement with the accounting records and returns; or
- certain disclosures of Directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

OTHER MATTER

We have reported separately on the Group Financial Statements of Centrica plc for the year ended 31 December 2011.

John Maitland
Senior Statutory Auditor
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
London
23 February 2012

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COMPANY BALANCE SHEET

31 December	Notes	2011 £m	2010 £m
Fixed assets			
Tangible assets	III	**64**	38
Investments in subsidiary undertakings	IV	**2,154**	2,132
		2,218	2,170
Current assets			
Debtors	V	**10,522**	10,134
Current asset investments	VI	**181**	266
Cash at bank and in hand		**164**	93
		10,867	10,493
Creditors (amounts falling due within one year)			
Borrowings	VII	**(454)**	(50)
Other creditors	VIII	**(5,695)**	(5,606)
		(6,149)	(5,656)
Net current assets		**4,718**	4,837
Total assets less current liabilities		**6,936**	7,007
Creditors (amounts falling due after more than one year)			
Borrowings	VII	**(3,361)**	(3,622)
Other creditors	VIII	**(92)**	(69)
		(3,453)	(3,691)
Provisions for liabilities	IX	**(16)**	(6)
Net assets		**3,467**	3,310
Capital and reserves – equity interests			
Share capital	X	**319**	318
Share premium	X	**874**	833
Capital redemption reserve	X	**16**	16
Profit and loss account	X	**2,258**	2,143
Shareholders' funds	X	**3,467**	3,310

The Financial Statements on pages 124 to 128 were approved and authorised for issue by the Board of Directors on 23 February 2012 and were signed on its behalf by:

Sam Laidlaw
Chief Executive

Nick Luff
Group Finance Director

The notes on pages 125 to 128 form part of these Financial Statements, along with notes 26 and 32 to the Group Financial Statements.

NOTES TO THE COMPANY BALANCE SHEET

I. PRINCIPAL ACCOUNTING POLICIES OF THE COMPANY

Basis of preparation

The Company Balance Sheet has been prepared in accordance with applicable UK Accounting Standards consistently applied and under the Companies Act 2006. The accounts have been prepared under the going concern basis. No profit and loss account is presented for the Company as permitted by the Companies Act 2006. The Company profit after tax for the year was £899 million (2010: £361 million loss).

Presentation of derivative financial instruments

In line with the Group's accounting policy for derivative financial instruments, the Company has classified those derivatives held for the purpose of treasury management as current or non-current, based on expected settlement dates.

Employee share schemes

The Group has a number of employee share schemes under which it makes equity-settled share-based payments to certain employees. The material schemes are described in note 32 of the Group Financial Statements. Equity-settled share-based payments are measured at fair value at the date of grant (excluding the effect of non-market-based vesting conditions). The fair value determined at the grant date is expensed on a straight-line basis together with a corresponding increase in equity over the vesting period, based on the Group's estimate of the number of awards that will vest and adjusted for the effect of non-market-based vesting conditions. The issue of share incentives by the Company to employees of its subsidiaries represents additional capital contributions. The addition to the Company's investment in subsidiary undertakings is reduced following the recharge of the associated costs to the subsidiaries.

Fair value is measured using methods appropriate to each of the different schemes as follows:

LTIS – EPS award	Market value on the date of grant
LTIS – TSR award	A Monte Carlo simulation to predict the total shareholder return performance
SAS and DMSS	Market value on the date of grant

Foreign currencies

Transactions in foreign currencies are translated at the rate of exchange ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated into pounds sterling at closing rates of exchange. Exchange differences on monetary assets and liabilities and transactions are taken to the Profit and Loss Account.

Tangible fixed assets

Tangible fixed assets are included in the Balance Sheet at cost, less accumulated depreciation and any provisions for impairment. Cost includes the original purchase price of the asset and the cost attributable to bringing it to its working condition for its intended use. Tangible fixed assets are depreciated on a straight-line basis at rates sufficient to write off the cost, less estimated residual values, of individual assets over their estimated useful lives of up to ten years.

Leases

Rentals under operating leases are charged to the Profit and Loss Account on a straight-line basis.

Investments

Fixed asset investments are held in the Balance Sheet at cost, less any provision for impairment as necessary. Current asset investments are stated at the lower of cost and net realisable value.

Pensions and other post-employment benefits

The Company's employees participate in a number of the Group's defined benefit pension schemes as described in note 29 to the Group Financial Statements. The Company is unable to identify its share of the underlying assets and liabilities in the schemes on a consistent and reasonable basis and therefore accounts for the schemes as if they were defined contribution schemes. The charge to the Profit and Loss Account is equal to the contributions payable to the schemes in the accounting period. Details of the defined benefit schemes of the Group (accounted for in accordance with the Group's accounting policies detailed in note S2 in the Supplementary Information section of the Group Financial Statements) can be found in note 29 to the Group Financial Statements.

Taxation

Current tax, including UK corporation tax, is provided at amounts expected to be paid (or recovered) using the tax rates and laws that have been enacted or substantively enacted by the balance sheet date.

Deferred tax is recognised in respect of all timing differences that have originated, but not reversed, at the balance sheet date where transactions or events that result in an obligation to pay more tax in the future, or a right to pay less tax in the future, have occurred at the balance sheet date. Timing differences are differences between the Group's taxable profits and its results as stated in the Financial Statements that arise from the inclusion of gains and losses in tax assessments in periods different from those in which they are recognised in the Financial Statements.

A deferred tax asset is regarded as recoverable and therefore recognised only when, on the basis of all available evidence, it can be regarded as more likely than not that there will be suitable taxable profits in the foreseeable future from which the reversal of the underlying timing differences can be deducted.

Deferred tax is measured at the average tax rates that are expected to apply in the periods in which the timing differences are expected to reverse, based on tax rates and laws that have been enacted or substantively enacted by the balance sheet date. Deferred tax is measured on an undiscounted basis.

Financial instruments and borrowings

The Company's accounting policies for financial instruments and borrowings are consistent with those of the Group, and are disclosed in note S2. The Company's financial risk management policies are consistent with those of the Group and are described in the Directors' Report – Governance on pages 49 to 51 and in note S3.

The Company is exempted by FRS 29 from providing detailed disclosures in respect of its financial instruments because the Company is included within the Group's consolidated Financial Statements and its financial instruments are incorporated into the disclosures in the notes to the Group Financial Statements.

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NOTES TO THE COMPANY BALANCE SHEET CONTINUED

II. DIRECTORS AND EMPLOYEES

Details of Directors' remuneration, share-based payments and pension entitlements in the Remuneration Report on pages 52 to 63 form part of these Financial Statements. Details of material employee share-based payments are given in note 32. Details of the remuneration of key management personnel are given in note 35.

III. TANGIBLE ASSETS

	2011 Plant, equipment and vehicles £m	2010 Plant, equipment and vehicles £m
Cost		
1 January	**111**	101
Additions	**44**	11
Disposals	**(3)**	(1)
31 December	**152**	111
Accumulated Depreciation		
1 January	**73**	62
Charge for the year	**17**	12
Disposals	**(2)**	(1)
31 December	**88**	73
NBV at 31 December	**64**	38

IV. INVESTMENTS IN SUBSIDIARY UNDERTAKINGS

	2011 Investments in subsidiaries' shares £m	2010 Investments in subsidiaries' shares £m
Cost		
1 January	**2,132**	2,122
Additions and disposals (i)	**22**	10
31 December	**2,154**	2,132

(i) Additions and disposals represent the net change in shares to be issued under employee share schemes in Group undertakings. Direct investments are held in Centrica Holdings Limited, Centrica Trading Limited and Centrica Beta Holdings Limited, all of which are incorporated in England. Principal undertakings are listed in note S9. The Directors believe that the carrying value of the investments is supported by their underlying net assets.

V. DEBTORS

	2011 Due within one year £m	2011 Due after more than one year £m	2011 Total £m	2010 Due within one year £m	2010 Due after more than one year £m	2010 Total £m
Amounts owed by Group undertakings	10,304	8	**10,312**	9,947	–	9,947
Derivative financial instruments (i)	8	175	**183**	5	151	156
Other debtors	3	–	**3**	6	–	6
Prepayments and other accrued income	13	11	**24**	14	11	25
	10,328	**194**	**10,522**	9,972	162	10,134

(i) Derivative financial instruments comprise foreign currency derivatives held for trading of £3 million (2010: £36 million), interest rate derivatives held for trading of £nil (2010: £3 million), interest rate derivatives held for hedging of £157 million (2010: £105 million) and foreign currency derivatives held for hedging of £22 million (2010: £12 million). The fair value of these derivatives is equivalent to the carrying value.

NOTES TO THE COMPANY BALANCE SHEET CONTINUED

VI. CURRENT ASSET INVESTMENTS

	2011 £m	2010 £m
Short-term investments	**181**	266

£54 million (2010: £54 million) of investments were held by the Law Debenture Trust, on behalf of the Company, as security in respect of the Centrica Unapproved Pension Scheme (refer to note 29 of the Group Financial Statements).

VII. BORROWINGS

	2011		2010	
Amounts falling due	**Within one year £m**	**After one year £m**	Within one year £m	After one year £m
Bank loans and overdrafts	**49**	**192**	50	215
Commercial paper	**114**	**–**	–	–
Bonds	**291**	**3,169**	–	3,407
	454	**3,361**	50	3,622

The Company's financial instruments and related disclosures are included within the consolidated Group Financial Statements. As permitted by FRS 29, Financial Instruments: Disclosures, further detailed disclosure in respect of the Company's financial instruments is not included. Disclosures in respect of the Group's borrowings are provided in note 12 to the Group Financial Statements.

VIII. OTHER CREDITORS

	2011		2010	
	Due within one year £m	**Due after more than one year £m**	Due within one year £m	Due after more than one year £m
Trade creditors	**44**	**–**	13	–
Amounts owed to Group undertakings	**5,582**	**–**	5,502	4
Derivative financial instruments (i)	**5**	**92**	27	65
Taxation and social security	**4**	**–**	4	–
Accruals and deferred income	**60**	**–**	60	–
	5,695	**92**	5,606	69

(i) Derivative financial instruments comprise foreign currency derivatives held for trading of £5 million (2010: £76 million), interest rate derivatives held for trading of £86 million (2010: £16 million) and interest rate derivatives held for hedging of £6 million (2010: £nil). The fair value of these derivatives is equivalent to the carrying value.

IX. PROVISIONS FOR LIABILITIES

	1 January 2011 £m	Profit and loss charge £m	Utilised in the year £m	Reserves movements £m	**31 December 2011 £m**
Other provisions	6	18	(8)	–	**16**
Deferred tax	–	(1)	–	1	**–**
	6	17	(8)	1	**16**

Potential unrecognised deferred corporation tax assets amounted to £11 million (2010: £3 million), primarily relating to other timing differences. Other provisions principally represent estimated liabilities for contractual settlements, business restructuring and National Insurance in respect of employee share scheme liabilities. The National Insurance provision was based on a share price of 289 pence at 31 December 2011 (2010: 331 pence). The majority of the amounts are expected to be utilised by 2015.

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NOTES TO THE COMPANY BALANCE SHEET CONTINUED

X. SHAREHOLDERS' FUNDS AND RESERVES

	Profit and loss account									
	Cash flow hedging reserve £m	Treasury shares £m	Share-based payments reserve £m	Retained earnings £m	**Profit and loss account £m**	Share capital £m	Share premium £m	Capital redemption reserve £m	**2011 Total £m**	2010 Total £m
1 January 2011	1	(22)	78	2,086	**2,143**	318	833	16	**3,310**	4,290
Profit for the year (i)	–	–	–	899	**899**	–	–	–	**899**	(361)
Losses on revaluation of cash flow hedges (net of taxation)	(27)	–	–	–	**(27)**	–	–	–	**(27)**	(1)
Dividends	–	–	–	(762)	**(762)**	–	–	–	**(762)**	(668)
Employee share schemes:										
Increase in treasury shares	–	(19)	–	–	**(19)**	–	–	–	**(19)**	(20)
Value of services provided	–	–	40	–	**40**	–	–	–	**40**	48
Exercise of awards	–	22	(28)	(9)	**(15)**	–	–	–	**(15)**	(37)
Gains on revaluation of available-for-sale securities (net of taxation)	–	–	–	(1)	**(1)**	–	–	–	**(1)**	3
Share issue	–	–	–	–	**–**	1	41	–	**42**	56
Net movement for the financial year	**(27)**	**3**	**12**	**127**	**115**	**1**	**41**	**–**	**157**	(980)
31 December 2011	**(26)**	**(19)**	**90**	**2,213**	**2,258**	**319**	**874**	**16**	**3,467**	3,310

(i) As permitted by section 408(3) of the Companies Act 2006, no profit and loss account is presented. The Company's profit for the year was £899 million (2010: loss of £361 million) before dividends paid of £762 million (2010: £668 million).

The Directors propose a final dividend of 11.11 pence per share (totalling £575 million) for the year ended 31 December 2011. The dividend will be submitted for formal approval at the Annual General Meeting to be held on 11 May 2012. These Financial Statements do not reflect this dividend payable, which will be accounted for in shareholders' equity as an appropriation of retained earnings in the year ending 31 December 2012.

Details of the Company's share capital are provided in the Group Statement of Changes in Equity and note 26 to the Group Financial Statements.

XI. COMMITMENTS

At 31 December 2011, the Company had commitments of £171 million (2010: £205 million) relating to contracts with outsource service providers. At 31 December 2011, lease commitments over land and buildings included non-cancellable operating lease payments due under one year of £1 million (2010: £1 million), within one to five years of £1 million (2010: £1 million) and guaranteed operating commitments of a subsidiary undertaking of £7 million (2010: £7 million).

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GAS AND LIQUIDS RESERVES (UNAUDITED)

The Group's estimates of reserves of gas and liquids are reviewed as part of the half-year and full-year reporting process and updated accordingly. A number of factors affect the volumes of gas and liquids reserves, including the available reservoir data, commodity prices and future costs. Due to the inherent uncertainties and the limited nature of reservoir data, estimates of reserves are subject to change as additional information becomes available.

The Group discloses 2P gas and liquids reserves, representing the central estimate of future hydrocarbon recovery. Reserves for Centrica-operated fields are estimated by in-house technical teams composed of geoscientists and reservoir engineers. Reserves for non-operated fields are estimated by the operator, but are subject to internal review and challenge.

As part of the internal control process related to reserves estimation, an assessment of the reserves, including the application of the reserves definitions is undertaken by an independent technical auditor. An annual reserves assessment has been carried out by DeGoyler and MacNaughton for the Group's global reserves. Reserves are estimated in accordance with a formal policy and procedure standard.

The Group has estimated 2P gas and liquids reserves in Europe, North America and Trinidad and Tobago.

The principal fields in UK Upstream are South Morecambe, Cygnus, Statfjord, Chiswick, NCMA Poinsettia, Ensign, York, Olympus, Grove and Kew fields associated with Upstream UK, and the Rough field associated with Storage UK. The European and Trinidad and Tobago reserves estimates are consistent with the guidelines and definitions of the Society of Petroleum Engineers, the Society of Petroleum Evaluation Engineers and the World Petroleum Council's Petroleum Resources Management System using accepted principles.

The principal fields in North America are Foothills, Medicine Hat, Entice and Central Alberta located in the province of Alberta, Canada. The North American reserves estimates have been evaluated in accordance with the Canadian Oil and Gas Evaluation Handbook (COGEH) reserves definitions and are consistent with the guidelines and definitions of the Society of Petroleum Engineers and the World Petroleum Council.

Estimated net 2P reserves of gas (billion cubic feet)	Europe	Trinidad and Tobago (iv)	**UK Upstream**	North America	**Total**
1 January 2011	2,026	161	**2,187**	538	**2,725**
Revisions of previous estimates (i)	8	15	**23**	58	**81**
Purchases/(disposals) of reserves in place (ii)	–	–	**–**	43	**43**
Extensions, discoveries and other additions (iii)	199	–	**199**	20	**219**
Production (v)	(193)	(15)	**(208)**	(56)	**(264)**
31 December 2011	**2,040**	**161**	**2,201**	**603**	**2,804**

Estimated net 2P reserves of liquids (million barrels)	Europe	Trinidad and Tobago (iv)	**UK Upstream**	North America	**Total**
1 January 2011	64	5	**69**	6	**75**
Revisions of previous estimates (i)	8	–	**8**	2	**10**
Purchases/(disposals) of reserves in place	–	(5)	**(5)**	–	**(5)**
Extensions, discoveries and other additions (iii)	14	–	**14**	1	**15**
Production (v)	(13)	–	**(13)**	(1)	**(14)**
31 December 2011	**73**	**–**	**73**	**8**	**81**

Estimated net 2P reserves (million barrels of oil equivalent)	Europe	Trinidad and Tobago (iv)	**UK Upstream**	North America	**Total**
31 December 2011 (vi)	**413**	**27**	**440**	**109**	**549**

(i) Includes minor reserves revisions to a number of fields in Europe, North America and Trinidad and Tobago.
(ii) Reflects the acquisition of additional equity in the Foothills properties in North America.
(iii) Recognition of reserves predominantly associated with Chiswick, Olympus, Grove, Kew and Foothills.
(iv) The Trinidad and Tobago reserves are subject to a production sharing contract and accordingly have been stated on an entitlement basis (including tax barrels).
(v) Represents total gas and oil produced from the Group's reserves.
(vi) Includes the total of estimated gas and liquid reserves at 31 December 2011 in million barrels of oil equivalent.

Liquids reserves include oil, condensate and natural gas liquids.

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FIVE YEAR RECORD

Year ended 31 December	2007 (restated) (i) (iii) £m	2008 (restated) (i) (ii) (iii) £m	2009 £m	2010 £m	2011 £m
Group revenue from continuing operations (i) (iii)	15,893	20,872	21,963	22,423	**22,824**
Operating profit from continuing operations before exceptional items and certain re-measurements:					
Downstream UK	840	712	1,011	1,216	**1,005**
Upstream UK	663	881	525	771	**1,023**
Storage UK	240	195	168	169	**75**
North America	187	215	153	234	**312**
Adjusted operating profit – operating profit before exceptional items, certain re-measurements and impact from fair value uplifts from Strategic Investments	1,930	2,003	1,857	2,390	**2,415**
Share of joint ventures' and associates' interest and taxation	(2)	(3)	(11)	(78)	**(102)**
Other	1	(8)	(5)	–	**–**
Depreciation of fair value uplifts to property, plant and equipment (iv)	–	–	(27)	(118)	**(105)**
	1,929	1,992	1,814	2,194	**2,208**
Operating profit/(loss) from discontinued operations:					
European operations (v)	20	(52)	105	(2)	**13**
The Consumers' Waterheater Income Fund (vi)	39	–	–	–	**–**
Exceptional items and certain re-measurements after taxation	383	(1,048)	(288)	726	**(844)**
Profit/(loss) attributable to equity holders of the parent	1,505	(137)	844	1,935	**421**

	Pence	Pence	Pence	Pence	Pence
Earnings/(loss) per ordinary share (ii)	36.5	(3.3)	16.5	37.6	**8.2**
Adjusted earnings per ordinary share (ii) (vii) (viii)	27.2	21.7	21.7	25.2	**25.8**
Dividend per share declared in respect of the year (ix)	11.6	12.2	12.8	14.3	**15.4**

Assets and liabilities At 31 December	2007 (restated) (ii) (x) £m	2008 (restated) (ii) (x) £m	2009 £m	2010 £m	2011 £m
Goodwill and other intangible assets	1,539	2,181	2,822	3,454	**3,739**
Other non-current assets	4,942	6,341	9,650	9,815	**10,234**
Net current assets/(liabilities)	747	2,163	330	283	**(674)**
Non-current liabilities	(3,868)	(6,313)	(8,675)	(7,820)	**(7,699)**
Net assets of disposal groups held for sale	–	–	128	87	**–**
Net assets	3,360	4,372	4,255	5,819	**5,600**
Debt, net of cash, cash equivalents and securities:					
Net debt (excluding non-recourse debt)	(795)	(511)	(3,136)	(3,312)	**(3,435)**

Cash flows Year ended 31 December	2007 (restated) (xi) £m	2008 (restated) (xi) £m	2009 (restated) (xi) £m	2010 (restated) (xi) £m	2011 £m
Cash flow from operating activities before exceptional payments (xi)	2,343	279	2,430	2,651	**2,531**
Payments relating to exceptional charges	(90)	(74)	(203)	(223)	**(194)**
Net cash flow from investing activities (xi)	(860)	(1,030)	(4,100)	(1,584)	**(1,400)**
Cash flow before cash flow from financing activities	1,393	(825)	(1,873)	844	**937**

(i) Group revenue and cost of sales have been restated to report gas sales revenue of Centrica Storage net of cost of sales, to better reflect the nature of the transactions.
(ii) Restated to capitalise borrowing costs on the adoption of IAS 23 (Amendment) and to reflect the change in British Gas Services Limited's revenue recognition policy.
(iii) Restated to present the European Energy segment, with the exception of the Group's operations in Germany, as a discontinued operation. The operating profit of the Group's operations in Germany is reported within Upstream. Also restated to include the operating profit of joint ventures and associates pre-interest and tax.
(iv) The depreciation of British Energy fair value uplifts is shown net of taxation.
(v) Discontinued in 2009.
(vi) Discontinued in 2007.
(vii) Adjusted earnings per ordinary share excludes depreciation of fair value uplifts to PP&E from Strategic Investments after taxation and certain re-measurements and exceptional items.
(viii) Figures for 2007 have been adjusted to reflect the bonus element of a Rights Issue undertaken during 2008.
(ix) Figures for 2007 and 2008 have been adjusted to reflect the bonus element of a Rights Issue undertaken during 2008.
(x) Restated to classify the non-current portions of derivative financial instruments from current assets and liabilities to non-current assets and liabilities.
(xi) The 2007-2010 comparatives have been restated for a change in presentation of emission certificate/allowance cash flows. See note 1(d).

Independent Auditors' Report to the members of Centrica plc

We have audited the Group Financial Statements of Centrica plc for the year ended 31 December 2010 which comprise the Group Income Statement, the Group Statement of Comprehensive Income, the Group Balance Sheet, the Group Statement of Changes in Equity, the Group Cash Flow Statement and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

Respective responsibilities of Directors and auditors

As explained more fully in the Directors' Responsibilities Statement set out on page 48, the Directors are responsible for the preparation of the Group Financial Statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the Group Financial Statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the Company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

Scope of the audit of the Financial Statements

An audit involves obtaining evidence about the amounts and disclosures in the Financial Statements sufficient to give reasonable assurance that the Financial Statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Group's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Directors; and the overall presentation of the Financial Statements.

Opinion on Financial Statements

In our opinion the Group Financial Statements:

- give a true and fair view of the state of the Group's affairs as at 31 December 2010 and of its profit and cash flows for the year then ended;
- have been properly prepared in accordance with IFRSs as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006 and Article 4 of the IAS Regulation.

Opinion on other matter prescribed by the Companies Act 2006

In our opinion the information given in the Directors' Report for the financial year for which the Group Financial Statements are prepared is consistent with the Group Financial Statements.

Matters on which we are required to report by exception

We have nothing to report in respect of the following:

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- certain disclosures of Directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

Under the Listing Rules we are required to review:

- the Directors' statement, set out on page 48, in relation to going concern;
- the part of the Corporate Governance Report relating to the Company's compliance with the nine provisions of the June 2008 Combined Code specified for our review; and
- certain elements of the report to shareholders by the Board on directors' remuneration.

Other matter

We have reported separately on the parent Company Financial Statements of Centrica plc for the year ended 31 December 2010 and on the information in the Directors' Remuneration Report that is described as having been audited.

John Maitland
(Senior Statutory Auditor)
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
London
24 February 2011

Year ended 31 December	Notes	2010 Business performance £m	2010 Exceptional items and certain re-measurements £m	2010 Results for the year £m	2009 Business performance £m	2009 Exceptional items and certain re-measurements £m	2009 Results for the year £m
Group revenue	6	**22,423**	**–**	**22,423**	21,963	–	21,963
Cost of sales before exceptional items and certain re-measurements	7	**(17,595)**	**–**	**(17,595)**	(17,663)	–	(17,663)
Exceptional items	9	**–**	**(102)**	**(102)**	–	(393)	(393)
Re-measurement of energy contracts	9	**–**	**1,177**	**1,177**	–	(62)	(62)
Cost of sales	7	**(17,595)**	**1,075**	**(16,520)**	(17,663)	(455)	(18,118)
Gross profit		**4,828**	**1,075**	**5,903**	4,300	(455)	3,845
Operating costs before exceptional items	7	**(2,641)**	**–**	**(2,641)**	(2,496)	–	(2,496)
Exceptional items	9	**–**	**(181)**	**(181)**	–	(175)	(175)
Operating costs		**(2,641)**	**(181)**	**(2,822)**	(2,496)	(175)	(2,671)
Share of profits/(losses) in joint ventures and associates, net of interest and taxation	9, 19	**7**	**(14)**	**(7)**	10	(9)	1
Group operating profit	6	**2,194**	**880**	**3,074**	1,814	(639)	1,175
Interest income	10	**214**	**–**	**214**	307	–	307
Interest expense	10	**(479)**	**–**	**(479)**	(486)	–	(486)
Net interest expense	10	**(265)**	**–**	**(265)**	(179)	–	(179)
Profit/(loss) from continuing operations before taxation		**1,929**	**880**	**2,809**	1,635	(639)	996
Taxation on profit/(loss) from continuing operations	11	**(708)**	**(221)**	**(929)**	(531)	185	(346)
Profit/(loss) from continuing operations after taxation		**1,221**	**659**	**1,880**	1,104	(454)	650
Profit/(loss) from discontinued operations	9, 38	**(8)**	**67**	**59**	40	(131)	(91)
Gain on disposal of discontinued operations	9, 38	**3**	**–**	**3**	–	297	297
Discontinued operations	38	**(5)**	**67**	**62**	40	166	206
Profit/(loss) for the year		**1,216**	**726**	**1,942**	1,144	(288)	856
Attributable to:							
Equity holders of the parent		**1,209**	**726**	**1,935**	1,094	(250)	844
Non-controlling interests	33	**7**	**–**	**7**	50	(38)	12
		1,216	**726**	**1,942**	1,144	(288)	856

Earnings per ordinary share	Notes	2010 Pence	2009 Pence
From continuing and discontinued operations:			
Basic	14	**37.6**	16.5
Diluted	14	**37.3**	16.4
From continuing operations:			
Basic	14	**36.4**	12.7
Diluted	14	**36.1**	12.6
Interim dividend paid per ordinary share	12	**3.84**	3.66
Final dividend proposed per ordinary share	12	**10.46**	9.14

The notes on pages 71 to 141 form part of these Financial Statements.

Year ended 31 December	Notes	2010 £m	2009 £m
Profit for the year		**1,942**	856
Other comprehensive (losses)/income:			
(Losses)/gains on revaluation of available-for-sale securities	31	**(4)**	11
Taxation on revaluation of available-for-sale securities	31	**(1)**	(2)
		(5)	9
Unrealised gains/(losses) on cash flow hedges	31	**10**	(253)
Transferred to income and expense on cash flow hedges	31	**236**	234
Transferred to assets and liabilities on cash flow hedges	31	**19**	(4)
Recycling of foreign exchange gains on cash flow hedges on disposal of business	31	**9**	10
Exchange differences on cash flow hedges	31	**(8)**	–
Taxation on cash flow hedges	31	**(79)**	(12)
		187	(25)
Exchange differences on translation of foreign operations	31	**70**	83
Recycling of foreign exchange loss on disposal of business	31	**(1)**	(10)
Taxation on related exchange differences	31	**14**	(41)
		83	32
Actuarial losses on defined benefit pension schemes	31	**(9)**	(805)
Actuarial gain on defined benefit schemes of discontinued operations	31	**–**	2
Exchange loss on translation of actuarial reserve	31	**(1)**	–
Taxation on actuarial losses on defined benefit pension schemes	31	**(2)**	241
		(12)	(562)
Share of joint ventures/associates actuarial gain (post tax)	19	**14**	–
Share of joint ventures/associates cash flow hedge reserve gain (post tax)	19	**1**	–
		15	–
Other comprehensive income/(loss), net of taxation		**268**	(546)
Total comprehensive income for the year		**2,210**	310
Attributable to:			
Equity holders of the parent		**2,203**	297
Non-controlling interests	33	**7**	13
		2,210	310

The notes on pages 71 to 141 form part of these Financial Statements.

31 December	Notes	2010 £m	2009 £m
Non-current assets			
Goodwill	15	**2,370**	2,088
Other intangible assets	16	**1,084**	734
Property, plant and equipment	18	**6,398**	6,059
Interests in joint ventures and associates	19	**2,507**	2,422
Deferred tax assets	27	**238**	534
Trade and other receivables	21	**97**	143
Derivative financial instruments	22	**341**	316
Securities	29	**234**	176
		13,269	12,472
Current assets			
Inventories	20	**344**	382
Current tax assets	27	**81**	69
Trade and other receivables	21	**4,187**	4,181
Derivative financial instruments	22	**449**	492
Securities	29	**23**	74
Cash and cash equivalents	24	**467**	1,294
		5,551	6,492
Assets of disposal groups classified as held for sale	38	**455**	478
Total assets		**19,275**	19,442
Current liabilities			
Trade and other payables	25	**(4,059)**	(3,955)
Current tax liabilities		**(182)**	(184)
Bank overdrafts, loans and other borrowings	26	**(77)**	(86)
Derivative financial instruments	22	**(755)**	(1,744)
Provisions for other liabilities and charges	28	**(195)**	(193)
		(5,268)	(6,162)
Net current assets		**283**	330
Non-current liabilities			
Trade and other payables	25	**(56)**	(82)
Bank overdrafts, loans and other borrowings	26	**(3,959)**	(4,594)
Derivative financial instruments	22	**(648)**	(1,006)
Deferred tax liabilities	27	**(1,367)**	(1,179)
Retirement benefit obligations	36	**(239)**	(565)
Provisions for other liabilities and charges	28	**(1,551)**	(1,249)
		(7,820)	(8,675)
Liabilities of disposal groups classified as held for sale	38	**(368)**	(350)
Net assets		**5,819**	4,255
Equity			
Called up share capital	30	**318**	317
Share premium account		**833**	778
Retained earnings		**4,386**	3,103
Accumulated other comprehensive loss	31	**(319)**	(587)
Other equity	32	**601**	581
Total shareholders' equity		**5,819**	4,192
Non-controlling interests in equity	33	**–**	63
Total non-controlling interests and shareholders' equity		**5,819**	4,255

The Financial Statements on pages 66 to 141 were approved and authorised for issue by the Board of Directors on 24 February 2011 and were signed below on its behalf by:

Sam Laidlaw
Chief Executive

Nick Luff
Group Finance Director

The notes on pages 71 to 141 form part of these Financial Statements.

Year ended 31 December 2010	Share capital (note 30) £m	Share premium £m	Retained earnings £m	Accumulated other comprehensive (loss)/income (note 31) £m	Other equity (note 32) £m	**Total £m**	Non-controlling interests (note 33) £m	**Total equity £m**
	Attributable to equity holders of the parent							
1 January 2010	317	778	3,103	(587)	581	**4,192**	63	**4,255**
Profit for the year	–	–	1,935	–	–	**1,935**	7	**1,942**
Other comprehensive income	–	–	–	268	–	**268**	–	**268**
Total comprehensive income	–	–	1,935	268	–	**2,203**	7	**2,210**
	317	778	5,038	(319)	581	**6,395**	70	**6,465**
Employee share schemes	1	55	16	–	(3)	**69**	–	**69**
Liquidation of subsidiaries (i)	–	–	–	–	–	**–**	(70)	**(70)**
Dividends	–	–	(668)	–	–	**(668)**	–	**(668)**
Taxation	–	–	–	–	20	**20**	–	**20**
Exchange adjustments	–	–	–	–	3	**3**	–	**3**
31 December 2010	**318**	**833**	**4,386**	**(319)**	**601**	**5,819**	**–**	**5,819**

Year ended 31 December 2009	Share capital (note 30) £m	Share premium £m	Retained earnings £m	Accumulated other comprehensive (loss)/income (note 31) £m	Other equity (note 32) £m	Total £m	Non-controlling interests (note 33) £m	Total equity £m
	Attributable to equity holders of the parent							
1 January 2009	315	729	2,759	(40)	549	4,312	60	4,372
Profit for the year	–	–	844	–	–	844	12	856
Other comprehensive (loss)/income	–	–	–	(547)	–	(547)	1	(546)
Total comprehensive income	–	–	844	(547)	–	297	13	310
	315	729	3,603	(587)	549	4,609	73	4,682
Employee share schemes	2	49	9	–	3	63	–	63
Amounts arising on consolidation (ii)	–	–	–	–	144	144	802	946
Repurchase of non-controlling interests	–	–	–	–	–	–	(201)	(201)
Disposal of Segebel S.A. (iii)	–	–	126	–	(126)	–	(589)	(589)
Dividends paid by subsidiaries	–	–	–	–	–	–	(11)	(11)
Dividends	–	–	(635)	–	–	(635)	–	(635)
Taxation	–	–	–	–	12	12	–	12
Exchange adjustments	–	–	–	–	(1)	(1)	(11)	(12)
31 December 2009	317	778	3,103	(587)	581	4,192	63	4,255

(i) On 14 May 2010 GF Two Limited (formerly Goldfish Holdings Limited) and its subsidiary, GF One Limited (formerly Goldfish Bank Limited), both non-trading entities were put into liquidation.
(ii) Gains on revaluation of previously held investments, as revalued on full consolidation, and recognition of non-controlling interests.
(iii) Transfer of revaluation gain on Segebel S.A. to retained earnings and de-recognition of non-controlling interests following the disposal.

The notes on pages 71 to 141 form part of these Financial Statements.

Year ended 31 December	Notes	2010 £m	2009 £m
Cash generated from continuing operations	34	**3,445**	3,082
Income taxes paid		**(412)**	(329)
Net petroleum revenue tax paid		**(128)**	(174)
Interest received		**5**	13
Interest paid		**(11)**	(3)
Payments relating to exceptional charges		**(223)**	(203)
Net cash flow from continuing operating activities	34	**2,676**	2,386
Net cash flow from discontinued operating activities	34	**7**	261
Net cash flow from operating activities		**2,683**	2,647
Purchase of Venture Production plc net of cash and cash equivalents acquired		**–**	(1,115)
Purchase of other businesses net of cash and cash equivalents acquired	37	**(606)**	(438)
Sale of businesses net of cash and cash equivalents disposed of		**9**	870
Purchase of intangible assets	6,34	**(661)**	(604)
Disposal and surrender of intangible assets		**15**	43
Purchase of property, plant and equipment	6	**(547)**	(594)
Disposal of property, plant and equipment		**32**	–
Investments in joint ventures and associates		**(149)**	(2,291)
Dividends received from joint ventures and associates	19	**83**	–
Repayments of loans to, and disposal of investments in, joint ventures and associates	19	**26**	18
Interest received		**19**	31
Net purchase of securities		**(56)**	(128)
Net cash flow from continuing investing activities		**(1,835)**	(4,208)
Net cash flow from discontinued investing activities		**(4)**	(312)
Net cash flow from investing activities		**(1,839)**	(4,520)
Issue of ordinary share capital	30	**31**	30
Purchase of treasury shares		**(9)**	(5)
Financing interest paid		**(292)**	(238)
Cash inflow from additional debt		**267**	1,887
Cash outflow from payment of capital element of finance leases		**(23)**	(22)
Cash outflow from repayment of other debt		**(928)**	(872)
Net cash flow from (reduction)/increase in debt	34	**(684)**	993
Realised net foreign exchange loss on cash settlement of derivative contracts		**(55)**	(2)
Equity dividends paid	12	**(668)**	(635)
Net cash flow from continuing financing activities		**(1,677)**	143
Net cash flow from discontinued financing activities		**–**	161
Net cash flow from financing activities		**(1,677)**	304
Net decrease in cash and cash equivalents		**(833)**	(1,569)
Cash and cash equivalents at 1 January		**1,285**	2,904
Effect of foreign exchange rate changes		**(1)**	(50)
Cash and cash equivalents at 31 December		**451**	1,285
Included in the following lines of the Balance Sheet:			
Cash and cash equivalents	24	**467**	1,294
Bank overdrafts, loans and other borrowings		**(19)**	(28)
Assets of disposal groups classified as held for sale	38	**3**	19
		451	1,285

The notes on pages 71 to 141 form part of these Financial Statements.

1. General information

Centrica plc is a Company domiciled and incorporated in the UK. The address of the registered office is given on page 49. The nature of the Group's operations and principal activities are set out in note 6 and in the Directors' Report – Business Review on pages 4 to 36.

The consolidated Financial Statements of Centrica plc are presented in pounds sterling. Operations and transactions conducted in currencies other than pounds sterling are included in the consolidated Financial Statements in accordance with the foreign currencies accounting policy set out in note 2.

2. Summary of significant accounting policies

The principal accounting policies applied in the preparation of these consolidated Financial Statements are set out below. These policies have been applied consistently to all the years presented, unless otherwise stated.

Basis of preparation

The consolidated Financial Statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union (EU) and therefore comply with Article 4 of the EU IAS Regulation and the Companies Act 2006.

The consolidated Financial Statements have been prepared on the historical cost basis, except for derivative financial instruments, available-for-sale financial assets, financial instruments designated as at fair value through profit or loss on initial recognition, and the assets and liabilities of the Group pension schemes that have been measured at fair value. The carrying values of recognised assets and liabilities that are hedged items in fair value hedges, and are otherwise carried at cost, are adjusted to record changes in the fair values attributable to the risks that are being hedged. The principal accounting policies adopted are set out below.

The preparation of Financial Statements in conformity with IFRS as adopted by the EU requires the use of certain critical accounting estimates. It requires management to exercise its judgement in the processes of applying the Group's accounting policies. The areas involving a higher degree of judgement, complexity or areas where assumptions and estimates are significant to the consolidated Financial Statements are described in note 3.

(a) Standards, amendments and interpretations effective in 2010

At the date of authorisation of these consolidated Financial Statements, the following standards and amendments to existing standards were effective for the current year:

- IFRS 3 (revised), Business Combinations. The revised standard applies to business combinations completing on or after 1 January 2010 with no requirement to restate previous business combinations. The revised standard continues to apply the acquisition method to business combinations with some significant changes. For example, all payments to purchase a business are recorded at fair value at acquisition date, with contingent consideration payments classified as a liability and subsequently re-measured through the Group Income Statement. All acquisition related costs are expensed. There is a choice on an acquisition-by-acquisition basis to measure the non-controlling interest in the acquiree at either fair value or at the non-controlling interest's proportionate share of the acquiree's net assets. The Group's business combinations executed during the year are set out in note 37. There has been no material impact to the Group's Financial Statements on adopting IFRS 3 (revised).
- IAS 27 (revised), Consolidated and Separate Financial Statements. As the Group has adopted IFRS 3 (revised) it is required to adopt IAS 27 (revised) at the same time, which applies prospectively for transactions occurring after 1 January 2010. The revised standard requires the effects of all transactions with non-controlling interests to be recorded in equity if there is no change in control, and such transactions no longer result in goodwill or gains and losses arising. The revised standard also specifies the accounting when control is lost. In such instances any remaining interest in the entity is re-measured to fair value and a gain or loss is recognised in profit or loss. During the year the Group disposed of a 50% interest in Lincs Windfarm Limited, formerly known as Centrica (Lincs) Limited, as set out in note 38, such that the Group no longer has a controlling interest.

The following amendments to existing standards and interpretations were also effective for the current period, but the adoption of these amendments to existing standards and interpretations did not have a material impact on the Financial Statements of the Group:

- IFRIC 17, Distributions of Non-cash Assets to Owners;
- IAS 39 (amendment), Financial Instruments: Recognition and Measurement – Eligible Hedged Items;
- IFRS 2 (amendment), Share-based Payment – Group Cash-settled Share-based Payment Transactions; and
- Improvements to IFRSs (2009).

(b) Standards, amendments and interpretations that are not yet effective and that have not been early adopted by the Group

At the date of authorisation of these Financial Statements, the following standards, amendments to existing standards and interpretations, which have not been applied in these consolidated Financial Statements, were in issue but not yet effective:

- IFRS 9, Financial Instruments, effective for annual periods beginning on or after 1 January 2013, subject to EU endorsement. The standard is part of a wider project to replace IAS 39, Financial Instruments: Recognition and Measurement. The impact of adopting this standard is under assessment.

The Directors anticipate that the adoption of the following standards, interpretations and amendments to existing standards and interpretations in future periods, which were also in issue at the date of authorisation of these Financial Statements, will have no material impact on the Financial Statements of the Group:

- IAS 32 (Amendment), Classification of Rights Issues, effective for annual periods commencing on or after 1 February 2010;
- IFRIC 14 (Amendment), Prepayments of a Minimum Funding Requirement, effective for annual periods beginning on or after 1 January 2011;
- IFRIC 19, Extinguishing Financial Liabilities with Equity Instruments, effective for annual periods beginning on or after 1 July 2010;
- IAS 24 (Revised), Related Party Disclosures, effective for annual periods beginning on or after 1 January 2011;
- Amendments to IFRS 7 Financial Instruments: Disclosures, effective for annual periods beginning on or after 1 July 2011, subject to EU endorsement;
- Amendment to IAS 12 Income Taxes, effective for annual periods beginning on or after 1 January 2012, subject to EU endorsement; and
- Improvements to IFRSs 2010, effective for annual periods beginning on or after 1 January 2011, subject to EU endorsement.

2. Summary of significant accounting policies continued

(c) Income Statement presentation

The Group's Income Statement and segmental note separately identify the effects of re-measurement of certain financial instruments, and items which are exceptional, in order to provide readers with a clear and consistent presentation of the Group's underlying performance, as described below.

(i) Certain re-measurements

As part of its energy procurement activities, the Group enters into a range of commodity contracts designed to achieve security of energy supply. These contracts comprise both purchases and sales and cover a wide range of volumes, prices and timescales. The majority of the underlying supply comes from high-volume, long-term contracts which are complemented by short-term arrangements. These short-term contracts are entered into for the purpose of balancing energy supplies and customer demand and to optimise the price paid by the Group. Short-term demand can vary significantly as a result of factors such as weather, power generation profiles and short-term movements in market prices.

Many of the energy procurement contracts are held for the purpose of receipt or delivery of commodities in accordance with the Group's purchase, sale or usage requirements and are therefore out of scope of IAS 39. However, a number of contracts are considered to be derivative financial instruments and are required to be fair valued under IAS 39, primarily because their terms include the ability to trade elements of the contracted volumes on a net-settled basis.

The Group has shown the fair value adjustments arising on these contracts separately in the certain re-measurements column. This is because the intention of management is, subject to short-term demand balancing, to use these energy supplies to meet customer demand. Accordingly, management believes the ultimate net charge to cost of sales will be consistent with the price of energy agreed in these contracts and that the fair value adjustments will reverse as the energy is supplied over the life of the contract. This makes the fair value re-measurements very different in nature from costs arising from the physical delivery of energy in the year.

At the balance sheet date the fair value represents the difference between the prices agreed in the respective contracts and the actual or anticipated market price of acquiring the same amount of energy on the open market. The movement in the fair value taken to certain re-measurements in the Income Statement represents the unwinding of the contracted volume delivered or consumed during the year, combined with the change in fair value of future contracted energy as a result of movements in forward energy prices during the year.

These adjustments represent the significant majority of the items included in certain re-measurements.

In addition to these, however, the Group has identified a number of comparable contractual arrangements where the difference between the price which the Group expects to pay or receive under a contract and the market price is required to be fair valued by IAS 39. These additional items relate to cross-border transportation or transmission capacity, storage capacity and contracts relating to the sale of energy by-products, on which economic value has been created which is not wholly recognised under the requirements of IAS 39. For these arrangements the related fair value adjustments are also included under certain re-measurements.

These arrangements are managed separately from proprietary energy trading activities where trades are entered into speculatively for the purpose of making profits in their own right. These proprietary trades are included in the results before certain re-measurements.

In addition, certain re-measurements includes the effects of unwinding the acquisition-date fair values attributable to forward energy procurement and energy sales contracts arising on the acquisition of Strategic Investments, as described below in section (d). The Group has shown the effect of unwinding the acquisition-date fair values attributable to forward energy procurement and energy sales contracts for these investments separately as a certain re-measurement, as the intention is to use these energy supplies in the normal course of business, and management believes the ultimate net charge reflected before the unwind of acquisition-date fair values will be consistent with the price of energy agreed within these contracts. Such presentation is consistent with the internal performance measures used by the Group.

(ii) Exceptional items

As permitted by IAS 1 (Revised), Presentation of Financial Statements, certain items are presented separately. The items that the Group separately presents as exceptional are items which are of a non-recurring nature and, in the judgement of the Directors, need to be disclosed separately by virtue of their nature, size or incidence in order to obtain a clear and consistent presentation of the Group's underlying business performance. Items which may be considered exceptional in nature include disposals of businesses, business restructurings, renegotiation of significant contracts and asset write-downs.

(d) Use of adjusted profit measures

The Directors believe that reporting adjusted profit and adjusted earnings per share measures provides additional useful information on business performance and underlying trends. These measures are used for internal performance purposes. The adjusted measures in this report are not defined terms under IFRS and may not be comparable with similarly titled measures reported by other companies.

The measure of operating profit used by management to evaluate segment performance is adjusted operating profit. Adjusted operating profit is operating profit before exceptional items and certain re-measurements and before depreciation resulting from fair value uplifts to property, plant and equipment on the acquisition of Strategic Investments, as described below. Additionally, adjusted operating profit includes the Group's share of the results from joint ventures and associates before interest and taxation. Note 6 contains an analysis of adjusted operating profit by segment and a reconciliation of adjusted operating profit to operating profit after exceptional items and certain re-measurements.

Adjusted earnings is earnings before exceptional items net of taxation, certain re-measurements net of taxation and depreciation of fair value uplifts to property, plant and equipment on the acquisition of Strategic Investments net of taxation. A reconciliation of earnings to adjusted earnings is provided in note 14.

Depreciation of fair value uplifts to property, plant and equipment on acquiring Strategic Investments

IFRS requires that a fair value exercise is undertaken allocating the cost of acquiring controlling interests and interests in associates to the fair value of the acquired identifiable assets, liabilities and contingent liabilities. Any difference between the cost of acquiring the interest and the fair value of the acquired net assets, which includes identified contingent liabilities, is recognised as acquired goodwill. The fair value exercise is performed at the date of acquisition.

2. Summary of significant accounting policies continued

The Directors have determined that for Strategic Investments it is important to separately identify the earnings impact of increased depreciation arising from the acquisition-date fair value uplifts made to property, plant and equipment over their useful economic lives. As a result of the nature of fair value assessments in the energy industry the value attributed to strategic assets is a subjective judgement based on a wide range of complex variables at a point in time. The subsequent depreciation of the fair value uplifts bears little relationship to current market conditions, operational performance or underlying cash generation. Management therefore reports and monitors the operational performance of Strategic Investments before the impact of depreciation on fair value uplifts to property, plant and equipment and the segmental results are presented on a consistent basis.

The Group has two Strategic Investments for which reported profits before certain re-measurements and exceptional items have been adjusted in arriving at adjusted profit and adjusted earnings per share. These Strategic Investments relate to the acquisition of Venture Production plc ('Venture'), the operating results of which are included within the Upstream UK – Upstream gas and oil segment, and the acquisition of the 20% interest in Lake Acquisitions Limited ('British Energy'), which owns the British Energy Group, the results (net of taxation and interest) of which are included within the Upstream UK – Power generation segment.

(i) Venture

The Group acquired a controlling interest in Venture in 2009. Significant adjustments have been made to the acquired property, plant and equipment to report the acquired oil and gas field interests at their acquisition-date fair values which are subsequently depreciated through the Group Income Statement over their respective useful economic lives using the unit of production method.

Whilst the impact of unwinding the property, plant and equipment at their acquisition-date fair values is included in overall reported profit for the year, the Directors have reversed the earnings impact of the increased depreciation and related taxation resulting from fair value uplifts to the acquired oil and gas interests in order to arrive at adjusted profit from continuing operations after taxation.

(ii) British Energy

Centrica acquired its 20% interest in Lake Acquisitions Limited and thus British Energy in 2009. The interest in British Energy is accounted for as an investment in an associate. IAS 28 requires investments in associates to be accounted for using the equity method such that the Group reports its share of the associate's profit or loss, which is net of interest and taxation, within the Group's Income Statement. IAS 28 requires that the Group's share of the associate's profit or loss includes the effects of unwinding the fair value adjustments arising from the notional fair value exercise undertaken at acquisition date.

The most significant fair value adjustments arising on the acquisition of the 20% investment in British Energy relate to the fair value uplifts made to the British Energy nuclear power stations to report the property, plant and equipment at their acquisition-date fair values and fair value uplifts made to British Energy's energy procurement contracts and energy sales contracts to report these at their acquisition-date fair values.

Whilst the impact of increased depreciation and related taxation through unwinding the fair value uplifts to the nuclear power stations is included in the share of associate's post-acquisition result included in overall reported Group profit for the year, the Directors have reversed these impacts in arriving at adjusted profit from continuing operations for the year. The impact of unwinding the acquisition-date fair values attributable to the acquired energy procurement and energy sales contracts is included within certain re-measurements as explained above.

Basis of consolidation

The Group Financial Statements consolidate the Financial Statements of the Company and entities controlled by the Company (its subsidiaries) up to 31 December each year, and incorporate the results of its share of jointly controlled entities and associates using the equity method of accounting.

Control is achieved where the Company has the power to govern the financial and operating policies of an investee entity so as to obtain benefits from its activities.

The results of subsidiaries acquired or disposed of during the year are consolidated from the effective date of acquisition or up to the effective date of disposal, as appropriate. Where necessary, adjustments are made to the Financial Statements of subsidiaries, associates and jointly-controlled entities to bring the accounting policies used into line with those used by the Group.

All intra-Group transactions, balances, income and expenses are eliminated upon consolidation.

A change in the ownership interest of a subsidiary, without loss of control is accounted for as an equity transaction. For purchases of non-controlling interests, the difference between any consideration paid and the relevant share acquired of the carrying value of the net assets of the subsidiary is recorded in equity. Gains or losses on disposals of non-controlling interests are also recorded in equity.

When the Group ceases to have control or significant influence, any retained interest in the entity is re-measured to its fair value with the change in carrying amount recognised in profit or loss. The fair value is the initial carrying amount for the purposes of subsequently accounting for the retained interest as a joint venture, associate or financial asset.

Interests in joint ventures

A jointly controlled entity is a joint venture which involves the establishment of an entity to engage in economic activity, which the Group controls jointly with its fellow venturers. Under the equity method, investments in jointly controlled entities are carried at cost plus post-acquisition changes in the Group's share of net assets of the jointly controlled entity, less any impairment in value in individual investments. The Income Statement reflects the Group's share of the results of operations after tax of the jointly controlled entity.

Certain exploration and production activity is conducted through joint ventures, where the venturers have a direct interest in and jointly control the assets of the venture. The results, assets, liabilities and cash flows of these jointly controlled assets are included in the consolidated Financial Statements in proportion to the Group's interest.

Interests in associates

An associate is an entity in which the Group has an equity interest and over which it has the ability to exercise significant influence. Under the equity method, investments in associates are carried at cost plus post-acquisition changes in the Group's share of the net assets of the associate, less any impairment in value in individual investments. The Income Statement reflects the Group's share of the results of the associate, which is net of interest and taxation and presents this as a single line item in arriving at Group operating profit on the face of the Income Statement.

Revenue

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be measured reliably. Revenue includes amounts receivable for goods and services provided in the normal course of business, net of discounts, rebates, VAT and other sales-related taxes.

Energy supply: Revenue is recognised on the basis of energy supplied during the year. Revenue for energy supply activities includes an assessment of energy supplied to customers between the date of the last meter reading and the year end (unread). Unread gas and electricity is estimated using historical consumption patterns, taking into account the industry reconciliation process for

2. Summary of significant accounting policies continued

total gas and total electricity usage by supplier, and is included in accrued energy income within trade and other receivables.

Proprietary energy trading: Revenue comprises both realised (settled) and unrealised (fair value changes) net gains and losses from trading in physical and financial energy contracts.

Home services and fixed-fee service contracts: Revenue from fixed-fee service contracts is recognised in the Income Statement with regard to the incidence of risk over the life of the contract, reflecting the seasonal propensity of claims to be made under the contracts and the benefits receivable by the customer, which span the life of the contract as a result of emergency maintenance being available throughout the contract term.

Amounts paid in advance greater than recognised revenue are treated as deferred income, with any paid in arrears recognised as accrued income. For one-off services, such as installations, revenue is recognised at the date of service provision.

Storage services: Storage capacity revenues are recognised evenly over the contract period, whilst commodity revenues for the injection and withdrawal of gas are recognised at the point of gas flowing into or out of the storage facilities. Gas purchases and gas sales transactions entered into to optimise the performance of the gas storage facilities are presented net within revenue.

Gas production: Revenue associated with exploration and production sales (of natural gas, crude oil and condensates) is recognised when title passes to the customer. Revenue from the production of natural gas, oil and condensates in which the Group has an interest with other producers is recognised based on the Group's working interest and the terms of the relevant production-sharing arrangements (the entitlement method). Where differences arise between production sold and the Group's share of production, this is accounted for as an overlift or underlift (see separate accounting policy). Gas purchases and gas sales entered into to optimise the performance of gas production facilities are presented net within revenue.

Power generation: Revenue is recognised on the basis of power supplied during the period. Power purchases and sales entered into to optimise the performance of power generation facilities are presented net within revenue.

Interest income: Interest income is accrued on a time basis, by reference to the principal outstanding and at the effective interest rate applicable, which is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset to that asset's net carrying value.

Cost of sales

Energy supply includes the cost of gas and electricity produced and purchased during the year taking into account the industry reconciliation process for total gas and total electricity usage by supplier, and related transportation, distribution, royalty costs and bought-in materials and services.

Home services' and fixed-fee service contracts' cost of sales includes direct labour and related overheads on installation work, repairs and service contracts in the year.

Segmental reporting

The Group's operating segments are reported in a manner consistent with the internal reporting provided to and regularly reviewed by the Group's Executive Committee for the purposes of evaluating segment performance and allocating resources.

Borrowing costs

Borrowing costs that arise in connection with the acquisition, construction or production of a qualifying asset are capitalised and subsequently amortised in line with the depreciation of the related asset. Borrowing costs are capitalised from the time of acquisition or from the beginning of construction or production until the point at which the qualifying asset is ready for use. Where a specific financing arrangement is in place, the specific borrowing rate for that arrangement is applied. For non-specific financing arrangements, a Group financing rate representative of the weighted average borrowing rate of the Group is used. Borrowing costs not arising in connection with the acquisition, construction or production of a qualifying asset are expensed.

Carbon Emissions Reduction Target programme (CERT)

UK-licensed energy suppliers are set a carbon emission reduction target by the Government which is proportional to the size of their customer base. The current CERT programme runs from April 2008 to March 2011. The target is subject to an annual adjustment throughout the programme period to take account of changes to a UK-licensed energy supplier's customer base. Energy suppliers can meet the target through expenditure on qualifying projects which give rise to carbon savings. The carbon savings can be transferred between energy suppliers. The Group charges the costs of the programme to cost of sales and capitalises costs incurred in deriving carbon savings in excess of the annual target as inventory, which is valued at the lower of cost and net realisable value and which may be used to meet the carbon emissions reduction target in subsequent periods or sold to third parties. The inventory is carried on a first-in, first-out basis. The carbon emission reduction target for the programme period is allocated to reporting periods on a straight-line basis as adjusted by the annual determination process.

Employee share schemes

The Group operates a number of employee share schemes, detailed in the Remuneration Report on pages 50 to 63 and in note 35, under which it makes equity-settled share-based payments to certain employees. Equity-settled share-based payments are measured at fair value at the date of grant (excluding the effect of non-market-based vesting conditions). The fair value determined at the grant date is expensed on a straight-line basis together with a corresponding increase in equity over the vesting period, based on the Group's estimate of the number of awards that will vest, and adjusted for the effect of non-market-based vesting conditions.

Fair value is measured using methods appropriate to each of the different schemes as follows:

LTIS: EPS awards after 2005	Market value on the date of grant
LTIS: TSR awards after 2005	A Monte Carlo simulation to predict the total shareholder return performance
Sharesave	Black-Scholes
ESOS	Black-Scholes using an adjusted option life assumption to reflect the possibility of early exercise
SAS, SIP, DMSS, RSS, ESPP and DBP	Market value on the date of grant

Foreign currencies

The consolidated Financial Statements are presented in pounds sterling, which is the functional currency of the Company and the Group's presentational currency. Each entity in the Group determines its own functional currency and items included in the Financial Statements of each entity are measured using that functional currency. Transactions in foreign currencies are, on initial recognition, recorded at the functional currency rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange ruling at the balance sheet date. All differences are included in the Income Statement for the period, with the exception of exchange differences on foreign currency borrowings that provide a hedge against a net investment in a foreign entity. These are taken directly to equity until the disposal or partial disposal of the net investment, at which time they are recognised in the Income Statement. Non-monetary items that are measured in terms of historical cost in a currency other than the functional currency

2. Summary of significant accounting policies continued

of the entity concerned are translated using the exchange rates as at the dates of the initial transactions.

For the purpose of presenting consolidated Financial Statements, the assets and liabilities of the Group's foreign subsidiary undertakings, jointly controlled entities and associates are translated into pounds sterling at exchange rates prevailing on the balance sheet date. The results of foreign subsidiary undertakings, jointly controlled entities and associates are translated into pounds sterling at average rates of exchange for the relevant period. Exchange differences arising from the retranslation of the opening net assets and results for the year are transferred to the Group's foreign currency translation reserve, a separate component of equity, and are reported in the Statement of Comprehensive Income. In the event of the disposal of an undertaking with assets and liabilities denominated in a foreign currency, the cumulative translation difference arising in the foreign currency translation reserve is charged or credited to the Income Statement on disposal.

Exchange differences on foreign currency borrowings, foreign currency swaps and forward exchange contracts used to hedge foreign currency net investments in foreign subsidiary undertakings, jointly controlled entities and associates are taken directly to reserves and are reported in the Statement of Comprehensive Income. All other exchange movements are recognised in the Income Statement for the year.

Business combinations and goodwill

The acquisition of subsidiaries is accounted for using the purchase method. The cost of the acquisition is measured as the cash paid and the aggregate of the fair values, at the date of exchange, of other assets transferred, liabilities incurred or assumed, and equity instruments issued by the Group in exchange for control of the acquiree. The acquiree's identifiable assets, liabilities and contingent liabilities that meet the conditions for recognition under IFRS 3 (revised), Business Combinations, are recognised at their fair value at the acquisition date, except for non-current assets (or disposal groups) that are classified as held for resale in accordance with IFRS 5, Non-Current Assets Held for Sale and Discontinued Operations, which are recognised and measured at fair value less costs to sell.

Goodwill arising on a business combination represents the excess of the cost of acquisition over the Group's interest in the fair value of the identifiable assets and liabilities of a subsidiary, jointly controlled entity or associate at the date of acquisition. Goodwill is initially recognised as an asset at cost and is subsequently measured at cost less any accumulated impairment losses. If, after reassessment, the Group's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities exceeds the cost of the business combination, the excess is recognised immediately in the Income Statement.

On an acquisition by acquisition basis, the interest of non-controlling shareholders in the acquiree is measured initially either at the non-controlling shareholders' proportion of the net fair value of the assets, liabilities and contingent liabilities recognised or at fair value.

Goodwill, which is recognised as an asset, is reviewed for impairment annually or more frequently if events or changes in circumstances indicate that the carrying amount may be impaired. Any impairment is recognised immediately in the Income Statement and is not subsequently reversed.

For the purpose of impairment testing, goodwill is allocated to each of the Group's cash-generating units or groups of cash-generating units that expect to benefit from the business combination in which the goodwill arose. Cash-generating units to which goodwill has been allocated are tested for impairment annually, or more frequently when there is an indication that the unit may be impaired. If the recoverable amount of the cash-generating unit or groups of cash-generating units is less than the carrying amount of the unit, the impairment loss is recognised immediately in the Income Statement and allocated first to reduce the carrying amount of any goodwill allocated to the unit and then to the other assets of the unit pro rata on the basis of the carrying amount of each asset in the unit. Any impairment is not subsequently reversed.

On disposal of a subsidiary, associate or joint venture entity, the attributable amount of goodwill is included in the determination of the profit or loss on disposal.

Other intangible assets

Intangible assets acquired separately are measured on initial recognition at cost. Intangible assets include emissions trading schemes, renewable obligation certificates, certain exploration and evaluation expenditures, brands and application software, the accounting policies for which are dealt with separately below. For purchased application software, for example investments in customer relationship management and billing systems, cost includes contractors' charges, materials, directly-attributable labour and directly-attributable overheads.

Capitalisation begins when expenditure for the asset is being incurred and activities necessary to prepare the asset for use are in progress. Capitalisation ceases when substantially all the activities that are necessary to prepare the asset for use are complete. Amortisation commences at the point of commercial deployment. The cost of intangible assets acquired in a business combination is their fair value as at the date of acquisition.

Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses. The useful lives of intangible assets are assessed to be either finite or indefinite. Intangible assets with finite lives are amortised over their useful economic life and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortisation period and the amortisation method for an intangible asset are reviewed at least at each financial year end. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset are accounted for on a prospective basis by changing the amortisation period or method, as appropriate, and treated as changes in accounting estimates.

Intangible assets are derecognised on disposal, or when no future economic benefits are expected from their use.

Intangible assets with indefinite useful lives are tested for impairment annually, and whenever there is an indication that the intangible asset may be impaired, either individually or at the cash-generating unit level, such intangibles are not amortised. The useful life of an intangible asset with an indefinite useful life is reviewed annually to determine whether the indefinite life assessment continues to be supportable. If not, the change in the useful life assessment from indefinite to finite is made on a prospective basis.

The amortisation period for the principal categories of intangible assets are as follows:

Application software	up to 10 years
Licences	up to 20 years
Consents	up to 25 years
Contractual customer relationships	up to 20 years
Identifiable acquired brand	Indefinite

EU Emissions Trading Scheme and renewable obligations certificates

Granted carbon dioxide emissions allowances received in a period are recognised initially at nominal value (nil value). Purchased carbon dioxide emissions allowances are recognised initially at cost (purchase price) within intangible assets. A liability is recognised when the level of emissions exceeds the level of allowances granted. The liability is measured at the cost of purchased allowances up to the level of purchased allowances held, and then

2. Summary of significant accounting policies continued

at the market price of allowances ruling at the balance sheet date, with movements in the liability recognised in operating profit.

Forward contracts for the purchase or sale of carbon dioxide emissions allowances are measured at fair value with gains and losses arising from changes in fair value recognised in the Income Statement. The intangible asset is surrendered and the liability is utilised at the end of the compliance period to reflect the consumption of economic benefits.

Purchased renewable obligation certificates are recognised initially at cost within intangible assets. A liability for the renewables obligation is recognised based on the level of electricity supplied to customers, and is calculated in accordance with percentages set by the UK Government and the renewable obligation certificate buyout price for that period. The intangible asset is surrendered and the liability is utilised at the end of the compliance period to reflect the consumption of economic benefits.

Property, plant and equipment

Property, plant and equipment is included in the Balance Sheet at cost, less accumulated depreciation and any provisions for impairment.

The initial cost of an asset comprises its purchase price or construction cost and any costs directly attributable to bringing the asset into operation. The purchase price or construction cost is the aggregate amount paid and the fair value of any other consideration given to acquire the asset.

Subsequent expenditure in respect of items of property, plant and equipment such as the replacement of major parts, major inspections or overhauls, are capitalised as part of the cost of the related asset where it is probable that future economic benefits will arise as a result of the expenditure and the cost can be reliably measured. All other subsequent expenditure, including the costs of day-to-day servicing, repairs and maintenance, is expensed as incurred.

Freehold land is not depreciated. Other property, plant and equipment, with the exception of upstream production assets (see below), are depreciated on a straight-line basis at rates sufficient to write off the cost, less estimated residual values, of individual assets over their estimated useful lives. The depreciation periods for the principal categories of assets are as follows:

Freehold and leasehold buildings	up to 50 years
Plant	5 to 20 years
Power stations and wind farms	up to 30 years
Equipment and vehicles	3 to 10 years
Storage	up to 40 years

Assets held under finance leases are depreciated over their expected useful economic lives on the same basis as for owned assets, or where shorter, the lease term.

The carrying values of property, plant and equipment are reviewed for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable.

Residual values and useful lives are reassessed annually and if necessary changes are accounted for prospectively.

Exploration, evaluation and production assets

Centrica uses the successful efforts method of accounting for exploration and evaluation expenditure. Exploration and evaluation expenditure associated with an exploration well, including acquisition costs related to exploration and evaluation activities, are capitalised initially as intangible assets. Certain expenditures such as geological and geophysical exploration costs are expensed. If the prospects are subsequently determined to be successful on completion of evaluation, the relevant expenditure, including licence acquisition costs, is transferred to property, plant and equipment and is subsequently depreciated on a unit of production basis. If the prospects are subsequently determined to be unsuccessful on completion of evaluation, the associated costs are expensed in the period in which that determination is made.

All field development costs are capitalised as property, plant and equipment. Such costs relate to the acquisition and installation of production facilities and include development drilling costs, project-related engineering and other technical services costs. Property, plant and equipment, including rights and concessions related to production activities, are depreciated from the commencement of production in the fields concerned, using the unit of production method, based on all of the proven and probable reserves of those fields. Changes in these estimates are dealt with prospectively.

The net carrying value of fields in production and development is compared on a field-by-field basis with the likely discounted future net revenues to be derived from the remaining commercial reserves. An impairment loss is recognised where it is considered that recorded amounts are unlikely to be fully recovered from the net present value of future net revenues. Exploration and production assets are reviewed annually for indicators of impairment.

Overlift and underlift

Offtake arrangements for oil and gas produced from jointly owned operations are often such that it is not practical for each participant to receive or sell its precise share of the overall production during the period. This results in short-term imbalances between cumulative production entitlement and cumulative sales, referred to as overlift and underlift.

An overlift payable, or underlift receivable, is recognised at the balance sheet date within trade and other payables, or trade and other receivables, respectively, and measured at market value, with movements in the period recognised within cost of sales.

Decommissioning costs

Provision is made for the net present value of the estimated cost of decommissioning gas production facilities at the end of the producing lives of fields, and storage facilities and power stations at the end of the useful life of the facilities, based on price levels and technology at the balance sheet date.

When this provision gives access to future economic benefits, a decommissioning asset is recognised and included within property, plant and equipment. Changes in these estimates and changes to the discount rates are dealt with prospectively and reflected as an adjustment to the provision and corresponding decommissioning asset included within property, plant and equipment. For gas production facilities and offshore storage facilities the decommissioning asset is amortised using the unit of production method, based on proven and probable reserves. For power stations the decommissioning asset is amortised on a straight-line basis over the useful life of the facility. The unwinding of the discount on the provision is included in the Income Statement within interest expense.

Leases

The determination of whether an arrangement is, or contains, a lease is based on the substance of the arrangement and requires an assessment of whether the fulfilment of the arrangement is dependent on the use of a specific asset or assets and whether the arrangement conveys a right to use the asset. Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases. Assets held under finance leases are capitalised and included in property, plant and equipment at their fair value, or if lower, at the present value of the minimum lease payments, each determined at the inception of the lease. The obligations relating to finance leases, net of finance charges in respect of future periods, are included within bank loans and other borrowings, with the amount payable within 12 months included in bank overdrafts and loans within current liabilities.

2. Summary of significant accounting policies continued

Lease payments are apportioned between finance charges and reduction of the finance lease obligation so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged directly against income.

Payments under operating leases are charged to the Income Statement on a straight-line basis over the term of the relevant lease.

Impairment of property, plant and equipment and intangible assets (excluding goodwill)

At each balance sheet date, the Group reviews the carrying amounts of its intangible assets and property, plant and equipment to determine whether there is any indication that those assets have suffered an impairment loss or experienced an impairment reversal. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of any impairment loss or impairment reversal. Where the asset does not generate cash flows that are independent from other assets, the Group estimates the recoverable amount of the cash-generating unit to which the asset belongs. An intangible asset with an indefinite useful life is tested for impairment annually, and whenever there is an indication that the asset may be impaired.

Recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money. Discount rates are based on the estimated cost of capital of each cash-generating unit. Additionally risks specific to the cash flows of the cash-generating units are reflected within cash flow forecasts.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognised immediately as an expense.

An impairment loss is reversed only if there has been a change in the estimate used to determine the asset's recoverable amount since the last impairment loss was recognised. Where an impairment loss subsequently reverses, the carrying amount of the asset (cash-generating unit) is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset (cash-generating unit) in prior years. A reversal of an impairment loss is recognised as income immediately. After such a reversal the depreciation or amortisation charge, where relevant, is adjusted in future periods to allocate the asset's revised carrying amount, less any residual value, on a systematic basis over its remaining useful life.

Non-current assets and disposal groups held for sale and discontinued operations

Non-current assets and disposal groups classified as held for sale are measured at the lower of carrying amount and fair value less costs to sell. No depreciation is charged in respect of non-current assets classified as held for sale.

Non-current assets and disposal groups are classified as held for sale if their carrying amount will be recovered through a sale transaction rather than through continuing use. This condition is regarded as met only when the sale is highly probable and the asset or disposal group is available for immediate sale in its present condition. Management must be committed to the sale which should be expected to qualify for recognition as a completed sale within one year from the date of classification.

The profits or losses and cash flows that relate to a major component of the Group or geographical region that has been sold or is classified as held for sale are presented separately from continuing operations as discontinued operations within the Income Statement and Cash Flow Statement.

Inventories

Inventories are valued on a weighted-average cost basis at the lower of cost and estimated net realisable value after allowance for redundant and slow-moving items, where applicable.

Take-or-pay contracts

Where payments are made to external suppliers under take-or-pay obligations for gas not taken, they are treated as prepayments and included within other receivables, as they generate future economic benefits.

Pensions and other post-retirement benefits

The Group operates a number of defined benefit pension schemes. The cost of providing benefits under the defined benefit schemes is determined separately for each scheme using the projected unit credit actuarial valuation method. Actuarial gains and losses are recognised in full in the period in which they occur. They are recognised in the Statement of Comprehensive Income.

The cost of providing retirement pensions and other benefits is charged to the Income Statement over the periods benefiting from employees' service. Past service cost is recognised immediately to the extent that the benefits are already vested, and otherwise is amortised on a straight-line basis over the average period until the benefits become vested. The difference between the expected return on scheme assets and the change in present value of scheme obligations resulting from the passage of time is recognised in the Income Statement within interest income or interest expense.

The retirement benefit obligation or asset recognised in the Balance Sheet represents the present value of the defined benefit obligation of the schemes as adjusted for unrecognised past service cost, and the fair value of the schemes' assets. The present value of the defined benefit obligation or asset is determined by discounting the estimated future cash outflows using interest rates of high-quality corporate bonds that are denominated in the currency in which the benefits are paid, and that have terms of maturity approximating to the terms of the related pension liability.

Payments to defined contribution retirement benefit schemes are charged as an operating expense as they fall due.

Provisions

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, that can be measured reliably, and it is probable that the Group will be required to settle that obligation. Provisions are measured at the Directors' best estimate of the expenditure required to settle the obligation at the balance sheet date, and are discounted to present value where the effect is material. Where discounting is used, the increase in the provision due to the passage of time is recognised in the Income Statement within interest expense. Onerous contract provisions are recognised where the unavoidable costs of meeting the obligations under a contract exceed the economic benefits expected to be received under it. Given the fungible nature of energy, contracts to purchase or sell energy are reviewed on a portfolio basis whereby it is assumed that the highest priced purchase contract supplies the highest priced sales contract and the lowest priced sales contract is supplied by the lowest priced purchase contract.

2. Summary of significant accounting policies continued

Taxation

Current tax, including UK corporation tax, UK petroleum revenue tax and foreign tax is provided at amounts expected to be paid (or recovered) using the tax rates and laws that have been enacted or substantively enacted by the balance sheet date.

Deferred tax is recognised in respect of all temporary differences identified at the balance sheet date, except to the extent that the deferred tax arises from the initial recognition of goodwill (if amortisation of goodwill is not deductible for tax purposes) or the initial recognition of an asset or liability in a transaction which is not a business combination and at the time of the transaction affects neither accounting profit nor taxable profit and loss. Temporary differences are differences between the carrying amount of the Group's assets and liabilities and their tax base.

Deferred tax liabilities may be offset against deferred tax assets within the same taxable entity or qualifying local tax group. Any remaining deferred tax asset is recognised only when, on the basis of all available evidence, it can be regarded as probable that there will be suitable taxable profits, within the same jurisdiction, in the foreseeable future, against which the deductible temporary difference can be utilised.

Deferred tax is provided on temporary differences arising on subsidiaries, jointly controlled entities and associates, except where the timing of the reversal of the temporary difference can be controlled and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred tax is measured at the average tax rates that are expected to apply in the periods in which the asset is realised or liability settled, based on tax rates and laws that have been enacted or substantively enacted by the balance sheet date. Measurement of deferred tax liabilities and assets reflects the tax consequences expected from the manner in which the asset or liability is recovered or settled.

Financial instruments

Financial assets and financial liabilities are recognised in the Group Balance Sheet when the Group becomes a party to the contractual provisions of the instrument. Financial assets are de-recognised when the Group no longer has the rights to cash flows, the risks and rewards of ownership or control of the asset. Financial liabilities are de-recognised when the obligation under the liability is discharged, cancelled or expires.

(a) Trade receivables

Trade receivables are recognised and carried at original invoice amount less an allowance for any uncollectible amounts. Provision is made when there is objective evidence that the Group may not be able to collect the trade receivable. Balances are written off when recoverability is assessed as being remote. If collection is due in one year or less they are classified as current assets. If not they are presented as non-current assets.

(b) Trade payables

Trade payables are recognised at original invoice amount. If payment is due within one year or less they are classified as current liabilities. If not, they are presented as non-current liabilities.

(c) Share capital

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of new shares are shown in equity as a deduction from the proceeds received. Own equity instruments that are reacquired (treasury shares) are deducted from equity. No gain or loss is recognised in the Income Statement on the purchase, sale, issue or cancellation of the Group's own equity instruments.

(d) Cash and cash equivalents

Cash and cash equivalents comprise cash in hand and current balances with banks and similar institutions, which are readily convertible to known amounts of cash and which are subject to insignificant risk of changes in value and have an original maturity of three months or less.

For the purpose of the Group Cash Flow Statement, cash and cash equivalents consist of cash and cash equivalents as defined above, net of outstanding bank overdrafts.

(e) Interest-bearing loans and other borrowings

All interest-bearing loans and other borrowings are initially recognised at fair value net of directly attributable transaction costs. After initial recognition, interest-bearing loans and other borrowings are subsequently measured at amortised cost using the effective interest method, except when they are the hedged item in an effective fair value hedge relationship, where the carrying value is also adjusted to reflect the fair value movements associated with the hedged risks. Such fair value movements are recognised in the Income Statement. Amortised cost is calculated by taking into account any issue costs, discount or premium.

(f) Available-for-sale financial assets

Available-for-sale financial assets are those non-derivative financial assets that are designated as available-for-sale, which are recognised initially at fair value within the Balance Sheet. Available-for-sale financial assets are re-measured subsequently at fair value with gains and losses arising from changes in fair value recognised directly in equity and presented in the Statement of Comprehensive Income, until the asset is disposed of or is determined to be impaired, at which time the cumulative gain or loss previously recognised in equity is included in the Income Statement for the period. Accrued interest or dividends arising on available-for-sale financial assets are recognised in the Income Statement.

At each balance sheet date the Group assesses whether there is objective evidence that available-for-sale financial assets are impaired. If any such evidence exists, cumulative losses recognised in equity are removed from equity and recognised in profit and loss. The cumulative loss removed from equity represents the difference between the acquisition cost and current fair value, less any impairment loss on that financial asset previously recognised in profit or loss.

Impairment losses recognised in the Income Statement for equity investments classified as available-for-sale are not subsequently reversed through the Income Statement. Impairment losses recognised in the Income Statement for debt instruments classified as available-for-sale are subsequently reversed if an increase in the fair value of the instrument can be objectively related to an event occurring after the recognition of the impairment loss.

(g) Financial assets at fair value through profit or loss

The Group holds investments in gilts which it designates as fair value through profit or loss in order to reduce significantly a measurement inconsistency that would otherwise arise. Investments are measured at fair value on initial recognition and are re-measured to fair value in each subsequent reporting period. Gains and losses arising from changes in fair value are recognised in the Income Statement within interest income or interest expense.

(h) Derivative financial instruments

The Group routinely enters into sale and purchase transactions for physical delivery of gas, power and oil. A number of these transactions take the form of contracts that were entered into and continue to be held for the purpose of receipt or delivery of the physical commodity in accordance with the Group's expected sale, purchase or usage requirements, and are not within the scope of IAS 39.

2. Summary of significant accounting policies continued

Certain purchase and sales contracts for the physical delivery of gas, power and oil are within the scope of IAS 39 due to the fact that they net settle or contain written options. Such contracts are accounted for as derivatives under IAS 39 and are recognised in the Balance Sheet at fair value. Gains and losses arising from changes in fair value on derivatives that do not qualify for hedge accounting are taken directly to the Income Statement for the year.

The Group uses a range of derivatives for both trading and to hedge exposures to financial risks, such as interest rate, foreign exchange and energy price risks, arising in the normal course of business. The use of derivative financial instruments is governed by the Group's policies approved by the Board of Directors. Further detail on the Group's risk management policies is included within the Directors' Report – Governance on pages 46 to 48 and in note 4 to the Financial Statements.

The accounting treatment for derivatives is dependent on whether they are entered into for trading or hedging purposes. A derivative instrument is considered to be used for hedging purposes when it alters the risk profile of an underlying exposure of the Group in line with the Group's risk management policies and is in accordance with established guidelines, which require the hedging relationship to be documented at its inception, ensure that the derivative is highly effective in achieving its objective, and require that its effectiveness can be reliably measured. The Group also holds derivatives which are not designated as hedges and are held for trading.

All derivatives are recognised at fair value on the date on which the derivative is entered into and are re-measured to fair value at each reporting date. Derivatives are carried as assets when the fair value is positive and as liabilities when the fair value is negative. Derivative assets and derivative liabilities are offset and presented on a net basis only when both a legal right of set-off exists and the intention to net settle the derivative contracts is present.

The Group enters into certain energy derivative contracts covering periods for which observable market data does not exist. The fair value of such derivatives is estimated by reference in part to published price quotations from active markets, to the extent that such observable market data exists, and in part by using valuation techniques, whose inputs include data which is not based on or derived from observable markets. Where the fair value at initial recognition for such contracts differs from the transaction price, a fair value gain or fair value loss will arise. This is referred to as a day-one gain or day-one loss. Such gains and losses are deferred and amortised to the Income Statement based on volumes purchased or delivered over the contractual period until such time observable market data becomes available. When observable market data becomes available, any remaining deferred day-one gains or losses are recognised within the Income Statement. Recognition of the gains or losses resulting from changes in fair value depends on the purpose for issuing or holding the derivative. For derivatives that do not qualify for hedge accounting, any gains or losses arising from changes in fair value are taken directly to the Income Statement and are included within gross profit or interest income and interest expense. Gains and losses arising on derivatives entered into for speculative energy trading purposes are presented on a net basis within revenue.

Embedded derivatives: Derivatives embedded in other financial instruments or other host contracts are treated as separate derivatives when their risks and characteristics are not closely related to those of the host contracts and the host contracts are not carried at fair value, with gains or losses reported in the Income Statement. The closely-related nature of embedded derivatives is reassessed when there is a change in the terms of the contract which significantly modifies the future cash flows under the contract. Where a contract contains one or more embedded derivatives, and providing that the embedded derivative significantly modifies the cash flows under the contract, the option to fair value the entire contract may be taken and the contract will be recognised at fair value with changes in fair value recognised in the Income Statement.

(i) Hedge accounting

For the purposes of hedge accounting, hedges are classified either as fair value hedges, cash flow hedges or hedges of net investments in foreign operations.

Fair value hedges: A derivative is classified as a fair value hedge when it hedges the exposure to changes in the fair value of a recognised asset or liability. Any gain or loss from re-measuring the hedging instrument to fair value is recognised immediately in the Income Statement. Any gain or loss on the hedged item attributable to the hedged risk is adjusted against the carrying amount of the hedged item and recognised in the Income Statement. The Group discontinues fair value hedge accounting if the hedging instrument expires or is sold, terminated or exercised, the hedge no longer qualifies for hedge accounting or the Group revokes the designation. Any adjustment to the carrying amount of a hedged financial instrument for which the effective interest method is used is amortised to the Income Statement. Amortisation may begin as soon as an adjustment exists and shall begin no later than when the hedged item ceases to be adjusted for changes in its fair value attributable to the risk being hedged.

Cash flow hedges: A derivative is classified as a cash flow hedge when it hedges exposure to variability in cash flows that is attributable to a particular risk either associated with a recognised asset, liability or a highly probable forecast transaction. The portion of the gain or loss on the hedging instrument which is effective is recognised directly in equity while any ineffectiveness is recognised in the Income Statement. The gains or losses that are recognised directly in equity are transferred to the Income Statement in the same period in which the highly probable forecast transaction affects income, for example when the future sale of physical gas or physical power actually occurs. Where the hedged item is the cost of a non-financial asset or liability, the amounts taken to equity are transferred to the initial carrying amount of the non-financial asset or liability on its recognition. Hedge accounting is discontinued when the hedging instrument expires or is sold, terminated or exercised without replacement or rollover, no longer qualifies for hedge accounting or the Group revokes the designation.

At that point in time, any cumulative gain or loss on the hedging instrument recognised in equity remains in equity until the highly probable forecast transaction occurs. If the transaction is no longer expected to occur, the cumulative gain or loss recognised in equity is recognised in the Income Statement.

Net investment hedges: Hedges of net investments in foreign operations are accounted for similarly to cash flow hedges. Any gain or loss on the effective portion of the hedge is recognised in equity, any gain or loss on the ineffective portion of the hedge is recognised in the Income Statement. On disposal of the foreign operation, the cumulative value of any gains or losses recognised directly in equity is transferred to the Income Statement.

2. Summary of significant accounting policies continued

Nuclear activity

The Group's investments in Lake Acquisitions Limited and NNB Holding Company Limited are accounted for as associates. The following accounting policies are specific to the accounting for the nuclear activity of these associates.

(a) Fuel costs – nuclear front end

Front end fuel costs consist of the costs of procurement of uranium, conversion and enrichment services and fuel element fabrication. All costs are capitalised into inventory and charged to the Income Statement in proportion to the amount of fuel burnt.

(b) Fuel costs – nuclear back end

Advanced Gas-cooled Reactors (AGR)

Spent fuel extracted from the reactors is sent for reprocessing and/or long-term storage and eventual disposal of resulting waste products. Back end fuel costs comprise a loading related cost per tonne of uranium and a rebate/surcharge to this cost dependent on the out-turn market electricity price in the year and are capitalised into inventory and charged to the Income Statement in proportion to the amount of fuel burnt.

Pressurised Water Reactor (PWR)

Back end fuel costs are based on wet storage in station ponds followed by dry storage and subsequent direct disposal of fuel. Back end fuel costs are capitalised into inventory on loading and charged to the income statement in proportion to the amount of fuel burnt.

(c) Nuclear property, plant and equipment and depreciation

The depreciation period for the principal categories of nuclear assets, which are depreciated on a straight-line basis from the date of the Group acquiring its share in British Energy, are as follows:

AGR power stations	Up to 13 years
PWR power station	25 years

Expenditure on major inspection and overhauls of production plant is depreciated over the period until the next outage which for AGR power stations is two to three years and for the PWR power station is 18 months.

(d) Nuclear Liabilities Fund (NLF) funding arrangements

Under the arrangements in place with the Secretary of State, the NLF will fund, subject to certain exceptions, British Energy's qualifying uncontracted nuclear liabilities and qualifying decommissioning costs.

In part-consideration for the assumption of these liabilities by the Secretary of State and the NLF, British Energy agreed to pay fixed decommissioning contributions each year and £150,000 (indexed to RPI) for every tonne of uranium in PWR fuel loaded into the Sizewell B reactor after the date of these arrangements.

(e) NLF and nuclear liabilities receivables

The Government indemnity is provided to indemnify any future shortfall on NLF funding of qualifying uncontracted nuclear liabilities (including PWR back end fuel services) and qualifying nuclear decommissioning costs such that the receivable equals the present value of the associated qualifying nuclear liabilities.

(f) Nuclear liabilities

Nuclear liabilities represent provision for British Energy's liabilities in respect of the costs of waste management of spent fuel and nuclear decommissioning.

(g) Unburnt fuels at shutdown

Due to the nature of the nuclear fuel process there will be quantities of unburnt fuel in the reactors at station closure. The costs relating to this unburnt fuel (final core) are estimated by applying a long-term inflation index to the projected costs, which are then discounted.

3. Critical accounting judgements and key sources of estimation uncertainty

(a) Critical judgements in applying the Group's accounting policies

The Group's accounting policies as set out in note 2 and Notes to the Financial Statements include descriptions of key judgements management has made in applying the Group's accounting policies. Areas of judgement that have the most significant effect on the amounts recognised in the Financial Statements (apart from those involving estimations which are dealt with below) include the following:

- the presentation of certain items as exceptional – notes 2 and 9;
- the use of adjusted profit and adjusted earnings per share measures – notes 2 and 14; and
- the classification of energy procurement contracts as derivative financial instruments and presentation as certain re-measurements – notes 2, 4, 9 and 22.

In addition to those described above, management has made the following key judgements in applying the Group's accounting policies that have the most significant effect on the Group's Financial Statements.

Wind farm partial disposal

On 5 February 2010 the Group disposed of 50% of the equity voting share capital and 50% of the existing shareholder loan of Lincs Windfarm Limited (formerly Centrica (Lincs) Limited) ('Lincs'), the owner of the proposed wind farm (see note 38).

As part of this disposal, the Group contracted to purchase 75% of the power output and levy exemption certificates and 50% of the renewable obligation certificates produced by the wind farm under a 15-year offtake agreement. The pricing of this arrangement was on an arm's length basis. The Group also contracted to provide management, operational and transitional support services to Lincs as directed by their board (and shareholders). A shareholders' agreement was put in place which included a number of reserved matters and provides for joint management of the major decisions of the company.

The Directors have judged that the disposal of equity voting share capital is a loss of control over the financial and operating policies of Lincs. The offtake agreement pricing together with the other arrangements in place mean that the majority of the benefits and residual risks of owning the windfarms reside with Lincs and not Centrica. Accordingly, the remaining investment in Lincs is equity accounted as an investment in a joint venture (see note 19). The Directors have judged that the 15-year offtake agreement is not a leasing arrangement. This is because the Group is not purchasing substantially all of the economic output of the wind farm. This contract is considered to be outside the scope of IAS 39 apart from the embedded derivative arising from the pricing terms which is marked to market separately.

In the previous year, the Group disposed of 50% of the equity voting share capital of GLID Wind Farms TopCo Limited ('GLID'), the owner of Glens of Foudland and Lynn and Inner Dowsing wind farms on 11 December 2009. This transaction was also deemed to be a loss of control and the remaining investment in GLID is equity accounted as an investment in a joint venture (see note 19). The Directors have judged that the 15-year offtake agreement is not a leasing arrangement. The contract is assessed as falling outside the scope of IAS 39 with respect to the own-use exemption, however the embedded derivative in the pricing mechanism is being marked to market separately.

3. Critical accounting judgements and key sources of estimation uncertainty continued

Finance lease – third-party power station tolling arrangement

The Group has a long-term tolling arrangement with the Spalding power station. The contract provides Centrica with the right to nominate 100% of the plant output until 2021 in return for a mix of capacity payments and operating payments based on plant availability. Centrica holds an option to extend the tolling arrangement for a further eight years, exercisable by 30 September 2020. If extended, Centrica is granted an option to purchase the station at the end of this further period. The Directors have judged that the arrangement should be accounted for as a finance lease as the lease term is judged to be substantially all of the economic life of the power station and the present value of the minimum lease payments at inception date of the arrangement amounted to substantially all of the fair value of the power station at that time. Details of the finance lease asset, finance lease creditor and interest charges are included in notes 18, 26 and 10 respectively.

Provision for onerous gas contract

On 1 October 2009 an onerous contract provision was established for a gas purchase contract for which a two-year notice had been served to terminate (see notes 9 and 28). This contract provided the Group with the option to purchase gas for which a significant capacity charge was incurred regardless of the offtake. The capacity charges are unavoidable costs of the contract. The economic benefits expected to be received under the contract have been estimated using the Group's standard contract valuation methodology. Management has judged that, following serving notice to terminate, this contract no longer forms part of the Group's gas supply and that any gas delivered under the contract is delivered to minimise the overall cost of the contract during the notice period rather than to satisfy the Group's overall demand for gas. Therefore the expected economic benefits have been estimated based on market prices rather than being valued on a portfolio basis as explained in note 2.

Operating Lease – third party power station tolling arrangement

The Group has a long-term tolling arrangement with the newly built Rijnmond power station in The Netherlands. The Rijnmond power station commenced operation in May 2010. The contract provides Centrica with the right to nominate 100% of the plant output until 2029 in return for a mix of capacity payments and operating payments based on plant availability. Centrica does not have the right to extend the agreement or any option to purchase the plant. The Directors have judged that the arrangement should be accounted for as an operating lease as the lease term is not judged to be substantially all of the economic life of the power station and the present value of the minimum lease payments at inception date of the arrangement did not amount to substantially all of the fair value of the power station at that time. Details of the operating lease disclosures are included in note 39.

Business combinations and acquisitions – purchase price allocations

For business combinations and acquisitions of associates and joint ventures, IFRS requires that a fair value exercise is undertaken allocating the purchase price (cost) of acquiring controlling interests and interests in associates and joint ventures to the fair value of the acquired identifiable assets, liabilities and contingent liabilities.

Any difference between the cost of acquiring the interest and the fair value of the acquired net assets, which includes identified contingent liabilities, is recognised as acquired goodwill. The fair value exercise is performed at the date of acquisition. As a result of the nature of fair value assessments in the energy industry the purchase price allocation exercise and acquisition-date fair value determinations require subjective judgements based on a wide range of complex variables at a point in time. Management uses all available information to make the fair value determinations. Business combinations are set out in note 37.

EU Emissions Trading Scheme

The Group has been subject to the EU Emissions Trading Scheme (EU ETS) since 1 January 2005. IFRIC 3, Emissions Rights, was withdrawn by the IASB in June 2005, and has not been replaced by definitive guidance. The Group has adopted an accounting policy which recognises carbon dioxide emissions liabilities when the level of emissions exceeds the level of allowances granted by the Government in the period. The liability is measured at the cost of purchased allowances up to the level of purchased allowances held, and then at market price of allowances ruling at the balance sheet date. Movements in the liability are reflected within operating profit. Forward contracts for sales and purchases of allowances are measured at fair value.

Petroleum revenue tax (PRT)

The definition of an income tax in IAS 12, Income Taxes, has led management to judge that PRT should be treated consistently with other income taxes. The charge for the year is presented within taxation on profit from continuing operations in the Income Statement. Deferred amounts are included within deferred tax assets and liabilities in the Balance Sheet.

(b) Key sources of estimation uncertainty

The key assumptions concerning the future, and other key sources of estimation uncertainty at the balance sheet date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year, are discussed below.

Revenue recognition – unread gas and electricity meters

Revenue for energy supply activities includes an assessment of energy supplied to customers between the date of the last meter reading and the year end (unread). Unread gas and electricity comprises both billed and unbilled revenue. It is estimated through the billing systems, using historical consumption patterns, on a customer by customer basis, taking into account weather patterns, load forecasts and the differences between actual meter reads being returned and system estimates. Actual meter reads continue to be compared to system estimates between the balance sheet date and the finalisation of the accounts. An assessment is also made of any factors that are likely to materially affect the ultimate economic benefits which will flow to the Group, including bill cancellation and re-bill rates. To the extent that the economic benefits are not expected to flow to the Group, the value of that revenue is not recognised. The judgements applied, and the assumptions underpinning these judgements, are considered to be appropriate. However, a change in these assumptions would have an impact on the amount of revenue recognised.

Industry reconciliation process – cost of sales

Industry reconciliation procedures are required as differences arise between the estimated quantity of gas and electricity the Group deems to have supplied and billed customers, and the estimated quantity industry system operators deem the individual suppliers, including the Group, to have supplied to customers. Difference in deemed supply is referred to as imbalance. The reconciliation procedures can result in either a higher or lower value of industry deemed supply than has been estimated as being supplied to customers by the Group, but in practice tends to result in a higher value of deemed supply. The Group then reviews the difference to ascertain whether there is evidence that its estimate of amounts supplied to customers is inaccurate or whether the difference arises from other causes. The Group's share of the resulting imbalance is included within commodity costs charged to cost of sales. Management estimates the level of recovery of imbalance which will be achieved either through subsequent customer billing or through developing industry settlement procedures.

Determination of fair values – energy derivatives

Derivative contracts are carried in the Balance Sheet at fair value, with changes in fair value recorded in either the Income Statement or the Statement of Comprehensive Income. Fair values of energy derivatives are estimated by reference in part to published price quotations in active markets and in part by using valuation

3. Critical accounting judgements and key sources of estimation uncertainty continued

techniques. More detail on the assumptions used in determining fair valuations is provided in note 29.

Gas and liquids reserves

The volume of proven and probable gas and liquids reserves is an estimate that affects the unit of production depreciation of producing gas and liquids property, plant and equipment, as well as being a significant estimate affecting decommissioning estimates and impairment calculations. The factors impacting gas and liquids estimates, the process for estimating reserve quantities and reserve recognition are described on page 149.

The impact of a change in estimated proven and probable reserves is dealt with prospectively by depreciating the remaining book value of producing assets over the expected future production. If proven and probable reserves estimates are revised downwards, earnings could be affected by higher depreciation expense or an immediate write-down (impairment) of the asset's book value.

Decommissioning costs

The estimated cost of decommissioning at the end of the producing lives of fields is reviewed periodically and is based on proven and probable reserves, price levels and technology at the balance sheet date. Provision is made for the estimated cost of decommissioning at the balance sheet date. The payment dates of total expected future decommissioning costs are uncertain and dependent on the lives of the facilities, but are currently anticipated to be between 2011 and 2055, with the substantial majority of the costs expected to be paid between 2020 and 2030.

Provisions are determined for the estimated costs of decommissioning British Energy's nuclear power stations and the costs of waste management and spent fuel. Various arrangements and indemnities are in place with the Secretary of State with respect to these costs, as explained in note 2.

Impairment of goodwill and indefinite-lived intangible assets

The Group determines whether goodwill and indefinite-lived intangible assets are impaired at least on an annual basis in accordance with the Group's accounting policy, as described in note 2. This requires the determination of the recoverable amount of the cash-generating units to which goodwill and indefinite-lived intangibles are allocated. The recoverable amounts are determined by either estimating the value in use of those cash-generating units or, in the case of the Upstream UK – Upstream gas and oil cash-generating unit, determining the fair value less costs to sell of the cash-generating unit. Value in use calculations require the Group to make an estimate of the expected future cash flows to be derived from the cash-generating units and to choose a suitable discount rate in order to calculate the present value of those cash flows. The fair value less costs to sell methodology is deemed more appropriate for the Upstream UK – Upstream gas and oil cash-generating unit as it is based on post-tax cash flows arising from each field within the cash-generating unit, which is consistent with the approach taken by management in determining the economic value of the underlying assets. Fair value less costs to sell is determined by discounting the post-tax cash flows expected to be generated by the gas and oil production and development assets within the Upstream UK – Upstream gas and oil cash-generating unit, net of associated selling costs, and takes into account assumptions market participants would use in estimating fair value. Further detail on impairments arising and the assumptions used in determining the value in use and fair value less costs to sell calculations is provided in note 17.

Impairment of power generation and upstream gas assets

Power generation and upstream gas assets are assessed for indicators of impairment at each reporting date in accordance with the Group's accounting policies as described in note 2. If an indicator of impairment exists, an assessment of the recoverable amount of the asset is required to be made. Indicators of impairment for these assets may include, but are not limited to, the following:

- reductions in reserve estimates or profiles of production;
- declines in long-term commodity prices;
- increases in capital expenditure or acceleration of known capital expenditure;
- significant unplanned outages or problems with operational performance; and
- changes in regulatory or tax environments.

The recoverable amount of power generation and upstream gas assets is assessed with reference to either each individual asset's value in use or fair value less costs to sell. The value in use is based on the pre-tax cash flows expected to be generated by the asset and is dependent on views of forecast generation/production, forecast commodity prices (using market prices where available and internal estimates for the remainder of the period) and the timing and extent of capital expenditure. The fair value less costs to sell is determined by using evidence from recent acquisitions for similar assets in the local oil and gas market, or by discounting the post-tax cash flows expected to be generated, net of associated selling costs, taking into account assumptions market participants would use in estimating fair value.

For gas fired power stations, which have a high degree of production flexibility, the value in use calculation also includes a scenario-based statistical assessment of the additional value which can be generated from optimising production to take advantage of volatile forward prices. Pre-tax cash flows for the first three years are based on the Group's internal Board-approved three-year business plans and thereafter are estimated on a consistent basis to reflect cash flows up to the date of cessation of operation of the asset. Pre-tax cash flows are discounted using a pre-tax discount rate that reflects current market assessments of the time value of money. Discount rates are based on the estimated cost of capital of each cash-generating unit. Additionally, risks specific to the cash flows of the cash-generating units are reflected within cash flow forecasts. Further details of impairments arising and the carrying values of the Group's power generation and upstream gas assets are included within note 18.

Trade and other receivables – provisions for credit losses

The methodology for determining provisions for credit losses on trade and other receivables and the level of such provisions are set out in note 21. The estimates and assumptions used to determine the level of provisions are reviewed periodically. Although the provisions recognised are considered appropriate, the use of different assumptions or changes in economic conditions could lead to changes in the provisions and therefore impact profit or loss.

3. Critical accounting judgements and key sources of estimation uncertainty continued

Pensions and other post–retirement benefits

The Group operates a number of defined benefit pension schemes. The cost of providing benefits under the defined benefit schemes is determined separately for each scheme under the projected unit credit actuarial valuation method. Actuarial gains and losses are recognised in full in the period in which they occur. The key assumptions used for the actuarial valuation are based on the Group's best estimate of the variables that will determine the ultimate cost of providing post-employment benefits, on which further detail is provided in note 36.

North America – Wind farm onerous contract provision

In 2009 an onerous contract provision amounting to £55 million was recognised within the North America – Upstream and wholesale energy segment relating to certain wind farm power purchase agreements to reflect the fair value of the obligation to purchase power which was above the net realisable value obtained from selling the power. The profitability of the wind farm power purchase agreements is measured taking into account the expected revenue and cost streams relating to each agreement. This measurement involves the use of estimates relating to expected wind forecasts, forward curves for energy prices and renewable energy certificates prices for which there is not a liquid market for the full term of all the contracts. In 2010 the position has deteriorated further, driven predominantly by falling forward power prices, and the provision has been increased by £67 million in the period resulting, after utilisation of part of the provision in 2010, in a provision of £101 million at the balance sheet date. Although the provision recognised is considered appropriate, it is reasonably possible that changes in economic conditions or the use of different assumptions could lead to further changes in the provision and therefore impact profit or loss in the future.

4. Financial risk management

The Group's normal operating, investing and financing activities expose it to a variety of financial risks: market risk (including commodity price risk, volumetric risk, currency risk, interest rate risk and equity price risk), credit risk and liquidity risk. The Group's overall risk management process is designed to identify, manage and mitigate business risk, which includes, among others, financial risk. Further detail on the Group's overall risk management process is included within the Directors' Report – Governance on pages 46 to 48.

2010 was marked by a continuing shortage of available credit in European energy markets due to the continuing impact from the financial crisis, emerging European Sovereign debt concerns and general economic conditions. Credit markets in North America have started to improve, although consolidation in the energy industry and the implications of the 'Deepwater Horizon' incident impacted overall market activity. The Group continues to be vigilant and manage credit risk in accordance with its risk management policy.

Financial risk management is overseen by the Group Financial Risk Management Committee (GFRMC) according to objectives, targets and policies set by the Board. Commodity price risk management is carried out in accordance with individual business unit Financial Risk Management Committees and their respective financial risk management policies, as approved by the GFRMC under delegated authority from the Board. Treasury risk management, including management of currency risk, interest rate risk, equity price risk and liquidity risk is carried out by a central Group Treasury function in accordance with the Group's financing and treasury policy and collateral risk policy, as approved by the Board. The wholesale credit risks associated with commodity trading and treasury positions are managed in accordance with the Group's credit risk policy. Downstream credit risk management is carried out in accordance with individual business unit credit policies.

Market risk management

Market risk is the risk of loss that results from changes in market prices (commodity prices, foreign exchange rates, interest rates and equity prices). The level of market risk to which the Group is exposed at a point in time varies depending on market conditions, expectations of future price or market rate movements and the composition of the Group's physical asset and contract portfolios.

(a) Commodity price risk management

The Group is exposed to commodity price risk in its upstream assets, energy procurement contracts, downstream and proprietary energy trading activities and uses specific limits to manage the exposure to commodity prices associated with the Group's activities to an acceptable level. Volumetric limits are supported by Profit at Risk (PaR) and Value at Risk (VaR) methodologies in the UK and in North America and a VaR methodology in Europe to measure the Group's exposure to commodity price risk. Limits are also set on PaR and VaR measurements as a further control over exposure to market prices.

(i) Energy procurement, upstream and downstream activities

The Group's energy procurement, upstream and downstream activities consist of equity gas and liquids production, equity power generation, bilateral procurement and sales contracts, market-traded purchase and sales contracts and derivative positions taken on with the intent of securing gas and power for the Group's downstream customers in the UK, Europe and North America from a variety of sources at an optimal cost. The Group actively manages commodity price risk by optimising its asset and contract portfolios and making use of volume flexibility.

The Group is exposed to commodity price risk in its energy procurement, upstream and downstream activities because the cost of procuring gas and electricity to serve its downstream customers varies with wholesale commodity prices. The risk is primarily that market prices for commodities will fluctuate between the time that sales prices are fixed or tariffs are set and the time at which the corresponding procurement cost is fixed, thereby potentially reducing expected margins or making sales unprofitable.

The Group is also exposed to volumetric risk in the form of an uncertain consumption profile arising from a range of factors, including weather, energy consumption changes, customer attrition and economic climate.

In order to manage the exposure to market prices associated with the Group's energy procurement, upstream and downstream activities the Group uses a specific set of limits (including position, volumetric, VaR/PaR) established and governed by GFRMC oversight, along with business unit market risk policies.

Volumetric limits are supported by PaR and VaR methodologies in the UK and in North America and a VaR methodology in Europe to measure the Group's exposure to commodity price risk. Limits are also set on PaR and VaR measurements as a further control over exposure to market prices. PaR measures the estimated potential loss in a position or portfolio of positions associated with the movement of a commodity price for a given confidence level, over the remaining term of the position or contract portfolio. VaR measures the estimated potential loss for a given confidence level over a predetermined holding period. The standard confidence level used is 95%. In addition, stress tests are regularly performed to evaluate the impact of substantial movements in commodity prices.

4. Financial risk management continued

The Group measures and manages the commodity price risk associated with the Group's entire energy procurement, upstream and downstream portfolio. Only certain of the Group's energy procurement, upstream and downstream contracts constitute financial instruments under IAS 39 (note 2). As a result, while the Group manages the commodity price risk associated with both financial and non-financial energy procurement, upstream and downstream contracts, it is the notional value of energy contracts being carried at fair value that represents the exposure of the Group's energy procurement, upstream and downstream activities to commodity price risk according to IFRS 7, Financial Instruments: Disclosures. This is because energy contracts that are financial instruments under IAS 39 are accounted for on a fair value basis and changes in fair value immediately impact profit or equity. Conversely, energy contracts that are not financial instruments under IAS 39 are accounted for as executory contracts and changes in fair value do not immediately impact profit or equity, and as such, are not exposed to commodity price risk as defined by IFRS 7. So whilst the PaR or VaR associated with energy procurement and downstream contracts outside the scope of IAS 39 is monitored for internal risk management purposes, only those energy contracts within the scope of IAS 39 are within the scope of the IFRS 7 disclosure requirements.

The net gain within operating profit of £1,163 million (2009: £71 million loss) on the re-measurement of energy contracts largely represents net gains on settlements or delivery of contracts. As gas and power were delivered under these contracts, net out of the money positions from 2009 unwound, generating a net credit to the income statement. There were also unrealised mark-to-market gains created by gas and power purchase contracts which are priced below the current wholesale market value of energy. These gains are calculated with reference to forward energy prices and therefore the extent of the economic gain or loss arising over the life of these contracts is uncertain, and entirely dependent upon the level of future wholesale energy prices. Generally, subject to short-term balancing, the ultimate net charge to cost of sales will be consistent with the price of energy agreed in these contracts and the fair value adjustments will reverse as the energy is supplied over the life of the contract.

The carrying value of energy contracts used in energy procurement, upstream and downstream activities at 31 December 2010 is disclosed in note 22. A sensitivity analysis that is intended to illustrate the sensitivity of the Group's financial position and performance to changes in the fair value or future cash flows of financial instruments associated with the Group's energy procurement, upstream and downstream activities as a result of changes in commodity prices is provided below in section (e).

(ii) Proprietary energy trading

The Group's proprietary energy trading activities consist of physical and financial commodity purchases and sales contracts taken on with the intent of benefiting in the short term from changes in market prices or differences between buying and selling prices. The Group conducts its trading activities in the over-the-counter market and through exchanges in the UK, North America and continental Europe. The Group is exposed to commodity price risk as a result of its proprietary energy trading activities because the value of its trading assets and liabilities will fluctuate with changes in market prices for commodities.

The Group sets volumetric and VaR limits to manage the commodity price risk exposure associated with the Group's proprietary energy trading activities. The VaR used measures the estimated potential loss for a 95% confidence level over a one-day holding period. The holding period used is based on market liquidity and the number of days the Group would expect it to take to close out a trading position.

As with any modelled risk measure, there are certain limitations that arise from the assumptions used in the VaR analysis. VaR assumes that the future will behave like the past and that the Group's trading positions can be unwound or hedged within the predetermined holding period. Furthermore, the use of a 95% confidence level, by definition, does not take into account changes in value that might occur beyond this confidence level.

The VaR, before taxation, associated with the Group's proprietary energy trading activities at 31 December 2010 was £0.2 million (2009: £1.6 million). The carrying value of energy contracts used in proprietary energy trading activities at 31 December 2010 is disclosed in note 22.

(b) Currency risk management

The Group is exposed to currency risk on foreign currency denominated forecast transactions, firm commitments, monetary assets and liabilities (transactional exposure) and on its net investments in foreign operations (translational exposure).

(i) Transactional currency risk

The Group is exposed to transactional currency risk on transactions denominated in currencies other than the underlying functional currency of the commercial operation transacting. The Group's primary functional currencies are pounds sterling in the UK, Canadian dollars in Canada, US dollars in the US, Norwegian krone in Norway and euros in The Netherlands. The risk is that the functional currency value of cash flows will vary as a result of movements in exchange rates. Transactional exposure arises from the Group's energy procurement activities in the UK and in Canada, where a number of transactions are denominated in euros or US dollars and on certain capital commitments denominated in foreign currencies. In addition, in order to optimise the cost of funding, the Group has, in certain cases, issued foreign currency denominated debt, primarily in US dollars, New Zealand dollars, euros or Japanese yen.

It is the Group's policy to hedge all material transactional exposures using forward contracts to fix the functional currency value of non-functional currency cash flows. At 31 December 2010, there were no material unhedged non-functional currency monetary assets or liabilities, firm commitments or probable forecast transactions (2009: £nil), other than foreign currency borrowings used to hedge translational exposures.

(ii) Translational currency risk

The Group is exposed to translational currency risk as a result of its net investments in North America and Europe. The risk is that the pounds sterling value of the net assets of foreign operations will decrease with changes in foreign exchange rates. The Group's policy is to protect the pounds sterling book value of its net investments in foreign operations, subject to certain parameters monitored by the GFRMC, by holding foreign currency debt, entering into foreign currency derivatives, or a mixture of both.

The Group manages translational currency risk taking into consideration the cash impact of any hedging activity as well as the risk to the net asset numbers in the Group's Financial Statements. The translation hedging programme including the potential cash impact is monitored by the GFRMC.

4. Financial risk management continued

The Group measures and manages the currency risk associated with all transactional and translational exposures. In contrast, IFRS 7 only requires disclosure of currency risk arising on financial instruments denominated in a currency other than the functional currency of the commercial operation transacting. As a result, for the purposes of IFRS 7, currency risk excludes the Group's net investments in North America and Europe as well as foreign currency denominated forecast transactions and firm commitments. A sensitivity analysis that is intended to illustrate the sensitivity of the Group's financial position and performance to changes in the fair value or future cash flows of foreign currency denominated financial instruments as a result of changes in foreign exchange rates is provided below in section (e).

(c) Interest rate risk management

In the normal course of business the Group borrows to finance its operations. The Group is exposed to interest rate risk because the fair value of fixed rate borrowings and the cash flows associated with floating rate borrowings will fluctuate with changes in interest rates. The Group's policy is to manage the interest rate risk on long-term borrowings by ensuring the exposure to floating interest rates remains within a 30% to 70% range, including the impact of interest rate derivatives. A sensitivity analysis that is intended to illustrate the sensitivity of the Group's financial position and performance to changes in interest rates is provided below in section (e).

(d) Equity price risk management

The Group is exposed to equity price risk because certain available-for-sale financial assets, held by the Law Debenture Trust on behalf of the Company as security in respect of the Centrica Unapproved Pension Scheme, are linked to equity indices (note 36). Investments in equity indices are inherently exposed to less risk than individual equity investments because they represent a naturally diverse portfolio. Note 36 details the Group's other retirement benefit assets and liabilities.

(e) Sensitivity analysis

IFRS 7 requires disclosure of a sensitivity analysis that is intended to illustrate the sensitivity of the Group's financial position and performance to changes in market variables (commodity prices, foreign exchange rates and interest rates) as a result of changes in the fair value or cash flows associated with the Group's financial instruments. The sensitivity analysis provided discloses the effect on profit or loss and equity at 31 December 2010 assuming that a reasonably possible change in the relevant risk variable had occurred at 31 December 2010 and been applied to the risk exposures in existence at that date to show the effects of reasonably possible changes in price on profit or loss and equity to the next annual reporting date. Reasonably possible changes in market variables used in the sensitivity analysis are based on implied volatilities, where available, or historical data for energy prices and foreign exchange rates. Reasonably possible changes in interest rates are based on management judgement and historical experience.

The sensitivity analysis has been prepared based on 31 December 2010 balances and on the basis that the balances, the ratio of fixed to floating rates of debt and derivatives, the proportion of energy contracts that are financial instruments, the proportion of financial instruments in foreign currencies and the hedge designations in place at 31 December 2010 are all constant. Excluded from this analysis are all non-financial assets and liabilities and energy contracts that are not financial instruments under IAS 39. The sensitivity to foreign exchange rates relates only to monetary assets and liabilities denominated in a currency other than the functional currency of the commercial operation transacting, and excludes the translation of the net assets of foreign operations to pounds sterling, but includes the corresponding impact of financial instruments used in net investment hedges.

The sensitivity analysis provided is hypothetical only and should be used with caution as the impacts provided are not necessarily indicative of the actual impacts that would be experienced because the Group's actual exposure to market rates is changing constantly as the Group's portfolio of commodity, debt and foreign currency contracts changes. Changes in fair values or cash flows based on a variation in a market variable cannot be extrapolated because the relationship between the change in market variable and the change in fair value or cash flows may not be linear. In addition, the effect of a change in a particular market variable on fair values or cash flows is calculated without considering interrelationships between the various market rates or mitigating actions that would be taken by the Group. The sensitivity analysis provided below excludes the impact of proprietary energy trading assets and liabilities because the VaR associated with the Group's proprietary energy trading activities has already been provided above in section (a).

4. Financial risk management continued

The impacts of reasonably possible changes in commodity prices on profit and equity, both after taxation, based on the assumptions provided above are as follows:

	2010		2009	
Energy prices	**Base price (i)**	**Reasonably possible change in variable**	Base price (i)	Reasonably possible change in variable
UK gas (p/therm)	**59**	**+/–11**	41	+/–10
UK power (£/MWh)	**51**	**+/–5**	41	+/–5
UK coal (US$/tonne)	**121**	**+/–21**	99	+/–20
UK emissions (€/tonne)	**14**	**+/–2**	13	+/–3
UK oil (US$/bbl)	**95**	**+/–18**	86	+/–19
North American gas (USc/therm)	**52**	**+/–9**	65	+/–11
North American power (US$/MWh)	**48**	**+/–4**	61	+/–5
European power (€/MWh)	**55**	**+/–8**	53	+/–5

(i) The base price represents the average forward market price over the duration of the active market curve used in the sensitivity analysis provided.

	2010		2009	
Incremental profit/(loss)	**Impact on profit £m**	**Impact on equity £m**	Impact on profit £m	Impact on equity £m
UK energy prices (combined) – increase/(decrease)	**98/(79)**	**32/(32)**	38/(38)	30/(30)
North American energy prices (combined) – increase/(decrease)	**25/(25)**	**7/(7)**	46/(46)	21/(21)
European energy prices (combined) – increase/(decrease)	**10/(10)**	**–/–**	14/(14)	–/–

The impacts of reasonably possible changes in interest rates on profit and equity, both after taxation, based on the assumptions provided above are as follows:

	2010			2009		
Interest rates and incremental profit/(loss)	**Reasonably possible change in variable %**	**Impact on profit £m**	**Impact on equity £m**	Reasonably possible change in variable %	Impact on profit £m	Impact on equity £m
UK interest rates	**+/–1.0**	**14/(12)**	**14/(18)**	+/–1.0	5/(9)	16/(19)
US interest rates	**+/–1.0**	**2/(6)**	**–/–**	+/–1.0	6/(7)	(7)/9
Canadian interest rates	**+/–1.0**	**2/(3)**	**–/–**	+/–1.0	4/(4)	–/–
Euro interest rates	**+/–1.0**	**(7)/5**	**–/–**	+/–1.0	(12)/12	–/–
Japanese interest rates	**+/–1.0**	**–/–**	**(16)/21**	+/–1.0	–/–	(13)/17

The impacts of reasonably possible changes in foreign currency rates relative to pounds sterling on profit and equity, both after taxation, based on the assumptions provided above are as follows:

	2010			2009		
Foreign exchange rates and incremental profit/(loss)	**Reasonably possible change in variable %**	**Impact on profit £m**	**Impact on equity £m**	Reasonably possible change in variable %	Impact on profit £m	Impact on equity £m
US dollar	**+/–10**	**(75)/94**	**20/(18)**	+/–10	(43)/51	4/(2)
Canadian dollar	**+/–10**	**(20)/20**	**52/(43)**	+/–10	–/3	10/(10)
Euro	**+/–10**	**(28)/33**	**(5)/7**	+/–10	(3)/(8)	14/(9)
Danish krone	**+/–10**	**–/–**	**–/–**	+/–10	–/–	27/(33)
Norwegian krone	**+/–10**	**–/1**	**13/(11)**	+/–10	(1)/1	5/(6)

4. Financial risk management continued

Credit risk management

Credit risk is the risk of loss associated with a counterparty's inability or failure to discharge its obligations under a contract. The Group is exposed to credit risk in its treasury, trading, energy procurement and downstream activities. The Group continues to take steps to tighten downstream credit policies, including the tightening of credit scores in customer management processes, whilst continuing to manage credit risk in accordance with financial risk management processes.

Note 22 provides further detail of the Group's exposure to credit risk on derivative financial instruments, note 21 provides detail of the Group's exposure to credit risk on trade and other receivables, note 24 provides detail of the Group's exposure to credit risk on cash and cash equivalents and note 29 provides the carrying value of all financial assets representing the Group's maximum exposure to credit risk.

(a) Treasury, trading and energy procurement activities

Wholesale counterparty credit exposures are monitored by individual counterparty and by category of credit rating, and are subject to approved limits. The majority of significant exposures are with counterparties rated A–/A3 or better. The Group uses master netting agreements to reduce credit risk and net settles payments with counterparties where net settlement provisions exist. In addition, the Group employs a variety of other methods to mitigate credit risk: margining, various forms of bank and parent company guarantees and letters of credit.

100% of the Group's credit risk associated with its treasury, trading and energy procurement activities is with counterparties in related energy industries or with financial institutions. The Group measures and manages the credit risk associated with the Group's entire treasury, trading and energy procurement portfolio. In contrast, IFRS 7 defines credit risk as the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation and requires disclosure of information about the exposure to credit risk arising from financial instruments only. Only certain of the Group's energy procurement contracts constitute financial instruments under IAS 39 (note 2). As a result, whilst the Group manages the credit risk associated with both financial and non-financial energy procurement contracts, it is the carrying value of financial assets within the scope of IAS 39 (note 29) that represents the maximum exposure to credit risk in accordance with IFRS 7.

(b) Downstream activities

In the case of business customers, credit risk is managed by checking a company's creditworthiness and financial strength both before commencing trade and during the business relationship. For residential customers, creditworthiness is ascertained normally before commencing trade by reviewing an appropriate mix of internal and external information to determine the payment mechanism required to reduce credit risk to an acceptable level. Certain customers will only be accepted on a prepayment basis or with a security deposit.

In some cases, an ageing of receivables is monitored and used to manage the exposure to credit risk associated with both business and residential customers. In other cases, credit risk is monitored and managed by grouping customers according to the method of payment or profile.

Liquidity risk management and going concern

Liquidity risk is the risk that the Group is unable to meet its financial obligations as they fall due. The Group experiences significant movements in its liquidity position due primarily to the seasonal nature of its business and margin cash arrangements associated with certain wholesale commodity contracts. To mitigate this risk the Group maintains significant committed facilities and holds cash on deposit. The Group's liquidity position has remained strong throughout 2010.

Year ended 31 December	**2010 £m**	2009 £m
Cash pledged as collateral at 1 January	**631**	626
Net cash (inflow)/outflow	**(466)**	79
Transferred to discontinued operations	**–**	(15)
Foreign exchange gains/(losses)	**8**	(59)
Cash pledged as collateral at 31 December (i)	**173**	631

(i) Within discontinued operations there was also a net £25 million cash outflow of collateral in the period (2009: £26 million inflow). The closing balance of cash pledged within discontinued operations was £11 million (2009: £6 million) and cash held was £nil (2009: £18 million).

The Group has a number of treasury and risk policies to monitor and manage liquidity risk. Cash forecasts identifying the Group's liquidity requirements are produced regularly and are stress-tested for different scenarios, including, but not limited to, reasonably possible increases or decreases in commodity prices and the potential cash implications of a credit rating downgrade. The Group seeks to ensure that sufficient financial headroom exists for at least a 12-month period to safeguard the Group's ability to continue as a going concern. It is the Group's policy to maintain committed facilities and/or available surplus cash resources of at least £1,200 million, to raise at least 75% of its net debt (excluding non-recourse debt) in the long-term debt market and to maintain an average term to maturity in the recourse long-term debt portfolio greater than five years.

At 31 December 2010, the Group had undrawn committed credit facilities of £2,873 million (2009: £2,083 million) and £467 million (2009: £1,294 million) of cash and cash equivalents. 121% (2009: 148%) of the Group's net debt has been raised in the long-term debt market and the average term to maturity of the long-term debt portfolio was 10.5 years (2009: 9.6 years).

The relatively high level of undrawn committed bank borrowing facilities and available cash resources has enabled the Directors to conclude that the Group has sufficient headroom to continue as a going concern. The statement of going concern is included in the Directors' Report – Governance, on page 48.

Maturities of derivative financial liabilities, trade and other payables, bank borrowings and provisions are provided in notes 22, 25, 26 and 28, respectively. Details of commitments and contingencies are provided in note 39.

5. Capital management

The Group funds its business using a combination of debt and shareholders' equity. The Group's capital employed was financed as follows:

31 December	2010 £m	2009 £m
Current and non-current borrowings	**4,036**	4,680
Deduct:		
Cash and cash equivalents	**(467)**	(1,294)
Current and non-current securities	**(257)**	(250)
Net debt (note 34b)	**3,312**	3,136
Shareholders' equity	**5,819**	4,192
Capital	**9,131**	7,328

The Group seeks to maintain an efficient capital structure with a balance of debt and equity. Debt levels are restricted to limit the risk of financial distress and, in particular, to maintain strong credit ratings. The Group's credit ratings are important in keeping the cost of debt down, in limiting collateral requirements in energy trading and hedging, and in ensuring the Group is an attractive counterparty to gas and power producers and to customers for longer term energy contracts. At 31 December 2010, the Group's long-term credit rating was A3 stable outlook for Moody's Investor Services Inc. and A– stable outlook for Standard & Poor's Rating Services. These ratings did not change during 2010.

The Group monitors its current and projected capital position on a regular basis, considering a medium-term view of three to five years, and different stress case scenarios, including the impact of changes in the Group's credit ratings and significant movements in commodity prices. A number of financial ratios are monitored, including those used by the credit rating agencies, such as debt to cash flow ratios and EBITDA [(i)] to gross interest expense. At 31 December 2010, the ratio of the Group's net debt to EBITDA was 1.0 (2009: 1.2). EBITDA to gross interest expense for the year ended 31 December 2010 was 6.7 (2009: 5.3).

The Group is not subject to externally-imposed capital requirements but, as is common for most companies, the level of debt that can be raised is restricted by the Company's Articles of Association. Net debt is limited to the greater of £5.0 billion and a gearing ratio of three times adjusted capital and reserves. This restriction can be amended or removed by the shareholders of the Company passing a special resolution. Based on adjusted capital and reserves as at 31 December 2010 of £5.8 billion, the limit for net debt was £17.4 billion.

The Group funds its debt principally through issuing bonds, denominated in pounds sterling, euros and US dollars. The Group also maintains substantial committed facilities from banks, but generally uses these to provide back up liquidity and does not typically draw on them.

(i) EBITDA is defined as earnings before interest, tax, depreciation, amortisation, and exceptional items and certain re-measurements from continuing operations.

6. Segmental analysis

Centrica's operating segments are those used internally by management to run the business and make decisions. Centrica's operating segments are based on products and services provided in each geographical area. The operating segments are also the Group's reportable segments. The types of products and services from which each reportable segment derives its revenues are:

Segment	Description
Downstream UK:	
Residential energy supply	The supply of gas and electricity to residential customers in the UK
Residential services	Installation, repair and maintenance of domestic central heating, plumbing and drains, gas appliances and kitchen appliances, including the provision of fixed-fee maintenance/breakdown service and insurance contracts in the UK
Business energy supply and services	The supply of gas and electricity and provision of energy-related services to business customers in the UK
Upstream UK:	
Upstream gas and oil	Production and processing of gas and oil and the development of new fields to grow reserves
Power generation	Generation and optimisation of power from gas, nuclear and wind sources
Industrial and commercial	Management, optimisation and scheduling of wholesale and industrial commodity sales, procurement and tolling contracts
Proprietary energy trading	Trading in physical and financial energy contracts
Storage UK	Gas storage in the UK
North America:	
Residential energy supply	The supply of gas and electricity to residential customers in North America
Business energy supply	The supply of gas, electricity and energy-related services to business customers in North America
Residential and business services	Installation and maintenance of Heating, Ventilation and Air Conditioning (HVAC) equipment, water heaters and the provision of breakdown services in North America
Upstream and wholesale energy	Gas production, power generation and procurement and trading activities in the North American wholesale energy markets

6. Segmental analysis continued

The measure of profit used by the Centrica Executive Committee is adjusted operating profit. Adjusted operating profit is operating profit before exceptional items and certain re-measurements (refer to note 9), before additional depreciation resulting from any fair value uplifts on Strategic Investments (refer to notes 2 and 14) and including the results from joint ventures and associates which are included before interest and tax. All transactions between segments are on an arm's length basis.

Year ended 31 December			2010			2009 (restated) (ii)
(a) Revenue	**Gross segment revenue £m**	**Less inter-segment revenue (i) £m**	**Group revenue £m**	Gross segment revenue £m	Less inter-segment revenue (i) £m	Group revenue £m
Continuing operations:						
Residential energy supply (ii)	**8,359**	**(4)**	**8,355**	7,911	–	7,911
Residential services (ii)	**1,464**	**–**	**1,464**	1,338	–	1,338
Business energy supply and services	**2,907**	**(1)**	**2,906**	3,316	–	3,316
Downstream UK	**12,730**	**(5)**	**12,725**	12,565	–	12,565
Upstream gas and oil	**1,637**	**(773)**	**864**	1,240	(689)	551
Power generation	**1,112**	**(7)**	**1,105**	1,317	(167)	1,150
Industrial and commercial	**2,017**	**(423)**	**1,594**	1,907	(555)	1,352
Proprietary energy trading (iii)	**17**	**(15)**	**2**	52	(11)	41
Upstream UK	**4,783**	**(1,218)**	**3,565**	4,516	(1,422)	3,094
Storage UK	**267**	**(35)**	**232**	266	(70)	196
Residential energy supply	**2,502**	**–**	**2,502**	2,644	–	2,644
Business energy supply	**2,682**	**–**	**2,682**	2,491	–	2,491
Residential and business services	**485**	**–**	**485**	406	–	406
Upstream and wholesale energy	**328**	**(96)**	**232**	656	(89)	567
North America	**5,997**	**(96)**	**5,901**	6,197	(89)	6,108
	23,777	**(1,354)**	**22,423**	23,544	(1,581)	21,963
Discontinued operations:						
European Energy (note 38)	**590**	**–**	**590**	2,357	–	2,357

(i) Inter-segment revenue is subject to year on year fluctuations due to the change in the mix of internal and external energy sales by Upstream UK.
(ii) To align with management responsibilities, the British Gas Community Energy business has been reallocated from the Residential services segment to Residential energy supply. The 2009 comparatives have been adjusted accordingly.
(iii) The external revenue presented for Proprietary energy trading comprises both realised (settled) and unrealised (fair value changes) from trading in physical and financial energy contracts. Inter-segment revenue arising in Proprietary energy trading represents the recharge of brokerage fees to other Group segments.

The Group operates in the following geographical areas:

Year ended 31 December	Revenue (based on location of customer)	
	2010 £m	2009 (i) £m
Continuing operations:		
UK	**15,811**	15,216
USA	**3,984**	3,946
Canada	**1,918**	2,162
Germany	**514**	563
Netherlands	**99**	23
Norway	**58**	53
Denmark	**24**	–
Trinidad and Tobago	**15**	–
	22,423	21,963

(i) Following the acquisition of a number of assets outside of the UK, including Trinidad and Tobago and Wildcat Hills (note 37), the Group has reviewed the allocation and presentation of geographic locations of revenue and re-presented the 2009 allocation accordingly.

6. Segmental analysis continued

Year ended 31 December

(b) Operating profit	2010 £m	2009 (restated) (i) £m
Continuing operations:		
Residential energy supply (i)	**742**	598
Residential services (i)	**241**	230
Business energy supply and services	**233**	183
Downstream UK	**1,216**	1,011
Upstream gas and oil (ii)	**581**	444
Power generation (ii)	**226**	147
Industrial and commercial	**(36)**	(93)
Proprietary energy trading	**–**	27
Upstream UK	**771**	525
Storage UK	**169**	168
Residential energy supply	**177**	94
Business energy supply	**88**	34
Residential and business services	**15**	18
Upstream and wholesale energy	**(46)**	7
North America	**234**	153
Adjusted operating profit – segment operating profit before exceptional items, certain re-measurements and impact of fair value uplifts from Strategic Investments (iii)	**2,390**	1,857
Share of joint ventures/associates' interest and taxation	**(78)**	(11)
Other (iv)	**–**	(5)
Depreciation of fair value uplifts to property, plant and equipment – Venture (ii)	**(60)**	(20)
Depreciation of fair value uplifts to property, plant and equipment (net of taxation) – associates – British Energy (ii)	**(58)**	(7)
	2,194	1,814
Exceptional items (note 9)	**(283)**	(568)
Certain re-measurements included within gross profit (note 9)	**1,177**	(62)
Certain re-measurements of associates' energy contracts (net of taxation) (note 9)	**(14)**	(9)
Operating profit after exceptional items and certain re-measurements	**3,074**	1,175
Discontinued operations:		
European Energy (note 38) (v)	**(5)**	(8)

(i) To align with management responsibilities, the British Gas Community Energy business has been reallocated from the Residential services segment to Residential energy supply. The 2009 comparatives have been adjusted accordingly.
(ii) See note 2 and note 14 for explanation of the depreciation on fair value uplifts to property, plant and equipment on acquiring Strategic Investments.
(iii) Includes results of equity-accounted interests before interest, taxation, certain re-measurements and depreciation on fair value uplifts to property, plant and equipment on Strategic Investments.
(iv) In 2009 Other comprised a £1 million loss relating to Corporate centre costs not recharged to segments and a £4 million loss relating to an inter-segment transaction between a Proprietary trading operation and a non-proprietary energy trading operation.
(v) Represents loss after taxation and before exceptional items and certain re-measurements attributable to equity holders of the parent. This is the measure of results of discontinued operations that is reported regularly to the Group's Executive Committee.

6. Segmental analysis continued

Year ended 31 December	Share of results of joint ventures and associates before interest and taxation		Depreciation and Impairments of property, plant and equipment (i)		Amortisation, write-downs and impairments of intangibles (restated) (v)	
(c) Included within adjusted operating profit	**2010 £m**	2009 £m	**2010 £m**	2009 £m	**2010 £m**	2009 £m
Continuing operations:						
Residential energy supply (ii), (v)	**–**	–	**6**	8	**38**	54
Residential services	**–**	–	**9**	12	**1**	10
Business energy supply and services	**–**	–	**2**	2	**7**	7
Downstream UK	**–**	–	**17**	22	**46**	71
Upstream gas and oil (i), (ii)	**3**	–	**487**	353	**81**	16
Power generation (i), (iii), (v)	**140**	28	**120**	112	**1**	4
Industrial and commercial	**–**	–	**–**	1	**10**	6
Proprietary energy trading	**–**	–	**–**	–	**–**	–
Upstream UK	**143**	28	**607**	466	**92**	26
Storage UK	**–**	–	**26**	23	**–**	–
Residential energy supply	**–**	–	**–**	2	**5**	6
Business energy supply	**–**	–	**1**	1	**4**	3
Residential and business services	**–**	–	**2**	2	**5**	2
Upstream and wholesale energy (ii)	**–**	–	**88**	71	**3**	2
North America	**–**	–	**91**	76	**17**	13
Other (iv)	**–**	–	**15**	12	**19**	15
	143	28	**756**	599	**174**	125
Discontinued operations:						
European Energy (note 38) (ii)	**–**	2	**–**	25	**–**	17

(i) Depreciation of property, plant and equipment is stated before depreciation of fair value uplifts for Strategic Investments.
(ii) During 2010, impairment charges of £15 million (2009: £35 million) were incurred within business performance in the Downstream UK – Residential energy supply segment relating to emissions allowances and write-downs of £81 million (2009: £16 million) in the Upstream – UK Upstream gas and oil segment and £2 million (2009: £nil) in the North America – Upstream and wholesale energy segment relating to exploration and evaluation assets, as described in note 16.
(iii) Share of results of joint ventures and associates is before interest, certain re-measurements, depreciation of fair value uplifts to property, plant and equipment on Strategic Investments and taxation.
(iv) Other comprises depreciation of property, plant and equipment and amortisation and write-downs of intangibles on Corporate centre assets which are charged out to other Group segments.
(v) Gas and power contract positions related to UK customers have been reallocated from the Upstream UK – Power generation segment to the Downstream UK – Residential energy supply segment (see note 6(d)). The associated impairments of emissions certificates have been restated.

6. Segmental analysis continued

31 December	Net segment assets/(liabilities) (restated) (ii), (iii), (vi), (vii)		Average capital employed Year ended 31 December (restated) (iv)	
(d) Assets and liabilities	**2010 £m**	2009 £m	**2010 £m**	2009 £m
Residential energy supply (i), (vi)	**27**	(28)	**195**	187
Residential services (vi)	**225**	21	**95**	42
Business energy supply and services (i)	**516**	445	**552**	502
Downstream UK	**768**	438	**842**	731
Upstream gas and oil (iii)	**2,691**	2,355	**1,245**	499
Power generation(ii), (iii), (vii)	**3,633**	3,629	**3,506**	1,879
Industrial and commercial(ii), (iii)	**128**	–	**(49)**	285
Proprietary energy trading (iii), (iv)	**119**	573	**(16)**	(68)
Upstream UK	**6,571**	6,557	**4,686**	2,595
Storage UK	**347**	359	**206**	191
Residential energy supply (iv)	**731**	790	**709**	808
Business energy supply (iv)	**441**	377	**288**	277
Residential and business services	**400**	268	**323**	270
Upstream and wholesale energy (vii)	**784**	638	**659**	594
North America	**2,356**	2,073	**1,979**	1,949
	10,042	9,427	**7,713**	5,466
Unallocated deferred tax assets (i)	**233**	723		
Derivative financial instruments held for energy procurement including balances held by joint ventures and associates	**(715)**	(2,076)		
Treasury derivatives	**63**	55		
Current tax liabilities (i)	**(16)**	(81)		
Securities (viii)	**257**	250		
Assets of discontinued operations (v), (vii)	**87**	60		
Bank overdrafts and loans	**(4,036)**	(4,680)		
Retirement benefit obligations	**(239)**	(565)		
Corporate centre assets (viii)	**143**	1,142		
Non-operating liabilities	**(4,223)**	(5,172)		
	5,819	4,255		

(i) Segment assets and liabilities include allocated current and deferred tax balances.
(ii) Restated to align comparatives with the 2010 presentation of gas and power contract positions related to UK customers within Downstream UK.
(iii) During 2010 Upstream UK changed its allocation process for inter-company funding and operating balances. The 2009 comparative has been restated to reflect this change.
(iv) Average capital employed calculation for 2010 has been calculated in line with the latest management reporting of average capital employed. Average capital employed excludes balances related to margin call debtors and now includes balances related to proprietary energy trading derivatives so the comparatives have been restated.
(v) Assets and liabilities of discontinued operations are classified as held for sale, as explained in note 38.
(vi) To align with management responsibilities, the British Gas Community Energy business has been reallocated from the Residential services segment to Residential energy supply. The 2009 comparatives have been adjusted accordingly.
(vii) To align with average capital employed, net segment assets/liabilities have been restated to include assets held for sale.
(viii) Corporate short-term deposits are considered to be a Corporate centre asset. The 2009 comparatives have been reallocated accordingly.

Capital employed represents the investment required to operate each of the Group's segments. Capital employed is used by the Group to calculate the return on capital employed for each of the Group's segments as part of the Group's managing for value concept. Additional value is created when the return on capital employed exceeds the cost of capital. Net segment assets of the Group can be reconciled to the Group's capital employed as follows:

	2010 £m	2009 (restated) (i) £m
Net segment assets at 31 December	**10,042**	9,427
Deduct:		
Intra-Group balances	**26**	46
Pre-productive assets	**(1,659)**	(1,729)
Margin call debtor (i)	**(161)**	(626)
Cash at bank, in transit and in hand excluding certain restricted cash	**(117)**	(92)
Effect of averaging month-end balances	**(418)**	(1,560)
Average capital employed for year ended 31 December	**7,713**	5,466

(i) Average capital employed calculation for 2010 has been calculated in line with latest management reporting of average capital employed. Average capital employed excludes balances related to margin call debtors and now includes balances related to proprietary energy trading derivatives. The 2009 comparative has been restated to reflect this change.

6. Segmental analysis continued

(e) Capital expenditure

Year ended 31 December	Capital expenditure on property, plant and equipment (note 18) 2010 £m	Capital expenditure on property, plant and equipment (note 18) 2009 £m	Capital expenditure on intangible assets other than goodwill (note 16) 2010 £m	Capital expenditure on intangible assets other than goodwill (note 16) 2009 (restated) (i) £m
Continuing operations:				
Residential energy supply (i)	**15**	1	**256**	236
Residential services	**6**	34	**15**	6
Business energy supply and services (i)	**1**	1	**68**	59
Downstream UK	**22**	36	**339**	301
Upstream gas and oil	**383**	358	**224**	50
Power generation (i)	**78**	139	**19**	45
Industrial and commercial	**4**	4	**15**	16
Proprietary energy trading	**–**	–	**–**	–
Upstream UK	**465**	501	**258**	111
Storage UK	**33**	60	**–**	–
Residential energy supply	**–**	–	**2**	6
Business energy supply	**–**	1	**10**	6
Residential and business services	**2**	1	**5**	–
Upstream and wholesale energy	**20**	52	**10**	2
North America	**22**	54	**27**	14
Other	**16**	3	**29**	38
Capital expenditure on continuing operations	**558**	654	**653**	464
Increase/(decrease) in prepayments related to capital expenditure	**18**	(2)	**6**	–
Unrealised gains on cash flow hedges transferred from reserves	**–**	4	**–**	–
Capitalised borrowing costs	**(37)**	(34)	**–**	–
Decrease/(increase) in trade payables related to capital expenditure	**8**	(28)	**2**	140
Net cash outflow	**547**	594	**661**	604

The Group operates in the following geographical areas:

31 December	Non-current assets (based on location of assets) (ii) 2010 £m	Non-current assets (based on location of assets) (ii) 2009 (iii) £m
Continuing operations:		
UK	**8,248**	8,236
Canada	**1,381**	1,126
USA	**820**	686
Netherlands	**839**	822
Norway	**752**	428
Trinidad and Tobago	**319**	5
	12,359	11,303

(i) Gas and power contract positions related to UK customers have been reallocated from the Upstream UK – Power generation segment to the Downstream UK – Residential energy supply segment (see note 6(d)). The associated Renewable Obligation Certificates (ROCs) purchases and emissions certificates purchases have been reallocated and the 2009 comparative restated.
(ii) Non-current assets exclude financial instruments, deferred tax assets and post-employment benefit assets.
(iii) Following the acquisition of a number of assets outside of the UK, including Trinidad and Tobago and Wildcat Hills (note 37), the Group has reviewed the allocation and presentation of geographic locations of its non-current assets and re-presented the 2009 allocation accordingly. Revenue has also been re-presented on the same basis (note 6a).

7. Costs of continuing operations

Analysis of costs by nature	2010 £m	2009 £m
Transportation, distribution and metering costs	**(3,627)**	(3,503)
Commodity costs (i)	**(11,295)**	(12,036)
Depreciation, amortisation and write-downs	**(770)**	(590)
Employee costs	**(565)**	(492)
Other direct costs relating to the upstream businesses	**(273)**	(289)
Other direct costs relating to the downstream businesses	**(1,065)**	(753)
Total cost of sales before exceptional items and certain re-measurements	**(17,595)**	(17,663)
Exceptional items and certain re-measurements (note 9)	**1,075**	(455)
Total cost of sales	**(16,520)**	(18,118)
Depreciation, amortisation and write-downs	**(224)**	(155)
Employee costs	**(1,068)**	(942)
Exploration costs expensed	**(7)**	(28)
Impairment of trade receivables (note 21)	**(269)**	(354)
Foreign exchange gains/(losses)	**1**	(2)
Other costs associated with upstream businesses	**(137)**	(151)
Other costs associated with downstream businesses	**(937)**	(864)
Total operating costs before exceptional items and certain re-measurements	**(2,641)**	(2,496)
Exceptional items and certain re-measurements (note 9)	**(181)**	(175)
Total operating costs	**(2,822)**	(2,671)

(i) Includes £167 million relating to the closing out of some out-of-the-money contracts for delivery of gas during 2011 and 2012.

8. Directors and employees

(a) Employee costs (i)	2010 £m	2009 £m
Wages and salaries	**(1,345)**	(1,223)
Social security costs	**(115)**	(103)
Other pension and retirement benefits costs	**(134)**	(77)
Share scheme costs	**(48)**	(38)
	(1,642)	(1,441)
Capitalised employee costs	**9**	7
Employee costs recognised in the Group Income Statement	**(1,633)**	(1,434)

(i) Details of Directors' remuneration, share-based payments and pension entitlements in the Remuneration Report on pages 58 to 63 form part of these Financial Statements. Details of employee share-based payments are given in note 35. Details of the remuneration of key management personnel are given in note 40.

(b) Average number of employees during the year	2010 Number	2009 Number
Downstream UK	**27,298**	26,216
Upstream UK	**1,556**	1,341
Storage UK	**255**	224
North America	**5,534**	5,042
Other operations (i), (ii)	**327**	1,302
	34,970	34,125
UK	**28,994**	27,674
USA	**3,146**	2,706
Canada	**2,388**	2,336
Netherlands (iii)	**260**	237
Spain (iv)	**126**	134
Norway	**30**	25
Germany	**18**	19
Rest of World (ii)	**8**	994
	34,970	34,125

(i) Includes 327 employees (2009: 1,302 employees) of European businesses which are classified as discontinued operations (note 38).
(ii) 2009 number includes average employee numbers of Segebel S.A. from the date of consolidation (20 January 2009) up to the date of disposal (26 November 2009).
(iii) Includes 201 employees (2009: 186 employees) of Oxxio B.V. which is classified as a discontinued operation (note 38).
(iv) Represents employees of Centrica Energía which is classified as a discontinued operation up to the date of disposal (4 November 2010).

9. Exceptional items and certain re-measurements

(a) Exceptional items for the year ended 31 December	2010 £m	2009 £m
Continuing operations:		
Provision for UK onerous gas procurement contract	**(35)**	(199)
Termination of a UK energy sales contract	**–**	(139)
Provision for North American wind power purchase agreements	**(67)**	(55)
Exceptional items from continuing operations included within gross profit	**(102)**	(393)
Impairments:		
Impairment of UK generation, exploration and production assets (i)	**(96)**	(79)
Impairment of North American assets	**(67)**	(70)
	(163)	(149)
UK contract re-negotiation and restructuring costs (ii)	**(43)**	(75)
Profit on disposal of investments (iii)	**25**	49
	(181)	(175)
Exceptional items from continuing operations included within Group operating profit	**(283)**	(568)
Taxation on exceptional items (note 11)	**118**	186
Net exceptional items from continuing operations after taxation	**(165)**	(382)
Discontinued operations:		
Impairment of Oxxio B.V. goodwill and other assets, provisions and write-offs after taxation	**–**	(24)
Profit on disposal of Segebel S.A. after taxation	**–**	297
Total exceptional items after taxation	**(165)**	(109)

(b) Certain re-measurements for the year ended 31 December	2010 £m	2009 £m
Continuing operations:		
Certain re-measurements recognised in relation to energy contracts:		
Net gains arising on delivery of contracts (iv)	**1,023**	928
Net gains/(losses) arising on market price movements and new contracts (v)	**130**	(1,097)
Net gains/(losses) arising on positions in relation to cross-border transportation or capacity contracts (vi)	**24**	(28)
Reversal of certain re-measurements in relation to the termination of energy sales contracts	**–**	135
Net re-measurements from continuing operations included within gross profit	**1,177**	(62)
Net losses arising on re-measurement of associates' energy contracts (net of taxation) (vii)	**(14)**	(9)
Net re-measurements included within Group operating profit	**1,163**	(71)
Taxation on certain re-measurements (note 11)	**(339)**	(1)
Net re-measurements from continuing operations after taxation	**824**	(72)
Discontinued operations:		
Net re-measurements on energy contracts of discontinued operations after taxation (note 38)	**67**	(107)
Total re-measurements after taxation	**891**	(179)

(i) Impairment charges have been recognised on certain UK generation, exploration and production assets as a result of low spark spreads, updated reserve data and changes in infrastructure development expectations. Of the total impairment, £68 million was recorded against UK power generation assets (property, plant and equipment and inventories) and £58 million against exploration and production assets, net of write-backs of £30 million. See note 18.

(ii) Exceptional restructuring charges have been recorded following the termination and migration of a significant supplier contract as a result of the British Gas integration plan. These have been recorded across the segments within Downstream UK.

(iii) During the year the Group disposed of investments in certain non-core assets acquired as part of the Venture acquisition in 2009.

(iv) As energy is delivered or consumed from previously contracted positions the related fair value recognised in the opening balance sheet (representing the discounted difference between forward energy prices at the opening balance sheet date and the contract price of energy to be delivered) is charged or credited to the Income Statement.

(v) Represents fair value gains/(losses) arising from the change in fair value of future contracted sales and purchase contracts as a result of changes in forward energy prices between reporting dates (or date of inception and the reporting date, where later).

(vi) Comprises movements in fair value arising on proprietary trades in relation to cross-border transportation or storage capacity, on which economic value has been created which is not wholly accounted for under the provisions of IAS 39.

(vii) Includes fair value unwinds relating to the recognition of energy procurement contracts and energy sales contracts at their acquisition-date fair values.

10. Net interest

	2010 Interest expense £m	2010 Interest income £m	2010 Total £m	2009 Interest expense £m	2009 Interest income £m	2009 Total £m
Continuing operations:						
Cost of servicing net debt						
Interest income	–	30	30	–	48	48
Interest expense on bonds, bank loans and overdrafts (i)	(284)	–	(284)	(253)	–	(253)
Interest expense on finance leases	(21)	–	(21)	(22)	–	(22)
	(305)	30	(275)	(275)	48	(227)
(Losses)/gains on revaluation						
(Losses)/gains on fair value hedges	(47)	47	–	(41)	43	2
Fair value (losses)/gains on other derivatives (i),(ii)	(121)	9	(112)	(52)	175	123
Fair value gains on other securities measured at fair value	–	10	10	–	3	3
Net foreign exchange translation of monetary assets and liabilities (iii)	–	85	85	(128)	–	(128)
	(168)	151	(17)	(221)	221	–
Other interest						
Notional interest arising on discounted items	(43)	30	(13)	(24)	29	5
Interest on cash collateral balances	–	1	1	–	4	4
Interest on supplier early payment arrangements	–	2	2	–	5	5
	(43)	33	(10)	(24)	38	14
	(516)	214	(302)	(520)	307	(213)
Capitalised borrowing costs (iv)	37	–	37	34	–	34
Interest (expense)/income	(479)	214	(265)	(486)	307	(179)

(i) On 6 December Centrica reduced its outstanding bond debt principal by £151 million and €353 million, and on 23 December by a further €30 million. The cost of repaying this debt before maturity was £60 million. As part of the same debt reduction and as a result of consequent changes in its currency hedging position, Centrica also cancelled certain outstanding bond-related derivative contracts for a net gain of £9 million.
(ii) Primarily reflects changes in the fair value of derivatives used to hedge the foreign exchange exposure associated with inter-company loans denominated in foreign currencies.
(iii) Primarily reflects foreign exchange gains/(losses) on inter-company loans denominated in foreign currencies.
(iv) Borrowing costs have been capitalised using an average rate of 4.78% (2009: 5.37%).

11. Taxation

(a) Analysis of tax charge for the year	2010 Business performance £m	2010 Exceptional items and certain re-measurements £m	2010 Results for the year £m	2009 Business performance £m	2009 Exceptional items and certain re-measurements £m	2009 Results for the year £m
The tax charge comprises:						
Current tax						
UK corporation tax	(464)	23	(441)	(333)	62	(271)
UK petroleum revenue tax	(223)	–	(223)	(112)	–	(112)
Foreign tax	(15)	(6)	(21)	(30)	4	(26)
Adjustments in respect of prior years	171	–	171	135	4	139
Total current tax	(531)	17	(514)	(340)	70	(270)
Deferred tax						
Current year	(81)	(235)	(316)	(147)	113	(34)
UK petroleum revenue tax	7	–	7	25	–	25
Foreign deferred tax	(39)	7	(32)	11	9	20
Change in tax rates (i)	15	(1)	14	–	–	–
Adjustments in respect of prior years	(79)	(9)	(88)	(80)	(7)	(87)
Total deferred tax	(177)	(238)	(415)	(191)	115	(76)
Total tax on profit from continuing operations (ii)	(708)	(221)	(929)	(531)	185	(346)

(i) The effect of the enacted decrease of 1% to the standard rate of UK corporation tax from 1 April 2011 on the relevant temporary differences at 31 December 2010 was a credit of £14 million.
(ii) Total tax on profit from continuing operations excludes taxation on the Group's share of profits in joint ventures and associates.

Tax on items taken directly to equity is disclosed in notes 31 and 32.

The Group earns its profits primarily in the UK, therefore the tax rate used for tax on profit from ordinary activities is the standard rate for UK corporation tax, which was 28% for 2010 (2009: 28%), with the exception of upstream profits, which were taxed at a UK corporation tax rate of 30% (2009: 30%) plus a supplementary charge at 20% (2009: 20%). Certain upstream assets also bear petroleum revenue tax at 50% (2009: 50%). Taxation for other jurisdictions is calculated at the rates prevailing in those respective jurisdictions.

11. Taxation continued

During June 2010 the UK government announced its intention to propose that Parliament reduce the main rate of UK corporation tax from 28% to 24% by 1 April 2014. The reduction in the corporation tax rate is being phased in over the period to April 2014. At 31 December 2010 the first reduction in the tax rate had been enacted by Parliament and the UK corporation tax rate will be 27% from 1 April 2011. No changes have been made to the rates applicable to UK gas and oil production activities. The current and deferred tax charges, assets and liabilities included within these Financial Statements have been based on the enacted UK corporation tax rates.

The effect of the additional proposed reduction in the UK corporation tax rate by 2014 would be to decrease the net deferred tax liability by £26 million.

(b) Factors affecting the tax charge for the year

The differences between the total tax shown above and the amount calculated by applying the standard rate of UK corporation tax to the profit before tax is as follows:

			2010			2009
	Business performance £m	**Exceptional items and certain re-measurements £m**	**Results for the year £m**	Business performance £m	Exceptional items and certain re-measurements £m	Results for the year £m
Profit from continuing operations before tax	**1,929**	**880**	**2,809**	1,635	(639)	996
Less: share of profits in joint ventures and associates, net of interest and taxation	**(7)**	**14**	**7**	(10)	9	(1)
Group profit from continuing operations before tax	**1,922**	**894**	**2,816**	1,625	(630)	995
Tax on profit from continuing operations at standard UK corporation tax rate of 28% (2009: 28%)	**(538)**	**(250)**	**(788)**	(455)	176	(279)
Effects of:						
Net expenses not deductible for tax purposes	**(42)**	**15**	**(27)**	(32)	9	(23)
Movement in unrecognised deferred tax assets	**(8)**	**1**	**(7)**	(3)	–	(3)
UK petroleum revenue tax rates	**(152)**	**–**	**(152)**	(60)	–	(60)
Overseas tax rates	**(2)**	**(4)**	**(6)**	1	(8)	(7)
Additional charges applicable to upstream profits	**(73)**	**27**	**(46)**	(37)	11	(26)
Changes to tax rates	**15**	**(1)**	**14**	–	–	–
Adjustments in respect of prior years	**92**	**(9)**	**83**	55	(3)	52
Taxation on profit from continuing operations	**(708)**	**(221)**	**(929)**	(531)	185	(346)

(c) Factors that may affect future tax charges

Production of gas and oil within the UK continental shelf is subject to several taxes: corporation tax at 30% (2009: 30%) on profits of gas and oil production; a supplementary charge at 20% (2009: 20%) on profits of gas and oil production (adjusted for financing costs) and petroleum revenue tax (PRT) at 50% (2009: 50%) on income generated from certain gas and oil production (net of certain costs).

PRT is a deductible expense for the purposes of corporation tax and the supplementary charge. The effective rate of tax suffered on profits of UK gas production therefore falls between 50% and 75%. To the extent that the Group's profits are earned from UK gas and oil production, its effective tax rate will remain above the current UK statutory rate of 28% (2009: 28%).

Income earned in North America and other territories outside the UK is generally subject to higher effective rates of tax than the current UK statutory rate. In the medium term, the Group's effective tax rate is expected to remain above the UK statutory rate.

12. Dividends

	2010 £m	2009 £m
Prior year final dividend of 9.14 pence (2009: 8.73 pence) per ordinary share	**470**	447
Interim dividend of 3.84 pence (2009: 3.66 pence) per ordinary share	**198**	188
	668	635

The prior year final dividend was paid on 16 June 2010 (2009: 10 June). The interim dividend was paid on 17 November 2010 (2009: 11 November).

The Directors propose a final dividend of 10.46 pence per ordinary share (totalling £539 million) for the year ended 31 December 2010. The dividend will be submitted for formal approval at the Annual General Meeting to be held on 9 May 2011 and, subject to approval, will be paid on 15 June 2011 to those shareholders registered on 3 May 2011.

13. Auditors' remuneration

	2010 £m	2009 (restated) (i) £m
Fees payable to the Company's auditors for the audit of the Company's annual accounts and Group consolidation	**3.6**	4.2
The auditing of other accounts within the Group pursuant to legislation (including that of countries and territories outside the UK)	**1.5**	1.9
Total fees related to audit of parent and subsidiary entities	**5.1**	6.1
Fees payable to the Company's auditors and its associates for other services:		
Other services pursuant to legislation (ii)	**0.5**	0.7
Services related to taxation	**0.1**	0.1
Services related to information technology	**0.1**	0.1
Services related to corporate finance transactions entered into or proposed to be entered into by or on behalf of the Company or any of its associates	**1.2**	0.3
All other services	**1.6**	1.5
	8.6	8.8
Fees in respect of pension schemes:		
Audit	**0.1**	0.1

(i) The Group has reanalysed its total audit fees and considers that fees in respect of the IFRS audit of the North American business should be included within the Group consolidation audit fee. The 2009 fees have been reanalysed accordingly.

(ii) Includes fees in respect of review performed on the Interim Financial Statements.

It is the Group's policy to seek competitive tenders for all major consultancy and advisory projects. Appointments are made taking into account factors including expertise, experience and cost. In addition, the Board has approved a detailed policy defining the types of work for which the auditors can tender and the approvals required. In the past, the auditors have been engaged on assignments in addition to their statutory audit duties where their expertise and experience with the Group are particularly important, including due diligence reporting and reporting accountant services on acquisitions.

14. Earnings per ordinary share

Basic earnings per ordinary share has been calculated by dividing the earnings attributable to equity holders of the Company for the year of £1,935 million (2009: £844 million) by the weighted average number of ordinary shares in issue during the year of 5,146 million (2009: 5,121 million). The Directors believe that the presentation of adjusted basic earnings per ordinary share, being the basic earnings per ordinary share adjusted for certain re-measurements, exceptional items and the impact of Strategic Investments, assists with understanding the underlying performance of the Group, as explained in note 2. The reconciliation of basic to adjusted basic earnings per ordinary share is as follows:

	2010		2009	
(a) Continuing and discontinued operations	**£m**	**Pence per ordinary share**	£m	Pence per ordinary share
Earnings – basic	**1,935**	**37.6**	844	16.5
Net exceptional items after taxation (notes 2 and 9)	**165**	**3.2**	109	2.1
Certain re-measurement (gains)/losses after taxation (notes 2 and 9) (i)	**(891)**	**(17.3)**	141	2.8
Depreciation of fair value uplifts to property, plant and equipment from Strategic Investments, after taxation	**88**	**1.7**	17	0.3
Earnings – adjusted basic	**1,297**	**25.2**	1,111	21.7
Earnings – diluted	**1,935**	**37.3**	844	16.4
Earnings – adjusted diluted	**1,297**	**25.0**	1,111	21.6

(i) Excludes non-controlling interests of £nil (2009: £38 million). Refer to note 33.

Venture

The Group acquired the Venture Group during 2009. As explained in note 2, the depreciation relating to fair value uplifts relating to the acquired property, plant and equipment and related taxation is excluded in arriving at adjusted earnings for the year, which amounted to £60 million (2009: £20 million) depreciation and a taxation credit of £30 million (2009: £10 million) in the period.

British Energy

The Group acquired a 20% interest in British Energy during 2009 and accounts for its interest as an investment in associate as set out in note 19. As explained in note 2, the impact of depreciation arising on fair value uplifts attributed to the nuclear power stations and related taxation included within the Group's share of the post-taxation results of the associate is excluded in arriving at adjusted earnings for the period, which amounted to £58 million (2009: £7 million) net of taxation.

	2010		2009	
(b) Continuing operations	**£m**	**Pence per ordinary share**	£m	Pence per ordinary share
Earnings – basic	**1,873**	**36.4**	648	12.7
Net exceptional items after taxation (notes 2 and 9)	**165**	**3.2**	382	7.5
Certain re-measurement (gains)/losses after taxation (notes 2 and 9)	**(824)**	**(16.0)**	72	1.4
Depreciation of fair value uplifts to property, plant and equipment from Strategic Investments, after taxation	**88**	**1.7**	17	0.3
Earnings – adjusted basic	**1,302**	**25.3**	1,119	21.9
Earnings – diluted	**1,873**	**36.1**	648	12.6
Earnings – adjusted diluted	**1,302**	**25.1**	1,119	21.8

	2010		2009	
(c) Discontinued operations	**£m**	**Pence per ordinary share**	£m	Pence per ordinary share
Earnings – basic	**62**	**1.2**	196	3.8
Earnings – diluted	**62**	**1.2**	196	3.8

14. Earnings per ordinary share continued

Certain re-measurements (notes 2 and 9) included within operating profit and discontinued operations comprise re-measurements arising on energy procurement activities and re-measurements of proprietary trades in relation to cross-border transportation or capacity contracts. All other re-measurements are included within results before exceptional items and certain re-measurements.

In addition to basic and adjusted basic earnings per ordinary share, information is presented for diluted and adjusted diluted earnings per ordinary share. Under this presentation, no adjustments are made to the reported earnings for either 2010 or 2009, however the weighted average number of shares used as the denominator is adjusted for potentially dilutive ordinary shares.

(d) Weighted average number of shares	**2010 Million shares**	2009 Million shares
Weighted average number of shares used in the calculation of basic earnings per ordinary share	**5,146**	5,121
Dilutive impact of share-based payment schemes	**45**	24
Weighted average number of shares used in the calculation of diluted earnings per ordinary share	**5,191**	5,145

15. Goodwill

	2010 £m	2009 £m
Cost		
1 January	**2,094**	1,559
Acquisitions (note 37)	**169**	916
Adjustments to provisional fair values of acquisitions completed in previous year (note 37)	**50**	–
Disposals	**–**	(3)
Transfer to assets held for sale	**–**	(367)
Exchange adjustments	**65**	(11)
31 December	**2,378**	2,094
Aggregate impairment		
1 January	**(6)**	(49)
Impairments (note 17)	**(2)**	(5)
Transfer to assets held for sale	**–**	43
Exchange adjustments	**–**	5
31 December	**(8)**	(6)
Net book value at 31 December	**2,370**	2,088

Analysis of goodwill at 31 December by acquisition	**2010 £m**	2009 £m
Direct Energy	**424**	389
Energy America	**29**	28
Enron Direct/Electricity Direct	**133**	133
Enbridge Services	**100**	91
CPL/WTU	**237**	228
ATCO	**59**	54
Residential Services Group	**84**	81
Strategic Energy	**98**	94
Clockwork	**84**	–
Dyno-Rod	**17**	17
Newfield	**57**	57
Caythorpe	**33**	33
Heimdal	**168**	165
Venture	**704**	654
Trinidad and Tobago	**70**	–
Other	**73**	64
	2,370	2,088

16. Other intangible assets

	Application software (iii) £m	Emissions allowances and renewable obligation certificates £m	Brands (i) £m	Customer relationships £m	Consents £m	Exploration and evaluation expenditure £m	Other £m	**Total £m**
Cost								
1 January 2010	633	188	59	80	12	193	37	**1,202**
Additions – acquired from a third party	166	242	–	–	–	225	–	**633**
Additions – internally generated	11	–	–	–	–	–	–	**11**
Acquisitions (note 37)	4	–	9	16	–	42	18	**89**
Disposals	(31)	–	–	(1)	–	(6)	–	**(38)**
Surrenders	–	(245)	–	–	–	–	–	**(245)**
Write-downs recognised in Income Statement	–	–	–	–	–	(83)	–	**(83)**
Transfer from assets held for sale	2	1	–	–	–	–	–	**3**
Exchange adjustments	11	–	–	1	–	5	–	**17**
31 December 2010	**796**	**186**	**68**	**96**	**12**	**376**	**55**	**1,589**
Aggregate amortisation and impairment								
1 January 2010	352	37	–	45	–	–	34	**468**
Amortisation	64	–	–	7	–	–	–	**71**
Impairments recognised in Income Statement (ii)	4	15	1	–	–	–	–	**20**
Disposals	(29)	–	–	(1)	–	–	–	**(30)**
Surrenders	–	(36)	–	–	–	–	–	**(36)**
Exchange adjustments	10	–	–	2	–	–	–	**12**
31 December 2010	**401**	**16**	**1**	**53**	**–**	**–**	**34**	**505**
Net book value at 31 December 2010	**395**	**170**	**67**	**43**	**12**	**376**	**21**	**1,084**

	Application software (iii) £m	Emissions allowances and renewable obligation certificates £m	Brands (i) £m	Customer relationships £m	Consents £m	Exploration and evaluation expenditure £m	Other £m	Total £m
Cost								
1 January 2009	521	193	59	108	29	97	46	1,053
Additions – acquired from a third party	111	278	–	5	–	46	2	442
Additions – internally generated	29	1	–	–	–	1	–	31
Acquisitions	15	8	15	202	–	100	263	603
Disposal of subsidiaries	–	–	–	–	(17)	–	–	(17)
Transfer to assets held for sale	(43)	(5)	(15)	(218)	–	–	(260)	(541)
Surrenders	–	(286)	–	–	–	–	–	(286)
Write-downs recognised in Income Statement	–	–	–	–	–	(55)	–	(55)
Exchange adjustments	–	(1)	–	(17)	–	4	(14)	(28)
31 December 2009	633	188	59	80	12	193	37	1,202
Aggregate amortisation and impairment								
1 January 2009	278	31	–	37	2	–	34	382
Amortisation	70	–	–	10	–	–	10	90
Impairments recognised in Income Statement (ii)	21	35	–	20	–	–	–	76
Disposal of subsidiaries	–	–	–	–	(2)	–	–	(2)
Surrenders	–	(29)	–	–	–	–	–	(29)
Transfer to assets held for sale	(18)	–	–	(18)	–	–	(10)	(46)
Exchange adjustments	1	–	–	(4)	–	–	–	(3)
31 December 2009	352	37	–	45	–	–	34	468
Net book value at 31 December 2009	281	151	59	35	12	193	3	734

(i) Brands include £57 million (2009: £57 million) associated with the Dyno-Rod brand, acquired on the acquisition of the Dyno group of companies during 2004. The 2010 brands additions relate to Mr Sparky and Benjamin Franklin, acquired as part of the Clockwork business combination (note 37). Management has ascribed the brands an indefinite useful life because there is no foreseeable limit to the period over which these brands are expected to generate net cash inflows. In reaching this determination, management has reviewed potential threats from competition, the risks of technological obsolescence and the expected usage of the brand by management.

(ii) A £15 million (2009: £35 million) impairment of emissions allowances was recognised within cost of sales, to reflect a reduction in fair value (less costs to sell) as a result of a decrease in market prices, that was offset by a reduction in the obligation related to emissions allowances of £15 million (2009: £35 million).

(iii) Application software includes assets under construction with a cost of £221 million (2009: £113 million). During the year a review of asset classifications identified a number of assets more appropriately classified as under construction, as a result 2009 software assets under construction have increased by £73 million.

17. Impairment testing of goodwill and intangibles with indefinite useful lives

(a) Carrying amount of goodwill and intangible assets with indefinite useful lives allocated to cash-generating units

Goodwill acquired through business combinations and indefinite-lived intangible assets have been allocated for impairment testing purposes to individual or groups of cash-generating units each representing the lowest level within the Group at which the goodwill or indefinite-lived intangible asset is monitored for internal management purposes as follows:

				2010			2009
Cash-generating unit	Principal acquisitions to which goodwill and intangibles with indefinite useful lives relates	Carrying amount of goodwill £m	Carrying amount of indefinite-lived intangible asset £m	Total £m	Carrying amount of goodwill £m	Carrying amount of indefinite-lived intangible asset £m	Total £m
Downstream UK – Business energy supply and services	Enron Direct/Electricity Direct	**133**	**–**	**133**	133	–	133
Downstream UK – Residential services – Dyno-Rod	Dyno-Rod	**17**	**57**	**74**	17	57	74
Upstream UK – Upstream gas and oil	Newfield/Heimdal/Venture/ Trinidad and Tobago (i)	**999**	**–**	**999**	876	–	876
North America – Residential energy supply	Direct Energy/ATCO/CPL/WTU (ii)	**643**	**–**	**643**	602	–	602
North America – Business energy supply	Direct Energy/ATCO/Strategic Energy	**203**	**–**	**203**	191	–	191
North America – Residential and business services	Enbridge Services/Residential Services Group/Clockwork (ii)	**286**	**9**	**295**	192	–	192
Other	Various (iii)	**89**	**1**	**90**	77	–	77
		2,370	**67**	**2,437**	2,088	57	2,145

(i) Goodwill associated with the Trinidad and Tobago acquisition (see note 37) is still being assessed as to which group of cash-generating units will benefit from the synergies of the combination. A conclusion will be reached on this issue before the end of the first year after the acquisition date (5 August 2011).

(ii) Carrying amount of goodwill also contains goodwill from other Direct Energy acquisitions which are not significant compared with the aggregate carrying value of goodwill reported within the cash-generating unit.

(iii) Goodwill balances allocated across multiple cash-generating units. The amount of goodwill allocated to each cash-generating unit is not significant compared with the aggregate carrying value of goodwill reported within the Group. Included in this amount is a £2 million impairment of goodwill attributable to Quintana Mineral Canada Investments Corporation (North America – Upstream and wholesale energy).

(b) Basis on which recoverable amount has been determined

Value in use calculations have been used to determine recoverable amounts for all of the goodwill and indefinite-lived intangible asset balances noted above, with the exception of the impairment test for the Upstream UK – Upstream gas and oil cash-generating unit, where fair value less costs to sell has been used as the basis for determining recoverable amount.

(i) Value in use

The value in use calculations use pre-tax cash flow projections based on the Group's internal Board-approved three-year business plans. The Group's business plans are based on past experience, and adjusted to reflect market trends, economic conditions, key risks, the implementation of strategic objectives and changes in commodity prices, as appropriate. Commodity prices used in the planning process are based in part on observable market data and in part on internal estimates. The extent to which the commodity prices used in the business plans are based on observable market data is determined by the extent to which the market for the underlying commodity is judged to be active. Note 29 provides additional detail on the active period of each of the commodity markets in which the Group operates.

Cash flows beyond the three-year plan period have been extrapolated using growth rates in line with historic long-term growth rates in the market where the cash-generating unit operates.

Cash flows are discounted using a discount rate specific to each cash-generating unit to determine the cash-generating unit's value in use, which is then deemed to be its recoverable amount. The recoverable amount is compared to the carrying value of each cash-generating unit's net assets to determine whether the carrying values of any of the Group's goodwill or indefinite-lived intangible asset balances are greater than their corresponding recoverable amounts.

(ii) Fair value less costs to sell

Fair value less costs to sell is used as the basis for determining the recoverable amount of goodwill allocated to Upstream UK – Upstream gas and oil. This methodology is deemed to be more appropriate as it is based on the post-tax cash flows arising from Upstream UK – Upstream gas and oil as a whole. This is consistent with the approach taken by management to evaluate the economic value of the underlying assets.

Fair value less costs to sell is determined by discounting the post-tax cash flows expected to be generated by the gas production and development assets within Upstream UK – Upstream gas and oil, net of associated selling costs, taking into account those assumptions that market participants would use in estimating fair value. Post-tax cash flows are derived from projected production profiles of each field within Upstream UK – Upstream gas and oil, taking into account forward prices for gas and liquids over the relevant period. Where forward market prices are not available, prices are determined based on internal model inputs. Note 29 provides additional detail on the active period of each of the commodity markets in which the Group operates.

17. Impairment testing of goodwill and intangibles with indefinite useful lives continued

The date of cessation of production depends on the interaction of a number of variables, such as the recoverable quantities of hydrocarbons, production costs, the contractual duration of the licence area and the selling price of the gas and liquids produced. As each field has specific reservoir characteristics and economic circumstances, the post-tax cash flows for each field are computed using individual economic models and key assumptions as determined by management. Post-tax cash flows used in the fair value less costs to sell calculation for the first three years are based on the Group's internal Board-approved three-year business plans and, thereafter, are based on long-term production and cash flow forecasts. Where necessary, the business plan and long-term forecasts are updated in the economic models to reflect the latest view of each field as at the balance sheet date. The future post-tax cash flows are discounted using a post-tax nominal discount rate of 8.5% to determine the fair value less costs to sell of Upstream UK – Upstream gas and oil. Fair value less costs to sell is compared to the carrying value of the Upstream UK – Upstream gas and oil cash-generating unit to determine whether goodwill is impaired. The discount rate used in the fair value less costs to sell calculation is determined in the same manner as the discount rates used in the value in use calculations described below, with the exception of the adjustment required to determine an equivalent pre-tax discount rate that is not required for the fair value less costs to sell calculation.

(c) Key rates used in value in use calculations

(i) Growth rate to perpetuity

Long-term growth rates are determined using a blend of publicly available historical data and long-term growth rate forecasts published by external analysts.

(ii) Discount rates

Discount rates reflect the current market assessments of the time value of money and are based on the estimated cost of capital of each cash-generating unit. Additionally, risks specific to the cash flows of the cash-generating units are reflected within cash flow forecasts. Each cash-generating unit's weighted average cost of capital is then adjusted to reflect the impact of tax in order to calculate an equivalent pre-tax discount rate.

Long-term growth rates used in the value in use calculations for each of the Group's cash-generating units are provided in the table below together with pre-tax discount rates.

	Downstream UK – Business energy supply and services	Downstream UK – Residential services	North America – Residential energy supply	North America – Business energy supply	North America – Residential and business services
Growth rate to perpetuity	**1.9%**	**1.9%**	**2.0%**	**2.0%**	**1.9%**
Pre-tax discount rate	**7.6%**	**7.6%**	**8.1%**	**8.1%**	**8.1%**

(iii) Inflation rates

Inflation rates used in the three-year business plan were based on a blend of a number of publicly available inflation forecasts available in the UK, Canada and the US. Inflation rates used for the value in use calculations were as follows: UK: 1.9%, Canada: 2.0% and the US: 2.0%.

(d) Key assumptions used and summary of results

(i) Downstream UK – Business energy supply and services

Key assumptions

- Gross margin percentage: based on the contractual terms for customers on existing contracts and gross margin percentages achieved in the period leading up to approval of the business plan for new and renewal customers, adjusted to reflect current market conditions and transportation cost inflation.
- Revenues: based on the average market share achieved immediately prior to the approval of the business plan, adjusted for growth forecasts based on sales and marketing activity and recent customer acquisitions, with prices based on forward market curves for both gas and electricity.
- Operating costs: based on a projection of headcount in line with expected activity and salary increases based on inflation expectations, with updated provisions for credit losses experienced historically to reflect the current UK economic environment.

Summary of results

The recoverable amount of the Downstream UK – Business energy supply and services cash-generating unit exceeded its carrying value at the impairment test date. Reasonably possible changes in the key assumptions listed above would not cause the recoverable amount of the goodwill to be equal to or less than the carrying amount.

(ii) Downstream UK – Residential services – Dyno-Rod

Key assumptions

- Gross margin percentage: based on gross margins achieved in the period leading up to the approval of the business plan.
- Revenues: based on revenue levels achieved in the period leading up to the approval of the business plan adjusted for the impact of increased marketing spend and the targeting of key accounts with individual sales staff, with a slight reduction in growth rates to reflect the current economic environment in the UK.
- Operating costs: based on a projection of headcount in line with expected activity and salary increases based on inflation expectations.

Summary of results

The recoverable amount of the Downstream UK – Residential services – Dyno-Rod cash-generating unit exceeded its carrying value at the impairment test date. Reasonably possible changes in the key assumptions listed above would not cause the recoverable amount of the goodwill or indefinite-lived intangible asset to be equal to or less than their carrying amounts.

17. Impairment testing of goodwill and intangibles with indefinite useful lives continued

(iii) Upstream UK – Upstream gas and oil

Key assumptions

Fair value less costs to sell amounts are determined with reference to forecast cash inflows and outflows generated by Upstream UK – Upstream gas and oil assets, net of associated selling costs. Cash inflows and outflows are estimated as follows:

- Cash inflows: based on forward market prices for gas and oil for the active period of the market and internal model inputs thereafter, with reserve volumes and production profiles based on internal management or operator estimates.
- Cash outflows: based on forecast capital and operating expenditure and the estimated future costs of abandonment.
- Taxation: based on tax rates expected to be in effect at the point of the forecast cash flow.

Summary of results

The recoverable amount of the Upstream UK – Upstream gas and oil cash-generating unit exceeded its carrying value at the impairment test date. Reasonably possible changes in the key assumptions listed above would not cause the recoverable amount of the goodwill to be equal to or less than the carrying amount.

(iv) North America – Residential energy supply

Key assumptions

- Gross margin percentage: based on contractual terms for customers on existing contracts and gross margin percentages achieved in the period leading up to the approval of the business plan for new and renewal customers, adjusted to reflect competitor data, where available. Where applicable, regulated gross margin percentages are based on the gross margin percentages included in regulatory applications submitted to the Alberta Utilities Commission in Canada.
- Revenues: based on average market share by individual market sector achieved in the period immediately prior to the approval of the business plan, adjusted for expectations of growth or decline based on individual jurisdictions to reflect regulatory or competitive differences, including customer propensity to switch, and contractual prices, with non-contractual prices based on forward market gas and power curves in Canada and the US.
- Operating costs: based on a projection of headcount in line with expected activity and salary increases based on inflation expectations, with slight decreases in costs to reflect planned business process efficiencies and experience of costs required to support customer acquisition, renewal, retention and other servicing activities.

Summary of results

The recoverable amount of the North America – Residential energy supply cash-generating unit exceeded its carrying value at the impairment test date. Reasonably possible changes in the key assumptions listed above would not cause the recoverable amount of the goodwill to be equal to or less than the carrying amount.

(v) North America – Business energy supply

Key assumptions

- Gross margin percentage: based on contractual terms for gross margin under contract and historical experience for planned renewals and new sales. Unit margins were planned to achieve an acceptable return on risk adjusted capital.
- Revenues: based on historical growth trends and planned sales activities by individual market sector. Prices are based on forward market curves for gas and electricity in Canada and the US.
- Operating costs: based on historical trends adjusted to reflect expected cost optimisations, as well as projection of headcount in line with activity.

Summary of results

The recoverable amount of the North America – Business energy supply cash-generating unit exceeded its carrying value at the impairment test date. Reasonably possible changes in the key assumptions listed above would not cause the recoverable amount of the goodwill to be equal to or less than the carrying amount.

(vi) North America – Residential and business services

Key assumptions

- Gross margin percentage: based on gross margin percentages achieved in the period leading up to the approval of the business plan, adjusted to reflect the current economic conditions and weak condition of the North American housing market.
- Revenues: based on historical growth trends by individual market sector, adjusted for new product offerings and continued penetration into new markets.
- Operating costs: based on projected headcount and inflationary increases.

Summary of results

The recoverable amount of the North America – Residential and business services cash-generating unit exceeded its carrying value at the impairment test date. Reasonably possible changes in the key assumptions listed above would not cause the recoverable amount of the goodwill to be equal to or less than the carrying amount.

18. Property, plant and equipment

	Land and buildings (i) £m	Plant, equipment and vehicles (ii), (iii) £m	Power generation (ii), (iii), (iv) £m	Gas storage and production (ii), (iii), (iv) £m	**Total £m**
Cost					
1 January 2010	23	389	2,144	8,649	**11,205**
Additions	2	27	87	401	**517**
Capitalised borrowing costs (note 10)	–	–	–	37	**37**
Acquisitions (note 37)	1	5	–	458	**464**
Capitalisation of unwind of fair value adjustment (v)	–	–	–	(5)	**(5)**
Adjustment to fair value of prior year acquisitions (note 37)	–	–	–	(61)	**(61)**
Disposals	–	(67)	(14)	(13)	**(94)**
Transfer from inventory	–	–	–	14	**14**
Transfer from assets held for sale	–	4	–	–	**4**
Revisions and additions to decommissioning liability (note 28)	–	–	1	261	**262**
Exchange adjustments	–	11	11	111	**133**
31 December 2010	**26**	**369**	**2,229**	**9,852**	**12,476**
Aggregate depreciation and impairment					
1 January 2010	11	203	545	4,387	**5,146**
Charge for the year	1	34	143	638	**816**
Impairments	–	–	64	93	**157**
Disposals	–	(66)	(11)	(11)	**(88)**
Exchange adjustments	–	7	2	38	**47**
31 December 2010	**12**	**178**	**743**	**5,145**	**6,078**
Net book value at 31 December 2010	**14**	**191**	**1,486**	**4,707**	**6,398**

	Land and buildings (i) £m	Plant, equipment and vehicles (ii), (iii) £m	Power generation (ii),(iii) £m	Gas storage and production (ii),(iii),(iv),(v) £m	Total £m
Cost					
1 January 2009	22	424	2,483	6,234	9,163
Additions	60	5	316	469	850
Capitalised borrowing costs (note 10)	–	–	–	34	34
Acquisitions	13	14	903	1,796	2,726
Capitalisation of unwind of fair value adjustment (v)	–	–	–	(18)	(18)
Disposals	–	(5)	(9)	(4)	(18)
Reclassification as joint venture	–	–	(370)	–	(370)
Transfer to assets held for sale	(71)	(47)	(1,094)	–	(1,212)
Revisions and additions to decommissioning liability	–	–	(6)	74	68
Exchange adjustments	(1)	(2)	(79)	64	(18)
31 December 2009	23	389	2,144	8,649	11,205
Aggregate depreciation and impairment					
1 January 2009	10	167	434	3,863	4,474
Charge for the year	2	43	144	455	644
Impairments	–	2	35	52	89
Disposals	–	(5)	(9)	(4)	(18)
Reclassification as joint venture	–	–	(27)	–	(27)
Transfer to assets held for sale	(1)	(7)	(24)	–	(32)
Exchange adjustments	–	3	(8)	21	16
31 December 2009	11	203	545	4,387	5,146
Net book value at 31 December 2009	12	186	1,599	4,262	6,059

During 2010, impairment charges have been recorded as follows; all within exceptional items (note 9):

Upstream UK – Power generation: £64 million charge as a result of low spark spreads. The recoverable amount has been determined using value in use calculations, with future cash flows discounted using a pre-tax discount rate of 7.6% (2009: 7.6%). Cash inflows are based on forward market prices for power for the active period of the market and internal models thereafter, with production profiles based on the best economic running decision. Cash outflows are based on planned operating and capital expenditure.

18. Property, plant and equipment continued

Upstream UK – Upstream gas and oil: £28 million charge as a result of updated reserves data and new infrastructure expectations. The charge is net of write backs of previous impairments of £30 million. The recoverable amount has been determined using fair value less cost to sell. Note 17 provides more detail on the general approach to impairment calculations and provides the assumptions used to assess Upstream UK – Upstream gas and oil for impairment.

North America – Upstream and wholesale energy: £65 million charge as a result of declining commodity prices and changing market conditions. The recoverable amount has been determined using fair value less cost to sell, based on evidence from recent acquisition transactions for similar assets in the local oil and gas market, net of estimated selling costs.

(i) The net book value of land and buildings comprises the following:	**2010 £m**	2009 £m
Freeholds	**8**	6
Long leaseholds	**1**	1
Short leaseholds	**5**	5
	14	12

(ii) Assets in the course of construction are included within the following categories of property, plant and equipment:	**2010 £m**	2009 (restated) £m
Plant, equipment and vehicles	**75**	95
Power generation	**30**	310
Gas storage and production	**894**	762
	999	1,167

During the year a review of asset classifications identified a number of assets more appropriately classified as under construction. As a result, 2009 assets under construction have increased by £35 million.

(iii) Assets held under finance leases included in totals above:				**2010**				2009
	Plant, equipment and vehicles £m	**Power generation £m**	**Gas storage and production £m**	**Total £m**	Plant, equipment and vehicles £m	Power generation £m	Gas storage and production £m	Total £m
Cost at 1 January	**2**	**469**	**415**	**886**	–	469	415	884
Additions	**–**	**–**	**–**	**–**	2	–	–	2
Cost at 31 December	**2**	**469**	**415**	**886**	2	469	415	886
Aggregate depreciation at 1 January	**1**	**146**	**365**	**512**	–	118	360	478
Charge for the year	**–**	**27**	**10**	**37**	1	28	5	34
Aggregate depreciation at 31 December	**1**	**173**	**375**	**549**	1	146	365	512
Net book value at 31 December	**1**	**296**	**40**	**337**	1	323	50	374

(iv) The net book value of decommissioning costs included within power generation and gas storage and production assets was £804 million (2009: £565 million).
(v) Relates to the consumption of a rig contract which was out-of-the-money on acquisition. As the contract is utilised, the fair value is added to the cost of the associated fixed assets.

The net book value of assets to which title was restricted at 31 December 2010 was £337 million (2009: £374 million), of which £296 million (2009: £323 million) relate to the Spalding power station finance lease asset. The value of assets pledged as security for liabilities as at 31 December 2010 was £300 million (2009: £157 million).

19. Interests in joint ventures and associates

			2010			2009
(a) Interest in joint ventures and associates	Investments in joint ventures and associates (i) £m	Shareholder loans £m	**Total £m**	Investments in joint ventures and associates £m	Shareholder loans £m	Total £m
1 January	2,356	66	**2,422**	286	44	330
Additions (i)	66	124	**190**	2,303	39	2,342
Reclassification as a subsidiary	–	–	**–**	(216)	–	(216)
Decrease in shareholder loans	–	(26)	**(26)**	–	(17)	(17)
Impairment of interest in joint venture	(4)	–	**(4)**	–	–	–
Disposals of investments	–	–	**–**	(1)	–	(1)
Share of (losses)/profits for the year	(7)	–	**(7)**	1	–	1
Share of reserve movements	15	–	**15**	–	–	–
Dividends	(83)	–	**(83)**	–	–	–
Exchange adjustments	–	–	**–**	(17)	–	(17)
31 December	**2,343**	**164**	**2,507**	2,356	66	2,422

(i) Additions include the reclassification of interests in Lincs Wind Farms Limited (note 38) and the acquisition of Alertme.com Limited.

19. Interests in joint ventures and associates continued

(b) Share of joint ventures' and associates' assets and liabilities

The Group's share of joint ventures' and associates' gross assets and gross liabilities at 31 December 2010 principally comprised of its interests in Braes of Doune Wind Farm (Scotland) Limited, Barrow Offshore Wind Limited, GLID Wind Farms TopCo Limited, Lincs Wind Farm Limited, Lake Acquisitions Limited (British Energy) and NNB Holding Company Limited.

The Group's share of the investments in and results of Braes of Doune Wind Farm (Scotland) Limited, Barrow Offshore Wind Limited, GLID Wind Farms TopCo Limited, Lincs Wind Farm Limited, Lake Acquisitions Limited (British Energy) and NNB Holding Company Limited are included within the Upstream UK – Power generation segment. The Group's share of the investments in and results of Secure Electrans Limited and Alertme.com Limited are included within the Downstream UK – Residential energy supply segment. The Group's share of the investments in and results of Bacton Storage Company Limited are included within the Storage UK segment. The Group's share of the investments in and results of North Sea Infrastructure Partners Limited and Ten Degrees North Energy Limited are included within the Upstream UK – Upstream gas and oil segment.

	Joint ventures				Associates			2010	2009
	Braes of Doune Wind Farm (Scotland) Limited £m	Barrow Offshore Wind Limited £m	GLID Wind Farms TopCo Limited (i) £m	Lincs Wind Farm Limited £m	Lake Acquisitions Limited (British Energy) £m	NNB Holding Company Limited £m	Other (ii) £m	**Total £m**	Total £m
Share of non-current assets	34	59	170	136	3,639	72	59	**4,169**	4,078
Share of current assets	3	7	28	21	592	34	13	**698**	702
	37	66	198	157	4,231	106	72	**4,867**	4,780
Share of current liabilities	(5)	(2)	(37)	(39)	(166)	(21)	–	**(270)**	(243)
Share of non-current liabilities	(15)	(15)	(178)	(112)	(1,909)	–	(21)	**(2,250)**	(2,181)
	(20)	(17)	(215)	(151)	(2,075)	(21)	(21)	**(2,520)**	(2,424)
Restricted interest on shareholder loan (iii)	–	–	–	(4)	–	–	–	**(4)**	–
Share of net assets of joint ventures and associates	17	49	(17)	2	2,156	85	51	**2,343**	2,356
Shareholder loans	15	–	22	112	–	–	15	**164**	66
Interests in joint ventures and associates	**32**	**49**	**5**	**114**	**2,156**	**85**	**66**	**2,507**	2,422
Net (debt)/cash included in share of net assets	(13)	4	(171)	(97)	57	33	(18)	**(205)**	237

(i) As part of a finance arrangement entered into by GLID Wind Farms TopCo Limited, the Group's shares in GLID Wind Farms TopCo Limited are pledged to a third party. The pledge will only come into force should GLID Wind Farms TopCo Limited default on any of its obligations under the finance arrangement.
(ii) Other includes joint ventures of North Sea Infrastructure Partners Limited, Bacton Storage Company Limited and Secure Electrans Limited and associates of Ten Degrees North Energy Limited and Alertme.com Limited.
(iii) The Group restricts the amount of interest receivable on the shareholder loan from Lincs Wind Farm Limited to 50% of the interest capitalised by the joint venture.

(c) Share of profits/(losses) in joint ventures and associates

	Joint ventures				Associates			2010	2009
	Braes of Doune Wind Farm (Scotland) Limited £m	Barrow Offshore Wind Limited £m	GLID Wind Farms TopCo Limited £m	Lincs Wind Farm Limited £m	Lake Acquisitions Limited (British Energy) (i) £m	NNB Holding Company Limited £m	Other (ii) £m	**Total £m**	Total £m
Income	6	9	29	–	421	–	3	**468**	76
Expenses excluding certain re-measurements (i)	(2)	(8)	(17)	(2)	(391)	(2)	–	**(422)**	(58)
Certain re-measurements	–	–	–	–	(31)	–	–	**(31)**	(12)
	4	1	12	(2)	(1)	(2)	3	**15**	6
Interest	–	–	(17)	–	(38)	–	–	**(55)**	(4)
Taxation excluding certain re-measurements (i)	(1)	–	2	–	15	–	–	**16**	(4)
Taxation on certain re-measurements	–	–	–	–	17	–	–	**17**	3
Share of post-taxation results of joint ventures and associates	3	1	(3)	(2)	(7)	(2)	3	**(7)**	1

(i) Includes £97 million (2009: £10 million) relating to depreciation of fair value uplifts to property, plant and equipment on acquiring the British Energy investments. The associated tax impact is £39 million credit (2009: £3 million).
(ii) Other includes joint ventures of North Sea Infrastructure Partners Limited, Bacton Storage Company Limited and Secure Electrans Limited and associates of Ten Degrees North Energy Limited and Alertme.com Limited.

19. Interests in joint ventures and associates continued

British Energy

The Group acquired a 20% interest in British Energy for £2,255 million and NNB Holding Company Limited for £32 million on 26 November 2009. The fair value exercise was completed during the year. The Group's share of profit arising from its investment in British Energy for the year to 31 December 2010 as set out in the table above includes the effect of unwinding the fair value adjustments. As explained in note 2 the depreciation, net of taxation, arising on fair value uplifts attributed to the nuclear power stations is reversed in arriving at adjusted profit for the period as shown in the reconciliation table below and as set out in notes 6 and 14.

(d) Reconciliation of share of profits/(losses) in joint ventures and associates to share of adjusted profits/(losses) in joint ventures and associates

	Joint ventures	Associates		2010	2009
	Wind Farms £m	Nuclear £m	Other (ii) £m	**Total £m**	Total £m
Share of post-taxation results of joint ventures and associates	(1)	(9)	3	**(7)**	1
Certain re-measurements (net of taxation)	–	14	–	**14**	9
Depreciation – British Energy (net of taxation) (i)	–	58	–	**58**	7
Interest	17	38	–	**55**	4
Taxation (excluding certain re-measurements and British Energy depreciation)	(1)	24	–	**23**	7
Share of adjusted results of joint ventures and associates	15	125	3	**143**	28

(i) Relates to depreciation of fair value uplifts to property, plant and equipment on acquiring the British Energy investments.
(ii) Other includes joint ventures of North Sea Infrastructure Partners Limited, Bacton Storage Company Limited and Secure Electrons Limited and associates of Ten Degrees North Energy Limited and Alertme.com Limited.

20. Inventories

	2010 £m	2009 £m
Gas in storage and transportation	**120**	140
Other raw materials and consumables	**106**	108
Finished goods and goods for resale	**118**	134
	344	382

The Group consumed £1,117 million of inventories (2009: £786 million) during the year. Inventory write-downs of £20 million (2009: £3 million) were recognised in gross profit during the year. £16 million of the write-downs in the year relate to Power Station and Gas Production spare parts. The remainder was recognised in exceptional items as a write-down of spare parts relating to assets impaired in the year.

21. Trade and other receivables

		2010		2009
	Current £m	**Non-current £m**	Current £m	Non-current £m
Financial assets:				
Trade receivables	**1,995**	**8**	1,711	14
Accrued energy income	**1,813**	**–**	1,876	–
Other accrued income	**202**	**–**	173	–
Cash collateral pledged	**173**	**–**	631	–
Other receivables	**307**	**12**	158	11
	4,490	**20**	4,549	25
Less: Provision for credit losses	**(641)**	**–**	(554)	–
	3,849	**20**	3,995	25
Non-financial assets:				
Prepayments and other receivables	**338**	**77**	186	118
	4,187	**97**	4,181	143

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21. Trade and other receivables continued

Trade and other receivables include financial assets representing the contractual right to receive cash or other financial assets from residential customers, business customers and treasury, trading and energy procurement counterparties as follows:

	2010 Current £m	2010 Non-current £m	2009 Current £m	2009 Non-current £m
Financial assets by class:				
Residential customers	**2,001**	**9**	1,883	14
Business customers	**1,643**	**11**	1,495	11
Treasury, trading and energy procurement counterparties	**846**	**–**	1,171	–
	4,490	**20**	4,549	25
Less: Provision for credit losses	**(641)**	**–**	(554)	–
	3,849	**20**	3,995	25

Receivables from residential and business customers are generally considered to be fully performing until such time as the payment that is due remains outstanding past the contractual due date. Contractual due dates range from being due upon receipt to due in 30 days. An ageing of the carrying value of trade and other receivables that are past due but not considered to be individually impaired by class is as follows:

Days past due	2010 Residential customers £m	2010 Business customers £m	2010 Treasury, trading and energy procurement counterparties £m	2009 Residential customers £m	2009 Business customers £m	2009 Treasury, trading and energy procurement counterparties £m
Less than 30 days	**194**	**168**	**3**	199	124	119
30-89 days	**138**	**189**	**1**	75	163	–
Less than 90 days	**332**	**357**	**4**	274	287	119
90-182 days	**64**	**77**	**1**	63	49	2
183-365 days	**99**	**82**	**1**	98	76	2
Greater than 365 days	**37**	**26**	**1**	41	16	1
	532	**542**	**7**	476	428	124

At 31 December 2010, there were £25 million (2009: £34 million) of receivables, net of provisions for credit losses, from residential customers and £22 million (2009: £8 million) from treasury, trading and energy procurement counterparties that were considered to be individually impaired. Receivables from residential customers are generally reviewed for impairment on an individual basis once a customer discontinues their relationship with the Group.

The provision for credit losses is based on an incurred loss model and is determined by application of expected default and loss factors, determined by historical loss experience and current sampling to the various balances receivable from residential and business customers on a portfolio basis, in addition to provisions taken against individual accounts. Balances are written off when recoverability is assessed as being remote. Movements in the provision for credit losses by class are as follows:

	2010 Residential customers £m	2010 Business customers £m	2010 Treasury, trading and energy procurement counterparties £m	2010 Total £m	2009 Residential customers £m	2009 Business customers £m	2009 Treasury, trading and energy procurement counterparties £m	2009 Total £m
1 January	(362)	(180)	(12)	**(554)**	(399)	(131)	(11)	(541)
Impairment of trade receivables	(142)	(124)	(1)	**(267)**	(240)	(116)	(1)	(357)
Transfer to assets held for sale	–	–	–	**–**	24	4	–	28
Receivables written off	132	53	1	**186**	247	62	–	309
Acquisitions	(1)	(1)	–	**(2)**	–	–	–	–
Exchange adjustments	(2)	(1)	(1)	**(4)**	6	1	–	7
31 December	**(375)**	**(253)**	**(13)**	**(641)**	(362)	(180)	(12)	(554)

21. Trade and other receivables continued

The impairment charge in trade receivables is stated net of credits for the release of specific provisions made in previous years, which are no longer required. These relate primarily to residential customers in the UK. At 31 December 2010 the Group held £56 million (2009: £17 million) of customer deposits for the purposes of mitigating the credit risk associated with receivables from residential and business customers and £3 million (2009: £nil) from treasury, trading and energy procurement customers. Exposure to credit risk associated with receivables from treasury, trading and energy procurement counterparties is monitored by counterparty credit rating as follows:

Receivables from treasury, trading and energy procurement counterparties by credit rating	Carrying value £m	AAA to AA £m	AA– to A– £m	BBB+ to BBB– £m	BB+ to BB– £m	B or lower £m	Unrated £m
2010	**846**	**12**	**334**	**175**	**14**	**–**	**311**
2009	1,171	12	703	237	13	12	194

The unrated counterparty receivables are comprised primarily of amounts due from subsidiaries of rated entities, exchanges or clearing houses. Receivables from treasury, trading and energy procurement counterparties are managed in accordance with the Group's counterparty credit policy as described in note 4.

22. Derivative financial instruments

Derivative financial instruments are generally held for the purpose of proprietary energy trading, treasury management or energy procurement. Derivatives held for the purpose of proprietary energy trading are carried at fair value, with changes in fair value recognised in the Group's results for the year before exceptional items and certain re-measurements, with the exception of certain derivatives related to cross-border transportation and capacity contracts (note 2). Derivative financial instruments held for the purposes of treasury management or energy procurement are also carried at fair value, with changes in the fair value of derivatives relating to treasury management reflected in the results for the year before exceptional items and certain re-measurements, and those relating to energy procurement reflected in certain re-measurements. In cases where a derivative qualifies for hedge accounting, derivatives are classified as fair value hedges, cash flow hedges or hedges of a net investment in a foreign operation. Notes 2 and 23 provide further detail on the Group's hedge accounting.

Energy contracts designated at fair value through profit and loss include certain energy contracts that the Group has, at its option, designated at fair value through profit and loss under IAS 39 because the energy contract contains one or more embedded derivatives that significantly modify the cash flows under the contract (note 2).

The carrying values of derivative financial instruments by product type for accounting purposes are as follows:

	2010		2009	
	Assets £m	**Liabilities £m**	Assets £m	Liabilities £m
Derivative financial instruments – held for proprietary energy trading:				
Energy derivatives – held for trading under IAS 39	**47**	**(31)**	68	(3)
Derivative financial instruments – held for the purpose of treasury management or energy procurement:				
Derivative financial instruments – held for trading under IAS 39				
Energy derivatives	**538**	**(1,022)**	590	(2,134)
Interest rate derivatives	**3**	**(16)**	3	(5)
Foreign exchange derivatives	**53**	**(100)**	45	(79)
Energy derivative contracts designated at fair value through profit and loss	**1**	**(143)**	–	(177)
Derivative financial instruments in hedge accounting relationships:				
Energy derivatives	**25**	**(86)**	2	(328)
Interest rate derivatives	**105**	**–**	69	(10)
Foreign exchange derivatives	**18**	**(5)**	31	(14)
Total derivative financial instruments	**790**	**(1,403)**	808	(2,750)
Included within:				
Derivative financial instruments – current	**449**	**(755)**	492	(1,744)
Derivative financial instruments – non-current	**341**	**(648)**	316	(1,006)

The contracts included within energy derivatives are subject to a wide range of detailed specific terms but comprise the following general components:

	2010 £m	2009 £m
Short-term forward market purchases and sales of gas and electricity:		
UK and Europe	**24**	(1,091)
North America	**(451)**	(583)
Structured gas purchase contracts	**89**	(34)
Structured gas sales contracts	**(176)**	(135)
Other	**(157)**	(139)
Net total	**(671)**	(1,982)

22. Derivative financial instruments continued

Net gains/(losses) on derivative financial instruments due to re-measurement	2010 Income Statement £m	2010 Equity £m	2009 Income Statement £m	2009 Equity £m
Financial assets and liabilities measured at fair value:				
Derivative financial instruments – held for proprietary energy trading	**(51)**	**–**	(48)	–
Derivative financial instruments – held for trading under IAS 39	**1,099**	**–**	153	–
Energy contracts designated at fair value through profit and loss	**36**	**–**	(36)	–
Derivative financial instruments in hedge accounting relationships	**39**	**260**	(15)	43
	1,123	**260**	54	43

Derivative-related credit risk – assets

Credit risk from derivative transactions is generated by the potential for the counterparty to default on its contractual obligations and is normally a small fraction of the contract's notional amount. Credit risk from derivatives is measured and managed by counterparty credit rating as follows:

Fair value of derivative financial instruments with a positive fair value by counterparty credit rating	Carrying value £m	AAA to AA £m	AA– to A– £m	BBB+ to BBB– £m	BB+ to BB– £m	B or lower £m	Unrated £m
2010	**790**	**26**	**647**	**42**	**2**	**–**	**73**
2009	808	35	567	44	3	–	159

To manage derivative-related counterparty credit exposure, the Group employs the use of margining and set-off rights in some agreements. Under margining agreements, the Group has the right to request that the counterparty pay down or collateralise the current fair value of its derivatives position when the position passes a specified threshold.

Maturity profiles of derivative financial instruments – liabilities

The following maturity analysis shows the remaining contractual maturities on an undiscounted basis for the Group's derivative financial instruments that are in a loss position at the balance sheet date and will be settled on a net basis:

Derivatives that will be settled on a net basis	2010 Energy £m	2010 Interest £m	2009 Energy £m	2009 Interest £m
Less than one year	**(415)**	**(3)**	(325)	1
One to five years	**(144)**	**2**	(185)	–
More than five years	**–**	**(14)**	–	(29)
	(559)	**(15)**	(510)	(28)

Certain of the Group's energy contracts that are accounted for as derivatives are for the physical purchase of energy. In these cases, IFRS 7 requires disclosure of a maturity analysis that shows cash outflows on all purchase contracts on an undiscounted basis, including those derivative contracts in a gain position at the balance sheet date as follows:

Energy procurement contracts that are carried at fair value	2010 £m	2009 £m
Less than one year	**(12,814)**	(15,314)
One to five years	**(15,199)**	(17,865)
More than five years	**(2,184)**	(4,877)
	(30,197)	(38,056)

The Group's foreign exchange derivative contracts will be settled on a gross basis. In these cases, IFRS 7 requires disclosure of a maturity analysis that shows cash outflows on all derivative contracts on an undiscounted basis, including those derivative contracts in a gain position at the balance sheet date. In addition to cash outflows on all foreign exchange derivative contracts that are gross settled on an undiscounted basis, the following analysis also provides disclosure of the related cash inflows:

Foreign exchange derivatives that will be settled on a gross basis	2010 Outflow £m	2010 Inflow £m	2009 Outflow £m	2009 Inflow £m
Less than one year	**(2,350)**	**2,335**	(1,925)	1,899
One to five years	**(1,154)**	**1,136**	(1,444)	1,426
More than five years	**(244)**	**158**	(232)	242
	(3,748)	**3,629**	(3,601)	3,567

23. Hedge accounting

For the purposes of hedge accounting, hedges are classified as either fair value hedges, cash flow hedges or hedges of net investments in foreign operations. Note 2 details the Group's accounting policies in relation to derivatives qualifying for hedge accounting under IAS 39. The fair values of derivative and primary financial instruments in hedge accounting relationships at 31 December were as follows:

	2010		2009	
	Assets £m	**Liabilities £m**	Assets £m	Liabilities £m
Fair value hedges	**105**	**–**	70	(5)
Cash flow hedges	**43**	**(91)**	32	(347)

Fair value hedges

The Group's fair value hedges consist of interest rate swaps, cross-currency interest rate swaps and forward rate agreements used to protect against changes in the fair value of fixed-rate, long-term debt due to movements in market interest rates. For qualifying fair value hedges, all changes in the fair value of the hedging instrument and in the fair value of the hedged item in relation to the risk being hedged are recognised as income within net interest expense.

Gains or losses arising on fair value hedges at 31 December were as follows:

Gains/(losses)	**2010 £m**	2009 £m
On hedging instruments	**41**	(12)
On hedged items attributable to the hedged risk	**(41)**	14
	–	2

Cash flow hedges

The Group's cash flow hedges consist primarily of:

- physical and financial gas and power purchase contracts used to protect against the variability in future cash flows associated with highly probable forecast purchases of gas and power due to movements in market commodity prices;
- forward foreign exchange contracts used to protect against the variability of functional currency denominated cash flows associated with non-functional currency denominated highly probable forecast transactions; and
- interest rate swaps, cross-currency interest rate swaps and forward rate agreements used to protect against the variability in cash flows associated with floating-rate borrowings due to movements in market interest rates.

Gains and losses are initially recognised in the cash flow hedging reserve in other comprehensive income and are transferred to the Income Statement when the forecast cash flows affect the Income Statement. Note 31 details movements in the cash flow hedging reserve. The ineffective portion of gains and losses on cash flow hedging are recognised immediately in the Income Statement. During 2010, the Group recognised a £2 million loss (2009: £2 million loss) due to cash flow hedge ineffectiveness.

Net investment hedges

The Group's net investment hedges consist of foreign currency debt issued in the same currency as the net investment, foreign exchange forwards and cross-currency interest rate swaps used to protect against the variability in the pounds sterling value of the Group's net investments in foreign operations due to movements in the relative strength of foreign currencies to pounds sterling.

Gains and losses on the effective portion of the hedge are recognised in equity and transferred to the Income Statement on disposal of the foreign operation. Gains and losses on the ineffective portion of the hedge are recognised immediately in the Income Statement. During 2010, the Group recognised losses of £nil due to net investment hedge ineffectiveness (2009: £4 million).

24. Cash and cash equivalents

	2010 £m	2009 £m
Cash at bank, in transit and in hand	**114**	121
Short-term deposits	**353**	1,173
Cash and cash equivalents	**467**	1,294

Cash and cash equivalents includes £206 million (2009: £64 million) held by the Group's insurance subsidiary undertakings that is not readily available to be used for other purposes within the Group.

Cash and cash equivalents by counterparty credit rating	**Carrying value £m**	AAA £m	AA £m	A £m
2010	**467**	**304**	**59**	**104**
2009	1,294	818	172	304

Credit risk associated with cash and cash equivalents is managed in accordance with the Group's counterparty credit policy as described in note 4.

25. Trade and other payables

	2010 Current £m	2010 Non-current £m	2009 Current £m	2009 Non-current £m
Financial liabilities:				
Trade payables	**1,063**	**–**	784	–
Deferred income	**293**	**–**	485	–
Capital creditors	**169**	**–**	174	–
Other payables	**368**	**–**	381	45
Accruals				
Commodity costs	**846**	**–**	1,032	–
Transportation, distribution and metering costs	**163**	**–**	146	–
Operating and other accruals	**676**	**–**	528	–
	1,685	**–**	1,706	–
	3,578	**–**	3,530	45
Non-financial liabilities:				
Other payables and accruals	**329**	**29**	327	31
Deferred income	**152**	**27**	98	6
	4,059	**56**	3,955	82

Maturity analysis of financial liabilities within trade and other payables on an undiscounted basis	2010 £m	2009 £m
Less than 90 days	**3,214**	3,046
90-182 days	**160**	249
183-365 days	**204**	235
	3,578	3,530
Greater than 365 days	**–**	45
	3,578	3,575

26. Bank overdrafts, loans and other borrowings

	Interest rate %	Principal m	2010 Current £m	2010 Non-current £m	2010 Total £m	2009 Current £m	2009 Non-current £m	2009 Total £m
Bank overdrafts and loans			**52**	**225**	**277**	63	384	447
Bonds (by maturity date)								
2 November 2012 (i)	6.103	£284	**–**	**296**	**296**	–	415	415
27 February 2013	1.045	¥3,000	**–**	**25**	**25**	–	21	21
9 December 2013 (ii)	7.307	€367	**–**	**326**	**326**	–	678	678
4 November 2014	Floating	$100	**–**	**64**	**64**	–	62	62
10 December 2014 (iii)	5.297	£315	**–**	**329**	**329**	–	353	353
31 March 2015 (iv)	Floating	$70	**–**	**45**	**45**	–	–	–
24 October 2016	5.706	£300	**–**	**320**	**320**	–	311	311
19 September 2018	7.038	£400	**–**	**444**	**444**	–	428	428
10 March 2022 (v)	6.362	£500	**–**	**527**	**527**	–	414	414
4 September 2026 (vi)	6.265	£200	**–**	**209**	**209**	–	149	149
16 April 2027 (vii)	6.083	$70	**–**	**45**	**45**	–	–	–
19 September 2033	7.100	£770	**–**	**777**	**777**	–	777	777
			–	**3,407**	**3,407**	–	3,608	3,608
Other borrowings								
12 December 2011 (viii)	Floating	£250	**–**	**–**	**–**	–	250	250
Obligations under finance leases			**25**	**327**	**352**	23	352	375
			77	**3,959**	**4,036**	86	4,594	4,680

(i) Principal amount of £116 million was redeemed on 6 December 2010.
(ii) Principal amount of €353 million was redeemed on 6 December 2010 and a further €30 million on 23 December 2010.
(iii) Principal amount of £35 million was redeemed on 6 December 2010.
(iv) Issued on 31 March 2010.
(v) Principal amount was increased by £40 million on 12 March 2010 and by an additional £60 million on 15 March 2010.
(vi) Principal amount was increased by £50 million on 24 March 2010.
(vii) Issued on 16 April 2010.
(viii) Redeemed on 12 February 2010.

26. Bank overdrafts, loans and other borrowings continued

Future finance lease commitments:	2010 Minimum lease payments £m	2010 Capital element of lease payments £m	2009 Minimum lease payments £m	2009 Capital element of lease payments £m
Amounts payable:				
Within one year	**45**	**25**	44	23
Between one and five years	**187**	**125**	183	115
After five years	**235**	**202**	283	237
	467	**352**	510	375
Less future finance charges	**(115)**		(135)	
Present value of lease obligations	**352**		375	

Maturity profile of the Group's borrowings including interest and principal:	2010 £m	2009 £m
Within one year (i)	**284**	326
Between one and five years	**2,072**	3,080
After five years	**4,070**	4,038
	6,426	7,444
Interest payments	**(2,390)**	(2,764)
	4,036	4,680

(i) Borrowings include amounts repayable on demand of £19 million (2009: £28 million).

27. Deferred and current corporation tax liabilities and assets

The following are the major deferred tax liabilities and assets recognised by the Group and movements thereon during the current and prior reporting periods:

	Accelerated tax depreciation (petroleum revenue tax) £m	Deferred corporation tax effect thereon £m	Decommissioning (petroleum revenue tax) £m	Deferred corporation tax effect thereon £m	Retirement benefit obligation and other provisions £m	Accelerated tax depreciation (corporation tax) £m	Other timing differences including losses carried forward £m	Marked-to-market £m	Total £m
1 January 2009	(209)	105	180	(90)	30	(1,036)	193	690	**(137)**
(Charge)/credit to income:									
Continuing operations	28	(14)	(4)	2	(113)	(63)	92	(4)	**(76)**
Discontinued operations	–	–	–	–	–	(32)	–	21	**(11)**
(Charge)/credit to equity	–	–	–	–	241	–	10	(12)	**239**
Transfer to assets held for sale	–	–	–	–	–	(3)	–	–	**(3)**
Acquisition of subsidiary	–	–	–	–	–	(1,070)	120	(18)	**(968)**
Disposal of subsidiaries	–	–	–	–	–	383	–	(41)	**342**
Exchange and other adjustments	–	–	–	–	–	(8)	2	(25)	**(31)**
31 December 2009	(181)	91	176	(88)	158	(1,829)	417	611	**(645)**
Change to tax rates	–	–	–	–	3	8	4	(1)	**14**
(Charge)/credit to income	(18)	5	25	(13)	(92)	179	(184)	(331)	**(429)**
(Charge)/credit to equity	–	–	–	–	(2)	–	33	(79)	**(48)**
Acquisition of subsidiaries	–	–	–	–	–	(55)	–	–	**(55)**
Adjustments to fair value of prior year acquisitions	–	–	2	–	–	16	4	–	**22**
Exchange and other adjustments	7	–	–	–	–	(12)	2	15	**12**
31 December 2010	**(192)**	**96**	**203**	**(101)**	**67**	**(1,693)**	**276**	**215**	**(1,129)**

27. Deferred and current corporation tax liabilities and assets continued

Certain deferred tax assets and liabilities have been offset where there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income taxes relate to the same fiscal authority. The following is an analysis of the deferred tax balances (after offset) for financial reporting purposes:

	2010 £m	2009 £m
Deferred tax liabilities	**(1,367)**	(1,179)
Deferred tax assets	**238**	534
	(1,129)	(645)

The following is an analysis of the deferred tax balances before offset:

	2010 £m	2009 £m
Deferred tax assets crystallising within one year	**100**	329
Deferred tax assets crystallising after one year	**973**	1,058
	1,073	1,387
Offset against deferred tax liabilities	**(835)**	(853)
Net deferred tax assets	**238**	534
Deferred tax liabilities crystallising within one year	**(325)**	(107)
Deferred tax liabilities crystallising after one year	**(1,877)**	(1,925)
	(2,202)	(2,032)
Offset against deferred tax assets	**835**	853
Net deferred tax liabilities	**(1,367)**	(1,179)

At the balance sheet date the Group had certain deductible temporary differences of £191 million (2009: £148 million) available for utilisation against future profits. No deferred tax asset has been recognised in respect of these temporary differences, due to the unpredictability of future profit streams. Substantially all of these assets may be carried forward indefinitely. At the balance sheet date, temporary differences of £87 million (2009: £76 million) existed in respect of the Group's overseas investments. The deferred tax liability arising on these temporary differences is estimated to be £3 million (2009: £3 million), which has been provided for.

Current tax assets of £81 million (2009: £69 million) include £nil (2009: £36 million) of recoverable petroleum revenue tax.

28. Provisions for other liabilities and charges

Current provisions for other liabilities and charges	1 January 2010 £m	Acquisitions and disposals £m	Charged in the year £m	Unused and reversed in the year £m	Transferred from non-current £m	Utilised £m	**31 December 2010 £m**
Restructuring costs (i), (ii)	56	–	51	(1)	8	(79)	**35**
Decommissioning costs (iii)	–	–	2	–	6	(6)	**2**
Purchase contract loss provision (iv)	106	–	38	(1)	132	(151)	**124**
Other (v)	31	(8)	26	(2)	5	(18)	**34**
	193	**(8)**	**117**	**(4)**	**151**	**(254)**	**195**

Non-current provisions for other liabilities and charges	1 January 2010 £m	Acquisitions and disposals £m	Charged in the year £m	Unused and reversed in the year £m	Revisions and additions £m	Transferred to current £m	Exchange adjustments £m	**31 December 2010 £m**
Restructuring costs (i), (ii)	22	–	5	–	–	(8)	–	**19**
Decommissioning costs (iii)	1,052	55	23	(1)	262	(6)	16	**1,401**
Purchase contract loss provision (iv)	108	–	93	–	–	(132)	2	**71**
Renegotiation provisions (vi)	27	–	–	–	–	–	–	**27**
Other (v)	40	–	4	(6)	–	(5)	–	**33**
	1,249	**55**	**125**	**(7)**	**262**	**(151)**	**18**	**1,551**

28. Provisions for other liabilities and charges continued

Financial and non-financial liabilities within provisions for other liabilities and charges	2010 Current £m	2010 Non-current £m	2009 Current £m	2009 Non-current £m
Financial liabilities:				
Restructuring costs (i), (ii)	**34**	**17**	55	19
Renegotiation provisions (vi)	**–**	**27**	–	27
Other (v)	**34**	**18**	31	25
	68	**62**	86	71
Non-financial liabilities:				
Restructuring costs (i)	**1**	**2**	1	3
Decommissioning costs (iii)	**2**	**1,401**	–	1,052
Purchase contract loss provision (iv)	**124**	**71**	106	108
Other (v)	**–**	**15**	–	15
	127	**1,489**	107	1,178
	195	**1,551**	193	1,249

Maturity analysis for financial liabilities within provisions for other liabilities and charges on an undiscounted basis	2010 £m	2009 £m
Within one year	**68**	86
Between one and two years	**41**	7
Between two and five years	**14**	54
After five years	**7**	10
	130	157

(i) The brought forward restructuring provisions relate to significant restructuring programmes undertaken to achieve the Group's stated cost reduction targets. Included within the provision are costs related to surplus properties of £28 million (2009: £39 million) estimated with reference to the expected cost to be incurred to the point of lease termination, including costs for dilapidations and sub-letting. The provisions are expected to be utilised between 2011 and 2022.

(ii) The amounts charged in the year mainly relate to the exceptional UK restructuring costs recognised in 2010, as explained in note 9 and will be substantially utilised in 2011.

(iii) Provision has been made for the estimated net present cost of decommissioning gas production and storage facilities at the end of their useful lives. The estimate has been based on proven and probable reserves, price levels and technology at the balance sheet date. The timing of decommissioning payments is dependent on the lives of the facilities but is anticipated to occur between 2011 and 2055, with the substantial majority of the provision being utilised between 2020 and 2030. The charge to income includes £25 million of notional interest (2009: £18 million).

(iv) The purchase contract loss provision relates to a UK onerous gas procurement contract and North American wind farm power purchase agreements, as explained in note 9. The provision will be utilised between 2011 and 2015.

(v) Other provisions include outstanding litigation for a number of items (none of which are individually significant) and provision for National Insurance payable in respect of Long Term Incentive Scheme liabilities. The National Insurance provision was based on a share price of 331.60 pence at 31 December 2010 (2009: 281.10 pence) and is expected to be utilised between 2011 and 2015.

(vi) In previous years, the Group renegotiated certain long-term take-or-pay contracts which would have resulted in commitments to pay for gas that would be in excess of requirements and/or at prices above likely market rates. The provision represents the net present cost of estimated payments due to suppliers as consideration for the renegotiations, most of which was settled in 2008, based on the reserves in a group of third–party fields.

29. Fair value of financial instruments

The fair value of a financial instrument is the amount at which the financial instrument could be exchanged in an arm's length transaction between knowledgeable and willing parties under no compulsion to act. The Group has documented internal policies for determining fair value, including methodologies used to establish valuation adjustments required for credit risk.

The fair values of the Group's financial instruments, together with the carrying amounts included in the Balance Sheet are analysed as follows:

Financial assets	Notes	2010 Carrying value £m	2010 Fair value £m	2009 Carrying value £m	2009 Fair value £m
Loans and receivables:					
Trade and other receivables, net of provisions	21	**3,869**	**3,869**	4,020	4,020
Cash and cash equivalents	24	**467**	**467**	1,294	1,294
		4,336	**4,336**	5,314	5,314
Financial assets measured at fair value:					
Derivative financial instruments	22	**790**	**790**	808	808
Securities:					
Treasury gilts designated at fair value through profit and loss		**164**	**164**	104	104
Available-for-sale financial assets:					
Debt instruments		**65**	**65**	118	118
Equity instruments		**28**	**28**	28	28
		257	**257**	250	250

29. Fair value of financial instruments continued

Financial liabilities	Notes	2010 Carrying value £m	2010 Fair value £m	2009 Carrying value £m	2009 Fair value £m
Financial liabilities measured at amortised cost:					
Trade and other payables	25	**(3,578)**	**(3,578)**	(3,575)	(3,575)
Bank overdrafts, loans and other borrowings:					
Bank overdrafts and loans	26	**(277)**	**(241)**	(447)	(422)
Bonds	26	**(3,407)**	**(3,693)**	(3,608)	(3,879)
Other borrowings	26	**–**	**–**	(250)	(252)
Obligations under finance leases	26	**(352)**	**(364)**	(375)	(375)
Provisions	28	**(130)**	**(130)**	(157)	(157)
		(7,744)	**(8,006)**	(8,412)	(8,660)
Financial liabilities at fair value:					
Derivative financial instruments	22	**(1,403)**	**(1,403)**	(2,750)	(2,750)

Securities

Securities comprise Treasury gilts designated at fair value through profit or loss on initial recognition and available-for-sale financial assets.

The fair values of securities are based on quoted market prices, when available. If quoted market prices are not available, fair values are estimated using observable market data.

£23 million of the amounts held as available-for-sale financial assets is ring-fenced within the regulated insurance entity, Centrica Insurance Company Limited, and is not available for use by the rest of the Group (2009: £3 million).

Bank overdrafts, loans and other borrowings

The fair values of bonds are based on quoted market prices. The fair values of bank loans have been determined by discounting cash flows with reference to relevant market rates of interest. The fair values of overdrafts and commercial paper are assumed to equal their book values due to the short-term nature of these amounts. The fair values of obligations under finance leases have been determined by discounting contractual cash flows with reference to the Group's cost of borrowing.

Other financial instruments

Due to their nature and/or short-term maturity, the fair values of trade and other receivables, cash and cash equivalents, trade and other payables and provisions are estimated to approximate their carrying values.

Derivative financial instruments and energy contracts designated at fair value through profit and loss

The fair values of foreign exchange and interest rate derivatives are determined by reference to closing market rates at the Balance Sheet date. The fair values of energy derivatives are determined using valuation techniques based in part on observable market data and in part on internal estimates not currently supported by observable market data. The extent to which fair values of energy derivatives are based on observable market data is determined by the extent to which the market for the underlying commodity is judged to be active. The Group has judged each of the markets in which it operates as active for the purposes of accounting as follows:

Active period of markets (years)	Gas	Power	Coal	Emissions	Oil
UK	2	2	3	2	3
North America	5	Up to 5	n/a	Up to 5	n/a
Europe	n/a	Up to 5	n/a	n/a	n/a

The fair values of energy contracts within the scope of IAS 39 that settle inside the active period of the market are based on quoted market prices and expected volumes, discounted at an average rate of 1% per annum (2009: 1%). The fair values of derivative financial instruments in North America and Europe are based primarily on quoted market prices. In the UK, however, certain energy contracts extend beyond the active period of the market. The fair values of energy contracts that extend beyond the active period of the market are determined by reference in part to published price quotations in active markets and in part by using valuation techniques based on commodity prices derived using assumptions that are based on internal market expectations and expected volumes, discounted using an average discount rate of 3% per annum for 2010.

Where the fair value at initial recognition for such contracts differs from the transaction price, a day-one gain or loss will arise. Such gains and losses are deferred and amortised to the Income Statement based on volumes purchased or delivered over the contractual period until such time as observable market data becomes available (see note 2 for further detail). The amount that has yet to be recognised in the Income Statement relating to the difference between the fair value at initial recognition (the transaction price) and the amount that would have arisen had valuation techniques used for subsequent measurement been applied at initial recognition, less subsequent releases, is as follows:

Net deferred (gains)/losses	2010 £m	2009 £m
1 January	**(86)**	51
Net gains deferred on new transactions	**(2)**	(74)
Recognised in the Income Statement during the year	**(21)**	(63)
31 December	**(109)**	(86)

29. Fair value of financial instruments continued

Fair value hierarchy

Financial assets and financial liabilities measured at fair value are classified into one of three categories:

Level 1

Fair value is determined using observable inputs that reflect unadjusted quoted market prices for identical assets and liabilities, for example exchange-traded commodity contracts valued using close-of-day settlement prices. The adjusted market price used for financial assets held by the Group is the current bid price.

Level 2

Fair value is determined using significant inputs that may be either directly observable inputs or unobservable inputs that are corroborated by market data, for example over-the-counter energy contracts within the active period valued using broker-quotes or third-party pricing services and foreign exchange or interest rate derivatives valued using quotes corroborated with market data.

Level 3

Fair value is determined using significant unobservable inputs that are not corroborated by market data and may be used with internally developed methodologies that result in management's best estimate of fair value, for example energy contracts within the inactive period valued using in-house valuation techniques.

The fair value hierarchy of financial assets and liabilities measured at fair value as at 31 December was as follows:

				2010				2009
	Level 1 £m	Level 2 £m	Level 3 £m	Total £m	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Financial assets								
Derivative financial instruments:								
Energy derivatives	–	492	119	**611**	46	550	64	660
Interest rate derivatives	–	108	–	**108**	–	72	–	72
Foreign exchange derivatives	–	71	–	**71**	2	74	–	76
Treasury gilts designated at fair value through profit and loss	164	–	–	**164**	104	–	–	104
Debt instruments	64	–	1	**65**	62	56	–	118
Equity instruments	17	–	11	**28**	17	–	11	28
Total financial assets	**245**	**671**	**131**	**1,047**	231	752	75	1,058
Financial liabilities								
Derivative financial instruments:								
Energy derivatives	(113)	(849)	(320)	**(1,282)**	(198)	(1,954)	(490)	(2,642)
Interest rate derivatives	–	(16)	–	**(16)**	–	(15)	–	(15)
Foreign exchange derivatives	–	(105)	–	**(105)**	–	(93)	–	(93)
Total financial liabilities	**(113)**	**(970)**	**(320)**	**(1,403)**	(198)	(2,062)	(490)	(2,750)

There were no significant transfers out of Level 1 into Level 2 and out of Level 2 into Level 1 during 2010 and 2009.

The reconciliation of the Level 3 fair value measurements during the year is as follows:

	Equity/debt instruments £m	Energy derivatives £m	2010 £m	Equity/debt instruments £m	Energy derivatives £m	2009 £m
Level 3 financial assets						
1 January	11	64	**75**	3	399	402
Total realised and unrealised losses:						
Gains/(losses) recognised in Income Statement	–	60	**60**	–	(247)	(247)
Gains recognised in Other Comprehensive Income	–	2	**2**	–	–	–
Purchases, sales, issuances and settlements (net)	1	37	**38**	–	–	–
Transfers from Level 3 to Level 2	–	(44)	**(44)**	–	(88)	(88)
Acquisitions	–	–	**–**	8	–	8
31 December	12	119	**131**	11	64	75
Total gains/(losses) for the year for Level 3 financial assets held at the end of the reporting period(i)	**–**	**74**	**74**	–	(258)	(258)

(i) £72 million gains (2009: £258 million losses) for the year for Level 3 financial assets held at the end of the reporting year were recognised within certain re-measurements and £2 million gains (2009: £nil) were recognised in Other Comprehensive Income. The 2009 figures have been restated for comparative purposes.

29. Fair value of financial instruments continued

Energy derivatives	2010 £m	2009 £m
Level 3 financial liabilities		
1 January	**(490)**	(568)
Total realised and unrealised losses:		
Recognised in Income Statement	**(72)**	(54)
Recognised in Other Comprehensive Income	**–**	(9)
Purchases, sales, issuances and settlements (net)	**77**	–
Transfers from Level 3 to Level 2	**165**	141
31 December	**(320)**	(490)
Total losses for the year for Level 3 financial liabilities held at the end of the reporting period(i)	**(86)**	(112)

(i) £86 million losses (2009: £103 million losses) for the year for Level 3 financial liabilities held at the end of the reporting year were recognised within certain re-measurements and £nil (2009: £9 million) were recognised in Other Comprehensive Income. The 2009 figures have been restated for comparative purposes.

The impacts of reasonably possible changes to assumed gas, power, coal, emissions and oil prices on the net fair value of the Group's fair value measurements categorised as Level 3 are as follows:

	2010	2009
Energy price	**Reasonably possible change in variable**	Reasonably possible change in variable
UK gas (p/therm)	**+/–11**	+/–10
UK power (£/MWh)	**+/–5**	+/–5
UK coal (US$/tonne)	**+/–21**	+/–20
UK emissions (€/tonne)	**+/–2**	+/–3
UK oil (US$/bbl)	**+/–18**	+/–19

Increase/(decrease) in fair value	2010 £m	2009 £m
UK energy prices – increase/(decrease)	**9/12**	(17)/17

The impacts disclosed above result from changing the assumptions used for fair valuing energy contracts in relation to gas, power, emissions, coal and oil prices to reasonably possible alternative assumptions at the Balance Sheet date. The fair value impacts only concern those contracts entered into which are within the scope of IAS 39 and are marked-to-market based on valuation models using assumptions that are not currently observable in an active market. The sensitivity analysis provided is hypothetical only and should be used with caution, as the impacts provided are not necessarily indicative of the actual impacts that would be experienced because the Group's actual exposure to market rates is constantly changing as the Group's portfolio of energy contracts changes. Changes in fair values based on a variation in a market variable cannot be extrapolated as the relationship between the change in market variable and the change in fair value will not always be linear. This can be seen in the results from the above 2010 sensitivity analysis. Due to the interaction of various contract price floors and ceilings and optionality in purchase/sales volumes, both scenarios lead to an increase in the total fair value of the Level 3 assets and liabilities.

30. Share capital

Share capital of the Company

Until 10 May 2010, the authorised share capital of the Company was 9,000,000,000 ordinary shares of $6^{14}/_{81}$p each (2009: 9,000,000,000 ordinary shares of $6^{14}/_{81}$p each) and 100,000 cumulative redeemable preference shares of £1 each (2009: 100,000 shares of £1 each). At the Annual General Meeting of the Company held on 10 May 2010, a Special Resolution was passed to delete all provisions of the Company's Memorandum of Association and adopt new Articles of Association in accordance with the Companies Act 2006. The passing of the Special Resolution enabled the removal of the requirement to have an authorised share capital and the removal of the reference to preference shares as no such class of share capital was in issue. Disclosure of authorised share capital is therefore no longer required.

	2010 £m	2009 £m
Allotted and fully paid share capital of the Company		
5,154,005,553 ordinary shares of $6^{14}/_{81}$p each (2009: 5,132,054,073 ordinary shares of $6^{14}/_{81}$p each)	**318**	317

The movement in allotted and fully paid share capital of the Company for the year was as follows:

	2010 Number	2009 Number
1 January	**5,132,054,073**	5,107,658,569
Issued under employee share schemes (i)	**21,951,480**	24,395,504
31 December	**5,154,005,553**	5,132,054,073

(i) Ordinary shares were allotted and issued to satisfy the exercise of share options, share incentive schemes, the Direct Energy Employee Share Purchase Plan and the matching element of the Share Incentive Plan as follows:

30. Share capital continued

	2010	2009
Number	**21,951,480**	24,395,504
Nominal value (£m)	**1.4**	1.5
Consideration (£m) (net of issue costs of £nil (2009: £nil))	**31**	30

The closing price of one Centrica ordinary share on 31 December 2010 was 331.60 pence (2009: 281.10 pence).

Centrica employee share ownership trusts purchase Centrica ordinary shares from the open market and receive newly issued shares to satisfy future obligations of certain employee share schemes. During the year, the trusts purchased 2.5 million shares (2009: 1.9 million), received 4.2 million newly allotted shares (2009: 7.2 million) and released 4.1 million shares (2009: 6.8 million shares) to employees on vesting. At 31 December 2010, the trusts held 8.5 million shares (2009: 5.9 million shares) at a carrying amount of £22 million (2009: £15 million). Until such time as the Company's own shares held by these trusts vest unconditionally, the amount paid for those shares, or the value they were issued at, are held as treasury shares and are deducted from shareholders' equity.

31. Accumulated other comprehensive (loss)/income

	Available-for-sale revaluation reserve £m	Cash flow hedging reserve £m	Foreign currency translation reserve £m	Actuarial gains and losses reserve £m	Total £m
1 January 2010	(6)	(244)	8	(345)	**(587)**
Exchange differences on translation of foreign operations	–	(8)	70	(1)	**61**
Recycling of foreign exchange on disposal of business	–	9	(1)	–	**8**
Actuarial losses on retirement benefit obligations (note 36)	–	–	–	(9)	**(9)**
Net losses on revaluation of available-for-sale securities	(4)	–	–	–	**(4)**
Cash flow hedges:					
Net fair value gains	–	10	–	–	**10**
Transferred to income and expense	–	236	–	–	**236**
Transferred to assets and liabilities	–	19	–	–	**19**
Share of other comprehensive income of joint ventures and associates	–	1	–	14	**15**
Taxation on above items	(1)	(79)	14	(2)	**(68)**
31 December 2010	**(11)**	**(56)**	**91**	**(343)**	**(319)**

	Available-for-sale revaluation reserve £m	Cash flow hedging reserve £m	Foreign currency translation reserve £m	Actuarial gains and losses reserve £m	Total £m
1 January 2009	(15)	(219)	(24)	218	(40)
Exchange differences on translation of foreign operations	–	–	83	–	83
Recycling of foreign exchange on disposal of business	–	10	(10)	–	–
Actuarial losses on retirement benefit obligations (note 36)	–	–	–	(804)	(804)
Net gains on revaluation of available-for-sale securities	11	–	–	–	11
Cash flow hedges:					
Net fair value losses	–	(253)	–	–	(253)
Transferred to income and expense	–	234	–	–	234
Transferred to assets and liabilities	–	(4)	–	–	(4)
Taxation on above items	(2)	(12)	(41)	241	186
31 December 2009	(6)	(244)	8	(345)	(587)

Foreign currency translation reserve

The foreign currency translation reserve comprises exchange translation differences on foreign currency net investments, offset by exchange translation differences on borrowings and derivatives classified as net investment hedges under the requirements of IAS 39. Exchange gains of £70 million (2009: losses of £22 million) on net investments in overseas undertakings have been offset in reserves against exchange losses of £nil (2009: gains of £105 million) on foreign currency borrowings and other instruments used for hedging purposes.

Cash flow hedging reserve

The cash flow hedging reserve comprises fair value movements on instruments designated as cash flow hedges under the requirements of IAS 39. Note 23 provides further detail on cash flow hedging.

Analysis of transfers from cash flow hedging reserve to Income Statement by line item	2010 £m	2009 £m
Gross profit	**236**	235
Net interest income	**–**	(1)
	236	234

31. Accumulated other comprehensive income/(loss) continued

The maturity analysis of amounts included in the cash flow hedging reserve, which includes fair value gains and losses in relation to commodity, interest rate and currency hedges, is as follows:

	2010 £m	2009 £m
Within one year	(38)	(173)
Between one and five years	(6)	(75)
After five years	(12)	4
	(56)	(244)

The maturity profile reflects the timing of expected transfers from the cash flow hedging reserve to the Income Statement as and when the hedged item affects the Income Statement which is, for the most part, on delivery of physical volumes for energy contracts and the accrual of interest for debt contracts.

32. Other equity

	Revaluation reserve £m	Treasury shares reserve £m	Share-based payments reserve £m	Merger reserve £m	Capital redemption reserve £m	Total £m
1 January 2010	26	(15)	87	467	16	581
Employee share schemes:						
Increase in treasury shares	–	(20)	–	–	–	(20)
Exercise of awards	–	13	(44)	–	–	(31)
Value of services provided	–	–	48	–	–	48
Taxation on above items	–	–	20	–	–	20
Exchange adjustments	1	–	2	–	–	3
31 December 2010	**27**	**(22)**	**113**	**467**	**16**	**601**

	Revaluation reserve £m	Treasury shares reserve £m	Share-based payments reserve £m	Merger reserve £m	Capital redemption reserve £m	Total £m
1 January 2009	10	(10)	66	467	16	549
Employee share schemes:						
Increase in treasury shares	–	(7)	–	–	–	(7)
Exercise of awards	–	2	(30)	–	–	(28)
Value of services provided	–	–	38	–	–	38
Reclassification as subsidiary	144	–	–	–	–	144
Disposal of subsidiaries	(126)	–	–	–	–	(126)
Taxation on above items	–	–	12	–	–	12
Exchange adjustments	(2)	–	1	–	–	(1)
31 December 2009	26	(15)	87	467	16	581

Merger reserve

On 17 February 1997, BG plc (formerly British Gas plc) demerged certain businesses (grouped together under GB Gas Holdings Limited (GBGH)) to form Centrica plc. Prior to demerger, the companies comprising the Centrica businesses were transferred to GBGH, a subsidiary undertaking of BG plc. Upon demerger, the share capital of GBGH was transferred to Centrica plc and was recorded at the nominal value of shares issued to BG plc shareholders. In accordance with sections 131 and 133 of the Companies Act 1985, no premium was recorded on the shares issued. On consolidation, the difference between the nominal value of the Company's shares issued and the amount of share capital and share premium of GBGH at the date of demerger was credited to a merger reserve.

Capital redemption reserve

In accordance with section 170 (1) of the Companies Act 1985, the Company transferred to the capital redemption reserve an amount equal to the nominal value of shares repurchased and subsequently cancelled.

Revaluation reserve

During 2005, the revaluation of the Group's existing interest in Centrica SHB Limited to fair value, following the acquisition by the Group of the remaining 40% stake in the company, was recorded as a revaluation reserve adjustment. During 2009, the revaluation of the Group's existing interest in Segebel S.A. and producing gas and oil assets located in Alberta, Canada, following the acquisition by the Group of additional interests, was recorded as a revaluation reserve adjustment. The subsequent disposal of Segebel S.A. resulted in a transfer of the revaluation gain relating to this investment to retained earnings.

Treasury shares reserve

Treasury shares reserve reflects the cost of shares in the Company held in share-based payment plans to meet future obligations to deliver shares to employees on vesting.

32. Other equity continued

Share-based payments reserve

The share-based payments reserve reflects the obligation to deliver shares to employees under the Group's share schemes in return for services provided.

33. Non-controlling interests

	2010 £m	2009 £m
1 January	**63**	60
Acquisition of new business	**–**	802
Profit on ordinary activities after taxation	**7**	12
Accumulated other comprehensive income	**–**	1
Purchase of non-controlling interests	**–**	(201)
Dividends paid	**–**	(11)
Disposal of business	**–**	(589)
Liquidation of business [(i)]	**(70)**	–
Exchange adjustments	**–**	(11)
31 December	**–**	63

(i) On 14 May 2010 GF Two Limited (formerly Goldfish Holdings Limited) and its subsidiary, GF One Limited (formerly Goldfish Bank Limited), both non-trading entities were put into liquidation. Lloyds Banking Group plc held a 30% economic interest in these entities until liquidation.

Non-controlling interests' share of profit from operations after taxation can be analysed as follows:

	2010			2009		
	Business performance £m	Exceptional items and certain re-measurements £m	Results for the year £m	Business performance £m	Exceptional items and certain re-measurements £m	Results for the year £m
Continuing operations	**7**	**–**	**7**	2	–	2
Discontinued operations	**–**	**–**	**–**	48	(38)	10
	7	**–**	**7**	50	(38)	12

34. Notes to the Group Cash Flow Statement

(a) Reconciliation of Group operating profit to net cash flow from operating activities

	2010 £m	2009 £m
Continuing operations		
Group operating profit including share of result of joint ventures and associates	**3,074**	1,175
Less share of loss/(profits) of joint ventures and associates	**7**	(1)
Group operating profit before share of results of joint ventures and associates	**3,081**	1,174
Add back/(deduct):		
Amortisation and write-down of intangible assets	**176**	209
Depreciation and write-down of property, plant and equipment	**973**	708
Impairments of joint ventures and associates	**4**	–
Profit on sale of businesses	**(26)**	(54)
Profit on sale of property, plant and equipment and other intangible assets	**4**	–
Movement in provisions	**159**	301
Pension service cost	**129**	74
Pension contributions	**(441)**	(403)
Employee share scheme costs	**48**	38
Re-measurement of energy contracts [(i)]	**(1,097)**	135
Unrealised foreign exchange gains on operating cash and cash equivalents	**–**	1
Operating cash flows before movements in working capital	**3,010**	2,183
Decrease in inventories	**31**	35
Decrease in trade and other receivables [(ii)]	**162**	781
Increase in trade and other payables [(ii)]	**242**	83
Cash generated from continuing operations	**3,445**	3,082
Income taxes paid	**(412)**	(329)
Net petroleum revenue tax paid	**(128)**	(174)
Interest received	**5**	13
Interest paid	**(11)**	(3)
Payments relating to exceptional charges	**(223)**	(203)
Net cash flow from continuing operating activities	**2,676**	2,386

34. Notes to the Group Cash Flow Statement continued

	2010 £m	2009 £m
Discontinued operations		
Operating profit/(loss) including share of result of joint ventures and associates	67	(46)
Less share of loss of joint ventures and associates	–	2
Operating profit/(loss) before share of joint ventures and associates	67	(44)
(Deduct)/add back:		
Amortisation and write-down of intangible assets	–	41
Depreciation and write-down of property, plant and equipment	–	25
Movement in provisions	4	25
Re-measurement of energy contracts	(42)	49
Operating cash flows before movements in working capital	29	96
Decrease in inventories	–	7
(Increase)/decrease in receivables	(151)	337
Increase/(decrease) in payables	136	(168)
Income taxes paid	(6)	(10)
Interest paid	(1)	(1)
Net cash flow from discontinued operating activities	7	261
Net cash flow from operating activities	2,683	2,647

(i) Adds back unrealised losses arising from re-measurement of energy contracts, including those related to proprietary trading activities.
(ii) Includes net inflow of £466 million of cash collateral in 2010 (2009: net outflow of £79 million).

(b) Net debt

	2010 £m	2009 £m
Current borrowings (note 26)	(77)	(86)
Non-current borrowings (note 26)	(3,959)	(4,594)
Less:		
Cash and cash equivalents	467	1,294
Securities – current	23	74
Securities – non-current	234	176
	(3,312)	(3,136)

(c) Reconciliation of net increase in cash and cash equivalents to movement in net debt

	2010 £m	2009 £m
Net decrease in cash and cash equivalents	(833)	(1,569)
Cash and cash equivalents of disposal groups classified as held for sale	16	(19)
	(817)	(1,588)
Add back/(deduct):		
Net purchase of securities	56	128
Cash inflow from additional debt	(267)	(1,887)
Cash outflow from payment of capital element of finance leases	23	22
Cash outflow from repayment of other debt	928	872
	(77)	(2,453)
Revaluation of:		
Securities	7	14
Loans and other borrowings	(40)	15
	(110)	(2,424)
Increase in interest payable on loans and other borrowings	(2)	(25)
Acquisitions	–	(477)
Disposals	(56)	298
Exchange adjustments	(8)	4
Other non-cash movements	–	(1)
Movement in net debt	(176)	(2,625)
Net debt at 1 January	(3,136)	(511)
Net debt at the end of the year	(3,312)	(3,136)

(d) Exploration and evaluation cash flows

Included within the £661 million (2009: £604 million) purchase of intangible assets in investing activities is £224m (2009: £46 million) relating to exploration and evaluation of oil and gas assets.

34. Notes to the Group Cash Flow Statement continued

(e) Relationship between current tax charge and taxes paid	UK £m	North America £m	Other £m	2010 £m	2009 £m
Current tax charge:					
Corporation tax	289	28	(26)	**291**	158
Petroleum revenue tax	223	–	–	**223**	112
	512	**28**	**(26)**	**514**	270
Taxes paid:					
Corporation tax	368	44	–	**412**	329
Petroleum revenue tax	128	–	–	**128**	174
	496	**44**	**–**	**540**	503

Differences between current tax charged and taxes paid arose principally due to the following factors:

- UK corporation tax is paid, based on estimated profits, partly during the year and partly in the following year. Fluctuations in profits from year to year may therefore give rise to divergence between the charge for the current year and taxes paid; and
- Petroleum revenue tax payments are based on income realised in the preceding period, with subsequent adjustments to reflect actual profits. Variations in production from period to period may therefore lead to temporary differences between tax charged and tax paid.

35. Share-based payments

Employee share schemes are designed to encourage participants to align their objectives with those of shareholders. Centrica operates nine employee share schemes.

(a) Summary of principal share-based payment plans and movements in the number of shares and options outstanding

Deferred and Matching Share Scheme (DMSS)

Awards under the DMSS are generally reserved for employees within the senior executive group. Under normal conditions the grant date of the scheme is the first day of each bonus year. This is followed by a vesting period of four years, being the bonus year plus a three-year performance period. The fair value of the award reflects the market value of the shares at the grant date. The scheme comprises three separate elements:

(i) Deferred shares

The scheme requires participants to defer between 20% and 40% of their annual pre-tax bonus into the scheme. The shares are held in trust over the three-year performance period, during which time they cannot be withdrawn. An employee who leaves prior to the vesting date will forfeit their right to the shares (except where permitted by the rules of the scheme). All shares held in trust will be eligible to receive dividends. The number of shares deferred is estimated from the participant's maximum bonus and the likelihood of bonus payout in the bonus year. Subsequent revisions are made based on the actual bonus paid in the year.

(ii) Investment shares

The scheme allows participants to elect to invest an additional amount of their annual bonus into the scheme up to a maximum of 50% of their total potential after-tax bonus for the year. This 50% limit includes the pre-tax amount automatically deferred each year. The shares may be funded directly from the employee (or through a release of the employee's Long Term Incentive Scheme (LTIS) shares at the Company's discretion), and thus the shares do not attract an IFRS 2 charge.

(iii) Matching shares

Deferred and investment shares will be matched with conditional matching shares, which will be released upon the achievement, over a three-year performance period, of three-year Group economic profit performance targets. Group economic profit is calculated by taking adjusted Group operating profit (as defined in note 6) after tax and subtracting a charge for capital employed based on the Group's weighted average cost of capital. Further information on the operation of the DMSS and related performance conditions can be found on pages 54 to 55. The likelihood of achieving the performance conditions is taken into account in calculating the number of awards expected to vest. Estimates are made in year one and revised in subsequent years. An employee who leaves prior to the vesting date will forfeit their right to the shares (except where permitted by the rules of the scheme).

The number of shares originally granted and fair value allocated are estimated on the grant date and then adjusted following the announcement of the actual annual performance bonus and subsequent investment by participants. A reconciliation of movements in allocations of deferred and matching shares actually made is shown in the table at the bottom of this section. Details of the fair values of awards granted and related assumptions are included in section (c) below.

35. Share-based payments continued

Executive Share Option Scheme (ESOS)

Under the ESOS, the Board may grant options over shares in Centrica plc to employees of the Group. Options are granted with a fixed exercise price equal to the market price of the shares at the legal date of grant which approximates, or is the same as, the grant date for accounting purposes, and are generally reserved for employees within the senior executive group. Options granted under the ESOS have all vested and became exercisable in full on the third anniversary of the last date of grant in 2006. The exercise of options is subject to continued employment within the Group (except where permitted by the rules of the scheme). Performance conditions are non-market based and therefore not included in the fair value calculations. Early exercise has been taken into account by estimating the expected life of the options. A reconciliation of option movements is as follows:

	2010		2009	
	Number in thousands	**Weighted average exercise price**	Number in thousands	Weighted average exercise price
Outstanding at start of the year	**11,180**	**£2.15**	17,986	£2.09
Granted	**–**	**–**	–	–
Exercised	**(6,148)**	**£2.09**	(6,242)	£1.95
Forfeited	**(20)**	**£2.18**	(564)	£2.33
Outstanding at end of the year	**5,012**	**£2.24**	11,180	£2.15
Exercisable at end of the year	**5,012**	**£2.24**	11,180	£2.15

For options outstanding at the end of the period, the range of exercise prices and average remaining life was as follows:

2010				2009			
Range of exercise prices	**Weighted average exercise price**	**Number of shares in thousands**	**Average remaining contractual life years**	Range of exercise prices	Weighted average exercise price	Number of shares in thousands	Average remaining contractual life years
£1.30-£1.39	**£1.31**	**306**	**2.2**	£1.30–£1.39	£1.31	1,256	3.2
£1.90-£1.99	**£1.99**	**594**	**3.2**	£1.90–£1.99	£1.99	1,239	4.2
£2.00-£2.09	**£2.03**	**1,562**	**3.4**	£2.00–£2.09	£2.03	3,298	4.5
£2.10-£2.19	**–**	**–**	**–**	£2.10–£2.19	£2.14	823	1.7
£2.20-£2.29	**£2.24**	**61**	**4.7**	£2.20–£2.29	£2.24	184	5.7
£2.50-£2.59	**£2.54**	**2,489**	**5.6**	£2.50–£2.59	£2.54	4,380	6.4
	£2.24	**5,012**	**4.4**		£2.15	11,180	4.9

For options exercised during the period, the weighted average share price at the date of exercise was £2.98 (2009: £2.57).

Long Term Incentive Scheme (LTIS)

Under the LTIS, allocations of shares in Centrica plc are generally reserved for employees at senior management level. The number of shares to be released to participants is calculated subject to the Company's total shareholder return (TSR) and earnings per share (EPS) growth during the three years following the grant date. Shares are released to participants immediately following the end of the period in which performance is assessed, however release of shares is subject to continued employment within the Group at the date of release (except where permitted by the rules of the scheme). The vesting of half of each award is made on the basis of TSR performance and is valued using a Monte Carlo simulation model. The vesting of the remaining half of awards is dependent on EPS growth. This is deemed to be a non-market condition under IFRS 2 and therefore the fair value of these awards is considered to be the market value at the grant date. The likelihood of achieving the performance conditions is taken into account in calculating the number of awards expected to vest. Further details on the operation of LTIS including related performance conditions are provided on pages 55 and 56.

For shares released during the period, the weighted average share price was £2.98 (2009: £2.32). The number of shares vested at the end of the year was 50,346 (2009: 82,632). A reconciliation of movements in allocations is shown in the table at the bottom of this section. Details of the fair values of awards granted and related assumptions are included in section (c) below.

Sharesave

Under Sharesave, the Board may grant options over shares in Centrica plc to all UK-based employees of the Group. To date, the Board has approved the grant of options with a fixed exercise price equal to 80% of the average market price of the shares for the three days prior to invitation which is three to four weeks prior to the grant date. Employees pay a fixed amount from salary into a savings account each month, and may elect to save over three and/or five years. At the end of the savings period, employees have six months in which to exercise their options using the funds saved. If employees decide not to exercise their options, they may withdraw the funds saved, and the options expire six months after maturity. Exercise of options is subject to continued employment within the Group (except where permitted by the rules of the scheme). Details of the fair values of awards granted and related assumptions are included in section (b) below.

35. Share-based payments continued

A reconciliation of movements in allocations is as follows:

	2010		2009	
	Number in thousands	Weighted average exercise price	Number in thousands	Weighted average exercise price
Outstanding at start of the year	**45,653**	**£2.09**	38,186	£2.20
Granted	**12,195**	**£2.28**	25,103	£1.94
Exercised	**(7,060)**	**£2.16**	(8,882)	£1.98
Forfeited	**(3,666)**	**£2.11**	(8,376)	£2.27
Expired	**(239)**	**£2.54**	(378)	£2.03
Outstanding at end of the year	**46,883**	**£2.12**	45,653	£2.09
Exercisable at end of the year	**11**	**£2.41**	16	£2.05

For options outstanding at the end of the year, the range of exercise prices and the average remaining life was as follows:

2010				2009			
Range of exercise prices	Weighted average exercise price	Number of shares in thousands	Average remaining contractual life years	Range of exercise prices	Weighted average exercise price	Number of shares in thousands	Average remaining contractual life years
£1.60–£1.69	**–**	**–**	**–**	£1.60–£1.69	£1.67	3,181	0.3
£1.90–£1.99	**£1.94**	**21,790**	**2.3**	£1.90–£1.99	£1.94	23,817	3.3
£2.10–£2.19	**£2.12**	**2,515**	**0.4**	£2.10–£2.19	£2.12	2,670	1.4
£2.20–£2.29	**£2.28**	**20,791**	**2.3**	£2.20–£2.29	£2.27	10,214	2.3
£2.50–£2.59	**£2.59**	**1,787**	**1.4**	£2.50–£2.59	£2.59	5,771	1.1
	£2.12	**46,883**	**2.2**		£2.09	45,653	2.5

For options exercised during the year, the weighted average share price at the date of exercise was £2.90 (2009: £2.36).

Share Award Scheme (SAS)

Under the SAS, allocations of shares in Centrica plc are made to selected employees at middle management levels, based on recommendation by the Chief Executive and the Group Director, Human Resources. There is no contractual eligibility for SAS and each year's award is made independently from previous awards. Allocations are subject to no performance conditions and vest unconditionally subject to continued employment within the Group (except where permitted by the rules of the scheme) in two stages – half of the award vesting after two years, the other half vesting after three years. On vesting, additional shares are awarded or a cash payment is made to reflect dividends that would have been paid on the allocations during the vesting period. The fair value is therefore considered to be the market value at the date of grant.

For shares released during the year, the weighted average share price at the date of release was £2.97 (2009: £2.31). A reconciliation of movements in allocations is shown in the table at the bottom of this section. Details of the fair values of awards granted and related assumptions are included in section (c) below.

Deferred Bonus Plan (DBP)

Awards under the DBP are generally reserved for a select group of employees. Under normal conditions the grant date of the plan is the first day of each bonus year. This is followed by a vesting period of three years, being the bonus year plus a two-year employment period (for awards made in 2010), and the bonus year plus a two-year performance period (for awards made in 2011).

The plan was first operated in 2010, in respect of the bonus period from the acquisition of the Venture business until the end of the 2009 financial year. The plan allowed participants to elect to defer up to 100% of their bonus into the plan. Deferred shares were matched with one and a half matching shares which will vest unconditionally for employees after being held for two years.

From 2011 onwards, the plan will require participants to defer 20% of their annual bonus into the plan (as deferred shares) and allow participants to elect to invest up to a further 30% of their annual bonus (as investment shares). Deferred and investment shares will be matched with conditional matching shares, ranging between one for one and two for one shares, dependent on an employee's grade. The vesting of matching shares will be subject to the satisfaction of company performance conditions. The likelihood of achieving the performance conditions is taken into account in calculating the number of awards expected to vest. Vesting of deferred awards and all matching awards is subject to continued employment within the Group (except where permitted by the rules of the plan). On vesting, additional shares are awarded or a cash payment is made to reflect the dividends that would have been paid on the allocations during the vesting period.

The number of shares originally granted and fair value allocated are estimated on the grant date and then adjusted following the announcement of the actual annual performance bonus and subsequent investment by participants. A reconciliation of the movement in allocations of deferred and matching shares actually made is shown in the table at the bottom of this section. Details of the fair values of awards granted under IFRS 2 and related assumptions are included in section (c) below.

35. Share-based payments continued

A reconciliation of movements in allocations for the DMSS, LTIS, SAS and DBP schemes is as follows:

Number of shares (in thousands)	2010 DMSS	2010 LTIS	2010 SAS	2010 DBP	2009 DMSS	2009 LTIS	2009 SAS	2009 DBP
Balance at start of year	**11,425**	**29,968**	**5,487**	**–**	6,564	26,497	3,607	–
Granted	**4,394**	**10,366**	**3,187**	**702**	5,708	13,111	3,370	–
Released	**(2,791)**	**(3,438)**	**(1,354)**	**–**	–	(6,319)	(1,191)	–
Forfeited (i)	**(344)**	**(4,599)**	**(332)**	**(9)**	(847)	(3,321)	(299)	–
Balance at end of year	**12,684**	**32,297**	**6,988**	**693**	11,425	29,968	5,487	–

(i) LTIS forfeitures include 2,291,970 (2009: 2,236,299) shares forfeited for non-performance reasons.

(b) Fair values and associated details of options granted under Sharesave

	2010	2009
No. of options granted (in thousands)	**12,195**	25,103
Weighted average fair value at grant date	**£0.67**	£0.49
Weighted average share price at grant date	**£2.97**	£2.30
Weighted average exercise price	**£2.28**	£1.94
Expected volatility (i)	**31.4%**	29.4%
Contractual option life	**4.2 years**	4.3 years
Expected life	**3.9 years**	4.3 years
Vesting period	**3.9 years**	4.0 years
Expected dividend yield	**4.5%**	5.0%
Risk-free interest rate (ii)	**2.3%**	2.4%
Expected forfeitures	**30%**	31%

(i) The expected volatility is based on historical volatility over the last three years.
(ii) The risk-free rate of return is the yield on zero-coupon UK Government bonds of a term consistent with the expected option life.

(c) Fair values and associated details of shares granted under the principal schemes

	2010 DMSS	2010 LTIS	2010 SAS	2010 DBP	2009 DMSS	2009 LTIS	2009 SAS	2009 DBP
No. of equity instruments granted (in thousands)	**4,855**	**10,366**	**3,187**	**1,160**	5,032	13,111	3,370	1,750
Weighted average fair value at grant date	**£3.32**	**£2.42**	**£2.97**	**£3.32**	£2.81	£1.65	£2.22	£2.81
Expected performance lapses	**0%**	**n/a**	**n/a**	**0%**	0%	n/a	n/a	n/a
Expected dividend yield	**n/a**	**n/a**	**n/a**	**n/a**	n/a	n/a	n/a	n/a
Vesting period	**4 years**	**3 years**	**2.5 years**	**3 years**	4 years	3 years	2.5 years	3 years
Expected volatility (i)	**n/a**	**30.4%**	**n/a**	**n/a**	n/a	31.2%	n/a	n/a
Expected forfeitures	**10%**	**20%**	**18%**	**25%**	25%	25%	20%	0%
Risk-free rate (ii)	**n/a**	**1.8%**	**n/a**	**n/a**	n/a	2.2%	n/a	n/a
Average volatility of FTSE 100	**n/a**	**27.2%**	**n/a**	**n/a**	n/a	31.2%	n/a	n/a
Average cross-correlation of FTSE 100 (iii)	**n/a**	**48.3%**	**n/a**	**n/a**	n/a	39.8%	n/a	n/a

(i) The expected volatility is based on historical volatility over the last three years.
(ii) The risk-free rate of return is the yield on zero-coupon UK Government bonds of a term consistent with the expected option life.
(iii) The cross-correlation of the FTSE 100 has been obtained from a model which calculates the correlation between Centrica's historical share price and each of the remaining FTSE 100 companies over the period commensurate with the performance period of the awards.

(d) Other share schemes

Below is a brief summary of the three other schemes. These are significantly smaller than the principal share schemes discussed above and therefore no detailed disclosures have been included for these schemes.

Restricted Share Scheme (RSS)

Awards under the RSS are normally reserved for certain selected key employees at senior management levels, based on recommendation by the Chief Executive and the Group Director, Human Resources. Neither the Executive Directors nor the next tiers of executive management are eligible to participate. There is no contractual eligibility for RSS and each year's award is made independently from previous awards. Allocations are not normally subject to performance conditions and normally vest unconditionally subject to continued employment within the Group (except where permitted by the rules of the scheme) in one or more stages dependent on the individual awards. On vesting, additional shares are awarded or a cash payment is made to reflect dividends that would have been paid on the allocations during the vesting period.

35. Share-based payments continued

Share Incentive Plan (SIP) and Direct Energy Employee Share Purchase Plan (ESPP)

SIP relates to UK employees and has a three year vesting period. ESPP relates to North America employees and has a two year vesting period. Under both SIP and ESPP employees may purchase 'partnership shares' through monthly salary deductions. The Company then awards one 'matching share' for every two partnership shares purchased. Partnership shares may be withdrawn at any time; however, matching shares are forfeited if the related partnership shares are withdrawn within the vesting period. Matching shares in the SIP vest unconditionally for employees after being held for three years and in the ESPP after being held for two years. Vesting of matching shares is also subject to continued employment within the Group (except where permitted by the rules of the plans). Within the UK there is a maximum of 22 matching shares per employee per month. Both UK partnership shares and matching shares are held in trust. Matching shares are valued at the market price at the grant date.

36. Pensions

Pension schemes

The majority of the Group's UK employees at 31 December 2010 were members of one of the three main schemes: the Centrica Pension Scheme, the Centrica Engineers Pension Scheme and the Centrica Pension Plan (formerly known as the Centrica Management Pension Scheme) (together the 'registered pension schemes'). The Centrica Pension Scheme (final salary section) and the Centrica Pension Plan (a final salary scheme) were closed to new members from 1 April 2003 and 1 July 2003 respectively. On 1 January 2009 the majority of the active members of the Centrica Pension Scheme (final salary section) were transferred to the Centrica Pension Plan (2008 section). The Centrica Pension Scheme also has a career average salary section which was closed to new members with effect from 1 July 2008 and replaced by a defined contribution section which is open to new members. The Centrica Engineers Pension Scheme (final salary section) was closed to new members from 1 April 2006, and a career average salary section was added to the scheme at that date. These schemes are defined benefit schemes and are tax-approved funded arrangements. They are subject to independent valuations at least every three years, on the basis of which the qualified actuary certifies the rate of employer contributions which, together with the specified contributions payable by the employees and proceeds from the schemes' assets, are expected to be sufficient to fund the benefits payable under the schemes.

The Centrica Unapproved Pension Scheme is an unfunded arrangement which provides benefits to certain employees whose benefits under the main schemes would otherwise be limited by the earnings cap. The Group also has a commitment to provide certain pension and post-retirement benefits to employees of Direct Energy Marketing Limited (Canada) under a defined benefit scheme.

The latest full actuarial valuations were carried out at the following dates: the registered pension schemes at 31 March 2009, the Unapproved Pension Scheme at 6 April 2010 and the Direct Energy Marketing Limited pension plan at 14 June 2008. These have been updated to 31 December 2010 for the purposes of meeting the requirements of IAS 19. Investments have been valued for this purpose at market value.

Governance

The UK-registered pension schemes are managed by trustee companies whose boards consist of both company-nominated and member-nominated directors. Each scheme holds units in the Centrica Combined Common Investment Fund (CCCIF), which holds the combined assets of the participating schemes. The method of allocation of units is set out in the Trust Deed of the CCCIF. The trustee of the CCCIF is a company, Centrica Combined Common Investment Fund Limited (CCCIF Limited) which was incorporated on 23 September 2002. The trustee of the CCCIF may be appointed or removed by the participant schemes. The board of CCCIF Limited is comprised of nine directors; three independent directors, three directors appointed by Centrica plc (including the chairman) and one director appointed by each of the three participating schemes. No direct investments are made in securities issued by Centrica plc or any of its subsidiaries, property leased to or owned by Centrica plc or any of its subsidiaries or securities of any fund manager or any of their associated companies.

Under the terms of the Pensions Act 2004, Centrica plc ('the Company') and each trustee board must agree the funding rate for its defined benefit pension scheme and a recovery plan to fund any deficit against the scheme-specific statutory funding objective. This approach was first adopted for the triennial valuations completed at 31 March 2006 and was again reflected in the 31 March 2009 valuations.

In addition, the Group has a commitment to provide contributions to defined contribution schemes for certain employees in the UK and North America who are not members of one of the Group's defined benefit pension schemes.

Major assumptions used for the actuarial valuation	31 December 2010 %	31 December 2009 %
Rate of increase in employee earnings	**4.7**	4.8
Rate of increase in pensions in payment and deferred pensions	**3.7**	3.8
Discount rate	**5.7**	6.0
RPI inflation assumption	**3.7**	3.8

On 8 July 2010 the Government announced that the inflation measure for minimum increases in occupational schemes was to be switched from the Retail Price Index (RPI) to the Consumer Price Index (CPI). This change only impacts the revaluation of deferred pensions in the main section of the Centrica Pension Plan. The resulting reduction in defined benefit obligation of £36 million has been treated as a change in assumption and recognised in the Statement of Comprehensive Income. The inflation assumption for CPI at 31 December 2010 is 3.0%.

The assumptions relating to longevity underlying the pension liabilities at the Balance Sheet date have been based on a combination of standard actuarial mortality tables, scheme experience and other relevant data, and include a medium cohort allowance, as published by the Institute and Faculty of Actuaries, with an underpin. The assumptions are equivalent to future longevity for members in normal health approximately as follows:

36. Pensions continued

Life expectancy at age 65 for a member	2010 Male Years	2010 Female Years	2009 Male Years	2009 Female Years
Currently aged 65	**22.6**	**24.0**	22.5	23.9
Currently aged 45	**24.4**	**25.3**	24.3	25.2

At 31 March 2009, the date of the most recent actuarial review, the schemes had approximately 34,900 members and beneficiaries.

The other demographic assumptions have been set having regard to the latest trends in scheme experience and other relevant data. The assumptions are reviewed and updated as necessary as part of the periodic actuarial valuation of the pension schemes.

Impact of changing material assumptions	2010 Increase/ decrease in assumption	2010 Indicative effect on scheme liabilities %	2009 Increase/ decrease in assumption	2009 Indicative effect on scheme liabilities %
Rate of increase in employee earnings	**0.25%**	**+/–1**	0.25%	+/–1
Rate of increase in pensions in payment and deferred pensions	**0.25%**	**+/–5**	0.25%	+/–5
Discount rate	**0.25%**	**–/+6**	0.25%	–/+6
Inflation assumption	**0.25%**	**+/–6**	0.25%	+/–6
Longevity assumption	**1 year**	**+/–2**	1 year	+/–2

The expected long-term rate of return and market value of the assets and the present value of the liabilities in the schemes at 31 December were:

	2010 Expected long term rate of return per annum %	2010 Valuation £m	2009 Expected long term rate of return per annum %	2009 Valuation £m
UK equities	**8.0**	**659**	8.3	1,101
Non-UK equities	**8.0**	**1,261**	8.3	1,106
High-yield debt	**7.5**	**229**	6.6	127
Fixed-interest bonds	**5.5**	**1,182**	6.0	524
Index-linked gilts	**4.2**	**773**	4.5	364
Property	**7.6**	**134**	8.0	55
Cash pending investment	**5.6**	**97**	6.1	256
Total fair value of plan assets	**6.6**	**4,335**	7.4	3,533
Present value of defined benefit obligation		**(4,574)**		(4,098)
Net liability recognised in the Balance Sheet		**(239)**		(565)
Associated deferred tax asset recognised in the Balance Sheet		**67**		158
Net pension liability		**(172)**		(407)
Net liability recognised in the Balance Sheet comprises:				
Surpluses		**–**		–
Deficits		**(239)**		(565)
		(239)		(565)

The overall expected rate of return on assets is a weighted average based on the actual plan assets held in each class and the expected returns on separate asset classes less costs of administering the plan and taxes paid by the plan itself. The returns on separate asset classes were derived as follows: the expected rate of return on equities, high-yield debt and property are based on the expected median return over a 10-year period, as calculated by the independent company actuary. The median return over a longer period than ten years was not expected to be materially dissimilar. The expected rate of return on fixed-interest bonds and index-linked gilts reflects yields directly observable on bond market indices. The expected rate of return on cash pending investment reflects the average rate of return on the actual asset classes that the cash was invested in shortly after the year end.

Included within the schemes' liabilities above are £33 million (2009: £31 million) relating to unfunded pension arrangements. Included within non-current securities are £52 million (2009: £48 million) of investments, held by the Law Debenture Trust on behalf of the Company, as security in respect of the Centrica Unapproved Pension Scheme.

Based on the triennial valuation at 31 March 2009, the Company and the trustees of the registered pension schemes agreed a schedule for deficit payments. An amount of £308 million has been paid in the year to 31 December 2010 and the following further deficit payments will be made: £6 million in 2011 and £57 million per annum from 2012 to 2016. In addition, a charge over the Humber power station has been provided as additional security for the trustees.

36. Pensions continued

Analysis of the amount charged to the Income Statement	2010 £m	2009 £m
Current service cost – continuing operations (i)	**115**	68
Loss on curtailment	**14**	6
Net charge to operating profit	**129**	74
Current service cost – discontinued operations	**–**	2
Net charge to the Income Statement	**129**	76

(i) In addition to current service cost on the Group's defined benefit pension schemes, the Group also charged £5 million (2009: £3 million) to operating profit in respect of defined contribution pension schemes.

Analysis of the amount credited to notional interest	2010 £m	2009 £m
Expected return on pension scheme assets	**275**	209
Interest on pension scheme liabilities	**(249)**	(185)
Net credit to notional interest income	**26**	24

Analysis of the actuarial (loss)/gain recognised in the Statement of Comprehensive Income	2010 £m	2009 £m
Actuarial gain (actual return less expected return on pension scheme assets)	**154**	344
Experience gains/(losses) arising on the scheme liabilities	**74**	(104)
Changes in assumptions underlying the present value of the schemes' liabilities	**(237)**	(1,044)
Actuarial loss to be recognised in accumulated other comprehensive loss, before adjustment for taxation	**(9)**	(804)
Cumulative actuarial (losses)/gains recognised in reserves at 1 January, before adjustment for taxation	**(480)**	324
Cumulative actuarial losses recognised in reserves at 31 December, before adjustment for taxation	**(489)**	(480)

Five-year history of surplus/(deficit)	2010 £m	2009 £m	2008 £m	2007 £m	2006 £m
Plan assets	**4,335**	3,533	2,642	3,327	2,988
Defined benefit obligation	**(4,574)**	(4,098)	(2,755)	(3,230)	(3,284)
Surplus/(deficit)	**(239)**	(565)	(113)	97	(296)

Five-year history of experience gains and losses	2010	2009	2008	2007	2006
Difference between the expected and actual return on scheme assets:					
Amount (£m)	**154**	344	(1,121)	(38)	95
Percentage of scheme assets	**3.6%**	9.7%	42.4%	1.1%	3.2%
Experience gains and losses on scheme liabilities:					
Amount (£m)	**74**	(104)	–	(16)	145
Percentage of the present value of scheme liabilities	**1.6%**	2.5%	–	0.5%	4.4%
Total actuarial (loss)/gain recognised in the Statement of Comprehensive Income:					
Amount (£m)	**(9)**	(804)	(399)	284	475
Percentage of the present value of scheme liabilities	**0.2%**	19.6%	14.5%	8.8%	14.5%

Movement in the defined benefit obligation during the year	2010 £m	2009 £m
1 January	**4,098**	2,755
Current service cost	**115**	70
Loss on curtailment	**14**	6
Interest on scheme liabilities	**249**	185
Plan participants' contributions	**33**	30
Benefits paid from schemes	**(104)**	(97)
Benefits paid by company	**(1)**	(1)
Actuarial loss	**163**	1,148
Acquisitions of businesses	**–**	63
Disposals of businesses	**–**	(62)
Exchange adjustments	**7**	1
31 December	**4,574**	4,098

36. Pensions continued

Movement in plan assets during the year	2010 £m	2009 £m
1 January	**3,533**	2,642
Expected return on scheme assets	**275**	209
Actuarial gain	**154**	344
Employer contributions	**441**	403
Plan participants' contributions	**33**	30
Benefits paid from schemes	**(104)**	(97)
Acquisitions of businesses	**–**	46
Disposals of businesses	**–**	(45)
Exchange gains	**3**	1
31 December	**4,335**	3,533

Estimated future employer contribution rates (pensionable salary and percentage of pensionable salary) for the year ended 31 December 2011	£m	%
Centrica Pension Scheme – Final salary section	**4**	**31.9**
Centrica Pension Scheme – Career average salary section	**96**	**16.3**
Centrica Engineers Pension Scheme – Final salary section	**173**	**24.6**
Centrica Engineers Pension Scheme – Career average salary section	**74**	**14.2**
Centrica Pension Plan – Management section	**70**	**26.7**
Centrica Pension Plan – 2008 section	**120**	**25.3**

37. Business combinations

Trinidad and Tobago

On 5 August 2010, the Group acquired full control of a business constituting a portfolio of interests in a number of gas assets located off the coast of Trinidad and Tobago for total cash consideration of $375 million (£247 million). The portfolio consists of a producing gas field which supplies gas into the Atlantic LNG facility as well as areas of development and exploration. The acquisition increases the gas reserves of the Group and provides access to the Atlantic basin LNG market. The acquisition is included within the Upstream UK – Upstream gas and oil segment.

Goodwill of £68 million arose on the acquisition. This is principally attributable to deferred tax arising on the fair value adjustments but also to an element of going concern value that is expected to give access to future opportunities and benefits in the region. None of the goodwill recognised is expected to be deductible for tax purposes. The fair values disclosed in the table below are provisional due to the complicated arrangements in the production sharing agreement and the interactions with the local tax regulations. Acquisition costs were negligible.

Wildcat Hills

On 30 September 2010, the Group acquired full control of a business constituting a portfolio of interests in a number of gas assets located to the West of Calgary in Canada for total cash consideration of CAN$352 million (£218 million). The portfolio consists of 97 natural gas and producing wells and working interests in three processing facilities. The acquisition increases the natural gas reserves of the Group and provides additional gas to meet supply requirements of the North American retail customers. The acquisition is included within the North America – Upstream and wholesale energy segment.

Goodwill of £nil arose on the acquisition. The fair values disclosed in the table below are provisional pending finalisation of oil and gas reserves acquired and due to ongoing work occurring on the decommissioning provision and abandonment asset.

Acquisition costs of £1 million were incurred as part of the acquisition and expensed to the Income Statement as part of operating costs.

Clockwork

On 1 July 2010, the Group acquired the business and net assets of Clockwork Home Services Inc and 100% of the shares of Air Time Canada Inc, together known as Clockwork. The total cash consideration for the acquisition was $183 million (£122 million), which includes deferred consideration of $17 million (£11 million) payable in 2012.

Clockwork provides heating, air conditioning, ventilation, plumbing and electrical services in the US and Canada. The acquisition supports the Group's existing home services business in the US and Canada by providing increased geographical coverage, as well as expanding Direct Energy's shared expertise. The acquisition is included within the North America – Residential and business services segment.

Goodwill of £87 million arose on the acquisition. This is principally attributable to the synergies relating to procurement, location rationalisation and overhead realignment. £67 million of the goodwill recognised is expected to be deductible for tax purposes.

For acquired trade receivables, the fair value and gross amount receivable is £4 million and £5 million respectively. £1 million is the best estimate of contractual cash flows not expected to be collected. The fair value and gross amount receivable of other acquired receivables is £3 million.

37. Business combinations continued

The fair values disclosed in the table below are provisional pending finalisation of working capital and due to ongoing work on the intangible assets and deferred revenue balances at acquisition.

Acquisition costs of £1 million were incurred as part of the acquisition and were expensed to the income statement as part of operating costs.

Fair values of the identifiable assets acquired and liabilities assumed

	Trinidad and Tobago £m	Wildcat Hills £m	Clockwork £m
Intangible assets	6	35	42
Property, plant and equipment – development and producing gas and oil field assets	245	213	–
Property, plant and equipment – other	–	–	4
Cash and cash equivalents	–	–	2
Inventories	–	–	2
Trade and other receivables: current	–	1	7
Trade and other payables: current	–	–	(15)
Trade and other payables: non-current	–	–	(7)
Deferred tax liabilities	(55)	–	–
Provisions for other liabilities and charges: non-current	(17)	(31)	–
Net assets acquired	**179**	**218**	**35**
Goodwill	68	–	87
Total consideration	**247**	**218**	**122**
Consideration comprises:			
Cash consideration	247	218	111
Deferred cash consideration	–	–	11

	Trinidad and Tobago £m	Wildcat Hills £m	Clockwork £m
Revenue incurred since the acquisition date and included within the Group Income Statement	15	16	59
Profit/(loss) incurred since the acquisition date and included within the Group Income Statement	–	(1)	(1)

Pro forma information

The pro forma consolidated results of the Group, as if the acquisitions of Clockwork, Trinidad and Tobago and Wildcat Hills had been made at the beginning of the period, would include revenue from continuing operations of £22,564 million (compared to reported Group revenue of £22,423 million and profit after taxation of £1,952 million (compared to reported profit after taxation of £1,942 million).

In preparing the pro forma results, revenue and costs have been included as if the businesses were acquired on 1 January 2010 and inter-company transactions had been eliminated. This information is not necessarily indicative of the results of the combined Group that would have occurred had the purchases actually been made at the beginning of the period presented, or indicative of the future results of the combined Group.

Other acquisitions

During the year the following acquisitions occurred as described below. Collectively the acquisitions are immaterial to the Group's financial statements. The fair values are provisional unless stated otherwise.

On 1 October 2010, the Group acquired the business and net assets of the gas and electricity services businesses of Connaught Compliance for total cash consideration of £11 million. Goodwill of £8 million arose on the acquisition. The business specialises in the installation, service and maintenance of commercial gas boilers and electrical systems. The acquisition supports the Group's existing provision of business services and is included within the Downstream UK – Business energy supply and services segment.

On 12 April 2010, the Group acquired 100% of the shares in Hillserve Limited for total cash consideration of £5 million. Goodwill of £3 million arose on the acquisition. Hillserve Limited is a regional installer of insulation based in North-West England. The acquisition supports the Group's intentions to develop its own insulation business within the UK. The acquisition is included within the Downstream UK – Residential energy supply segment.

On 6 December 2010, the Group acquired 100% of the shares in ECL Contracts Limited (ECL) for total cash consideration of £4 million. Goodwill of £3 million arose on the acquisition. ECL is a specialist external-wall insulation company. The acquisition supports the Group's aim to be the leading supplier of domestic insulation, and allows the Group to diversify its own product range beyond loft and cavity wall insulation into solid wall insulation. The acquisition is included within the Downstream UK – Residential energy supply segment.

37. Business combinations continued

On 28 April 2010, the Group acquired the business and net assets of REPower for total cash consideration of $5 million (£3 million). Goodwill of £nil arose on the acquisition. REPower is engaged in the development of prepayment software, processes and systems. The acquisition supports the Group's intentions of launching and commercialising pre-paid retail electricity in the North American electricity market. The acquisition is included within the North America – Residential energy supply segment.

On 29 March 2010, the Group acquired a number of producing gas assets in Craigmyle, Canada for total cash consideration of CAN$4 million (£2 million). Goodwill of £nil arose on the acquisition. The acquisition increases the gas reserves of the Group and creates operational synergies within Canada. The acquisition is included within the North America – Upstream and wholesale energy segment.

The Group also acquired Cool Planet Technologies Limited on 17 November 2010 for £1 million, JK Environmental Services (UK) Limited on 3 December 2010 for £1 million and 12 Dyno franchisees during 2010 for total consideration of £2 million.

2009 acquisitions – fair value updates

During the prior year, the Group acquired 100% of the issued share capital of Venture Production Plc (Venture) for total consideration of £1,253 million in a series of transactions occurring between 18 March 2009 and 9 November 2009. The Group obtained a controlling interest in Venture on 27 August 2009 and Venture was consolidated as a subsidiary of the Group from this date. The fair values disclosed in the 2009 Annual Report and Accounts were provisional as the Directors had not yet reached a final determination on all aspects of the fair value exercise at that time.

During the year the Directors have reached a final determination on all aspects of the fair value exercise. A number of revisions to the fair values disclosed in the 2009 Annual Report and Accounts were made. The key factors that led to these fair value revisions are described below. The revisions resulted in an overall decrease in the fair value of net assets of Venture and associated increase in goodwill at the date of acquisition of £50 million. These revisions are immaterial and so have not been adjusted in the prior year and accordingly have been reflected in the Group Balance Sheet at 31 December 2010.

	Key factors	Increase/(decrease) in fair value of net assets of Venture at acquisition date £m
Property, plant and equipment	Updated assumptions and estimates in respect of key inputs used in the valuation models for future contractual payments	(61)
Current liabilities	Updated assumptions and expectations in respect of key inputs used in the valuation of certain tax related liability positions	(4)
Provisions for other liabilities and charges	Updated assumptions and expectations in respect of key inputs used in the valuation of decommissioning liabilities	(7)
Net deferred tax liabilities	Updated assumptions and expectations in respect of the deferred tax arising plus the deferred tax effect of the above adjustments	22

38. Disposals, discontinued operations and disposal groups held for sale

Wind farm assets

On 5 February 2010 the Upstream UK – Power generation segment disposed of 50% of the issued share capital and 50% of the shareholder loan of Centrica (Lincs) Limited (Lincs) to Dong Wind (UK) Limited and Siemens Project Ventures GmbH for £55 million. Centrica has retained 50% of its interests in Lincs, which owns a wind farm under construction off the Lincolnshire coast. Centrica's investment in Lincs is now being treated as a joint venture due to the joint control that arises from this transaction.

This disposal followed the sale on 11 December 2009 of 50% of the issued share capital of GLID Wind Farms TopCo Limited (GLID), formerly known as Centrica Renewable Holdings Limited, which was sold to the Trust Company of the West for £84 million. Centrica retained 50% of the issued share capital of GLID, which owns 100% of the issued share capital of both Glens of Foudland Limited and Lynn and Inner Dowsing Limited (the owners and operators of the Glens of Foudland and Lynn and Inner Dowsing wind farms respectively). Centrica's investment in GLID is now being treated as a joint venture due to the joint control that arises from this transaction.

European businesses

The European segment was classified as a discontinued operation from 30 June 2009 following the Group's decision to dispose of its 100% interests in Segebel S.A. (Segebel), Oxxio BV (Oxxio) in the Netherlands and Centrica Energía S.L. (Centrica Energía) in Spain.

The disposal of Segebel to EDF was completed on 26 November 2009.

The sale of Centrica Energía to Villar Mir Energía S.L. (VME) was completed on 4 November 2010 for total proceeds of €35 million (£29 million). The proceeds include a dividend of €21 million (£17 million) which was paid before the business was disposed of.

The sale process for the disposal of Oxxio has taken longer than anticipated when the assets were originally classified as held for sale and was therefore on-going during the year. Completion is anticipated during 2011. Accordingly Oxxio continued to be reported within discontinued operations during 2010. The group leases a power station in Rijnmond, the Netherlands, through a tolling agreement. This power station became operational in May 2010 and the initial expectation was that the agreement would be transferred with the Oxxio disposal so the results of the power station were included within discontinued operations. During December 2010 a decision was taken not to include the lease on the power station in the current sale process and its results have been removed from discontinued operations and included within the Upstream UK – Industrial and commercial segment. The comparatives have not been restated as the power station was not operational in 2009.

(a) Discontinued operations

The results of Centrica Energía and Oxxio, which continued to be reported within discontinued operations in 2010 are analysed as follows:

Year ended 31 December	Business performance £m (2010)	Exceptional items and certain re-measurements £m (2010)	Results for the year £m (2010)	Business performance £m (2009)	Exceptional items and certain re-measurements £m (2009)	Results for the year £m (2009)
Revenue	**590**	**–**	**590**	2,357	–	2,357
Cost of sales before exceptional items and certain re-measurements	**(514)**	**–**	**(514)**	(2,008)	–	(2,008)
Re-measurement of energy contracts	**–**	**69**	**69**	–	(123)	(123)
Cost of sales	**(514)**	**69**	**(445)**	(2,008)	(123)	(2,131)
Gross profit	**76**	**69**	**145**	349	(123)	226
Operating costs before exceptional items	**(78)**	**–**	**(78)**	(246)	–	(246)
Exceptional items	**–**	**–**	**–**	–	(24)	(24)
Operating costs	**(78)**	**–**	**(78)**	(246)	(24)	(270)
Share of profits/(losses) in joint ventures and associates, net of interest and taxation	**–**	**–**	**–**	2	(4)	(2)
Operating (loss)/profit	**(2)**	**69**	**67**	105	(151)	(46)
Net interest expense	**(1)**	**–**	**(1)**	(12)	–	(12)
(Loss)/profit from operations before taxation	**(3)**	**69**	**66**	93	(151)	(58)
Taxation on profit from operations	**(5)**	**(2)**	**(7)**	(53)	20	(33)
(Loss)/profit after taxation from operations	**(8)**	**67**	**59**	40	(131)	(91)
Net gain on disposal of Segebel and Energía (after taxation)	**3**	**–**	**3**	–	297	297
(Loss)/profit after taxation from discontinued operations	**(5)**	**67**	**62**	40	166	206
Attributable to:						
Equity holders of the parent	**(5)**	**67**	**62**	(8)	204	196
Non-controlling interests	**–**	**–**	**–**	48	(38)	10
	(5)	**67**	**62**	40	166	206

The 2009 comparatives additionally include the results of Segebel up to its disposal date.

38. Disposals, discontinued operations and disposal groups held for sale continued

(b) Disposal groups classified as held for sale

Assets, and associated liabilities, that are expected to be recovered principally through a sale transaction rather than continuing use are classified as held for sale on the face of the Balance Sheet, and presented separately from the assets and liabilities of the Group's continuing operations.

At 31 December 2010, the sale of Oxxio in the Netherlands had not completed and consequently the related assets and liabilities have been presented as held for sale on the face of the Balance Sheet as follows:

	£m
Goodwill	**62**
Other intangible assets	**15**
Property, plant and equipment	**34**
Derivative financial instruments: non-current	**1**
Trade and other receivables: current	**330**
Derivative financial instruments: current	**10**
Cash and cash equivalents	**3**
Assets of disposal groups classified as held for sale	**455**
Trade and other payables: current	**(344)**
Provisions for other liabilities and charges: current	**(4)**
Derivative financial instruments: current	**(17)**
Derivative financial instruments: non-current	**(3)**
Liabilities of disposal groups classified as held for sale	**(368)**
Net assets of disposal groups classified as held for sale	**87**
Total shareholders' equity	**87**

Trade and other receivables include £269 million financial assets and £61 million non-financial assets. £218 million of financial trade and other receivables relate to residential customers, £38 million relate to business customers and £13 million relate to treasury, trading and energy procurement counterparties, net of provisions for credit losses. Trade and other payables include £56 million financial liabilities and £288 million non-financial liabilities.

The fair value of financial instruments held by disposal groups classified as held for sale are equal to their carrying values.

The derivative financial instruments included in the Balance Sheet comprise energy derivatives – held for trading under IAS 39 and relate to short-term forward market purchases and sales of electricity. Net gains of £62 million associated with these derivatives were recognised in the Income Statement during 2010.

The derivative financial instruments held by discontinued operations are classified into the following fair value hierarchies (as defined in note 29):

	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Energy derivatives – held for trading under IAS 39				
Financial assets	3	8	–	**11**
Financial liabilities	(5)	(15)	–	**(20)**

38. Disposals, discontinued operations and disposal groups held for sale continued

(c) Disposals

On 4 November 2010 the disposal of Centrica Energía resulted in a loss on disposal of £6 million. On 5 February 2010 the disposal of Lincs resulted in no gain or loss on disposal. The loss on disposal arising in the period from these transactions is as follows:

	Lincs £m	Centrica Energía £m
Non-current assets	42	1
Current assets	63	71
Current liabilities	(2)	(56)
Non-current liabilities	(103)	–
Total net assets disposed	**–**	**16**
Cash consideration	5	12
Hedging reserve released upon transfer of derivatives	(9)	–
Revaluation of retained interest	6	–
Disposal costs	(2)	(2)
Loss on disposal before taxation	–	(6)
Taxation on profit on disposal	–	–
Loss on disposal after taxation	**–**	**(6)**

On 11 August 2010 the Group disposed of its 100% interest in Hummingbird Oil Pte Ltd resulting in an exceptional gain on disposal of £25 million (see note 9). Hummingbird Oil Pte Ltd was a non-core investment acquired during the 2009 acquisition of Venture plc and was held at £nil net book value.

In 2009, the disposal of the Group's 100% interest in Segebel on 26 November 2009 resulted in a profit on disposal, net of taxation, of £297 million. During 2010, a surplus provision of £9 million relating to the disposal of Segebel was released.

The disposal of 50% of the Group's interest in GLID Wind Farms TopCo Limited on 11 December 2009 resulted in an exceptional profit on disposal, net of taxation, of £49 million.

39. Commitments and contingencies

(a) Commitments

Commitments in relation to the acquisition of property, plant and equipment	2010 £m	2009 £m
Construction of a power station at Langage	**–**	43
Construction of Lincs wind farm [(i)]	**–**	385
Gas field developments	**119**	116
Other power station capital expenditure	**52**	16
Other	**13**	3
	184	563

(i) The Lincs wind farm was disposed of on 5 February 2010, as described in note 38.

Commitments in relation to the acquisition of intangible assets	2010 £m	2009 £m
Renewable obligation certificates to be purchased from:		
Joint ventures [(i)]	**1,145**	578
Other parties	**631**	868
Carbon emissions certificates	**61**	326
Certified emission reduction certificates	**105**	110
Exploration activity	**80**	205
Other	**66**	40
	2,088	2,127

(i) Renewable obligation certificates are purchased from several joint ventures which produce power from wind energy. The commitments disclosed above are the gross contractual commitments and do not take into account the Group's economic interest in the joint venture.

39. Commitments and contingencies continued

Commitments in relation to other contracts	2010 £m	2009 £m
Liquefied natural gas capacity	**629**	675
Transportation capacity	**666**	689
Outsourcing of services	**444**	325
Other	**414**	444
	2,153	2,133

Commitments in relation to commodity purchase contracts	2010 £m	2009 (restated) (i) £m
Within one year (ii)	**8,517**	7,431
Between one and five years (iii)	**21,287**	20,275
After five years	**10,616**	14,149
	40,420	41,855

(i) Restated to net off amounts receivable under commodity sales contracts where there is a right of set-off with the counterparty.
(ii) Includes £132 million (2009: £144 million) in relation to discontinued operations, as described in note 38.
(iii) Includes £38 million (2009: £112 million) in relation to discontinued operations, as described in note 38.

The Group procures gas and electricity through a mixture of production from owned gas fields, power stations, wind farms and procurement contracts. Procurement contracts include short-term forward market purchases of gas and electricity at fixed and floating prices. They also include gas and electricity contracts indexed to market prices and long-term gas contracts with non-gas indexation. The commitments in relation to commodity purchase contracts disclosed above are stated net of amounts receivable under commodity sales contracts, where there is a right of set-off with the counterparty.

The total volume of gas to be taken under certain long-term structured contracts depends on a number of factors, including the actual reserves of gas that are eventually determined to be extractable on an economic basis. The commitments disclosed above are based on the minimum quantities of gas that the Group is contracted to buy at estimated future prices.

The commitments in this note differ in scope and in basis from the maturity analysis of energy derivatives disclosed in note 22. Whilst the commitments in relation to commodity purchase contracts include all purchase contracts, only certain procurement and sales contracts are within the scope of IAS 39 and included in note 22. In addition, the volumes used in calculating principal values in note 22 are estimated using valuation techniques, rather than being based on minimum contractual quantities and in note 22 there is no offset of amounts receivable under commodity sales contracts where there is a right of set-off with the counterparty.

Commitments by associates and joint ventures	2010 £m	2009 £m
Share of associates' commitments	**290**	302
Share of joint ventures' commitments	**319**	2
	609	304

(b) Operating lease commitments

At 31 December, the total of future minimum lease payments under non-cancellable operating leases for each of the following years were:

	2010 £m	2009 £m
Within one year (i)	**146**	109
Between one and five years (ii)	**331**	214
After five years	**486**	116
	963	439

	2010 £m	2009 £m
The total of future minimum sub-lease payments expected to be received under non-cancellable operating sub-leases at 31 December	**22**	19
Lease and sub-lease payments recognised as an expense in the year were as follows:		
Minimum lease payments	**101**	68
Contingent rents – renewables (iii)	**115**	113
Contingent rents – other	**4**	3

(i) Includes £1 million (2009: £2 million) in relation to discontinued operations, as described in note 38.
(ii) Includes £2 million (2009: £2 million) in relation to discontinued operations, as described in note 38.
(iii) The Group has entered into long-term arrangements with renewable providers to purchase physical power, renewable obligation certificates and levy exemption certificates from renewable sources. Payments made under these contracts are contingent upon actual production and therefore the commitment to a minimum lease payment included above is £nil (2009: £nil). Payments made for physical power are charged to the Income Statement as incurred and disclosed as contingent rents.

39. Commitments and contingencies continued

(c) Decommissioning costs

The Group has provided certain guarantees and indemnities in respect of decommissioning costs. The most significant is to BG Group plc in respect of the decommissioning costs of the Morecambe gas fields. The Company and its wholly owned subsidiary, Hydrocarbon Resources Limited, have agreed to provide security, in respect of such guarantees and indemnities, to BG International Limited, which, as original licence holder for the Morecambe gas fields, will have exposure to decommissioning costs relating to the Morecambe gas fields should liabilities not be fully discharged by the Group. The security is to be provided when the estimated future net revenue stream from the Morecambe gas fields falls below 150% of the estimated cost of such decommissioning. The nature of the security may take a number of different forms and will remain in force until the costs of such decommissioning have been irrevocably discharged and the relevant Department of Business, Innovation and Skills (formerly Department of Business Enterprise and Regulatory Reform) decommissioning notice in respect of the Morecambe gas fields has been revoked.

(d) Contingent liabilities

There are no material contingent liabilities.

(e) Guarantees and indemnities

In connection with the Group's energy trading, transportation and upstream activities, certain Group companies have entered into contracts under which they may be required to prepay or provide credit support or other collateral in the event of a significant deterioration in creditworthiness. The extent of credit support is contingent upon the balance owing to the third party at the point of deterioration.

40. Related party transactions

During the year, the Group entered into the following arm's length transactions with related parties who are not members of the Group:

	2010		2009	
	Sale of goods and services £m	**Purchase of goods and services £m**	Sale of goods and services £m	Purchase of goods and services £m
Joint ventures:				
Barrow Offshore Wind Limited	**–**	**21**	–	22
Braes of Doune Wind Farm (Scotland) Limited	**–**	**13**	–	17
Glens of Foundland Wind Farm Limited	**–**	**3**	–	–
GLID Wind Farms TopCo Limited	**–**	**8**	–	9
Inner Dowsing Wind Farm Limited	**–**	**19**	–	–
Lynn Wind Farm Limited	**–**	**18**	–	–
Associates:				
Alertme.com Limited	**–**	**1**	–	–
Lake Acquisitions Limited	**278**	**284**	–	1
North Sea Infrastructure Partners Limited	**–**	**24**	–	34
Sevan Production General Partnership (i)	**–**	**13**	–	–
Other investments:				
Point Fortin LNG Exports Limited	**12**	**–**	–	–
	290	**404**	–	83

(i) Sevan Production General Partnership is an associate of Hummingbird Oil Pte Ltd, which was disposed of by the Group on 11 August 2010 (see note 38).

Investment and funding transactions for joint ventures and associates are disclosed in note 19.

Balances outstanding with related parties at 31 December were as follows:

	2010		2009	
	Amounts owed from related parties £m	**Amounts owed to related parties £m**	Amounts owed from related parties £m	Amounts owed to related parties £m
Joint ventures:				
Bacton Storage Company Limited	**14**	**–**	2	–
Barrow Offshore Wind Limited	**–**	**5**	11	5
Braes of Doune Wind Farm (Scotland) Limited	**15**	**3**	21	3
Lincs Wind Farm Limited	**128**	**–**	–	–
Glens of Foundland Wind Farm Limited	**–**	**1**	–	–
GLID Wind Farms TopCo Limited	**49**	**19**	41	26
Inner Dowsing Wind Farm Limited	**–**	**5**	–	–
Lynn Wind Farm Limited	**–**	**4**	–	–
Associates:				
Lake Acquisitions Limited	**33**	**53**	–	–
North Sea Infrastructure Partners Limited	**–**	**2**	–	3
Other investments:				
Point Fortin LNG Exports Limited	**5**	**–**	–	–
	244	**92**	75	37

40. Related party transactions continued

The terms of the outstanding balances related to trade receivables from related parties are typically 30 to 120 days. The balances are unsecured and will be settled in cash. No provision for bad or doubtful debts owed by related parties was required (2009: £nil).

Key management personnel comprise members of the Board and Executive Committee, a total of 14 individuals at 31 December 2010 (2009: 13). Key management personnel and their families purchase gas, electricity and home services products from the Group for domestic purposes on terms equal to those for other employees of the Group.

Remuneration of key management personnel	2010 £m	2009 £m
Short-term benefits	10	10
Post-employment benefits	1	1
Share-based payments	10	9
	21	20

41. Fixed-fee service and insurance contracts

Fixed-fee service contracts are entered into with home services customers in the UK and home and business services customers in North America. These contracts continue until cancelled by either party to the contract. These plans incorporate both an annual service element and a maintenance element.

Insurance contracts are entered into with home service customers in the UK by British Gas Insurance Limited, an entity regulated by the Financial Services Authority (FSA) since August 2009. Product offerings include central heating, boiler and controls, plumbing and drains and electrical appliance insurance cover. These contracts are normally for periods of 12 months with the option of renewal.

Fixed-fee service and insurance contracts protect purchasers of these contracts against the risk of breakdown of electrical, plumbing, heating, cooling and household appliances, resulting in the transfer of an element of risk from contract holders to Centrica. Benefits provided to customers vary in accordance with terms and conditions of the contracts entered into, however, generally include repair and/or replacement of the items affected.

The risk and level of service required within these contracts is dependent upon the occurrence of uncertain future events, in particular the number of call-outs, the cost per call-out and the nature of the fault. Accordingly, the timing and amount of future cash outflows related to the contracts is uncertain.

The key terms and conditions that affect future cash flows are as follows:

- provision of labour and parts for repairs, dependent on the agreement and associated level of service;
- one safety and maintenance inspection either annually or in every continuous two-year period, as set out in the agreement;
- no limit to the number of call-outs to carry out repair work; and
- caps on certain maintenance and repair costs within fixed-fee service and insurance contracts.

Revenue from fixed-fee service and insurance contracts is recognised with regard to the incidence of risk over the life of the contract, reflecting the seasonal propensity of claims to be made under the contracts and the benefits receivable by the customer, which span the life of the contract as a result of emergency maintenance being available throughout the contract term. Cost of sales relates directly to the engineer workforce employed by Centrica within home services, the cost of which is accounted for over a 12-month period with adjustments made to reflect the seasonality of workload over a given year. The costs of claims under the fixed-fee service and insurance contracts will be the costs of the engineer workforce employed by Centrica within home services. These costs are accounted for over a 12-month period with adjustments made to reflect the seasonality of workload over a given year.

Weather conditions and the seasonality of maintenance can affect the number of call-outs, the cost per call-out and the nature of the fault. Centrica's obligations under the terms of home services fixed-fee service and insurance contracts are based on the number of breakdowns occurring within the contract period.

Centrica actively manages the risk exposure of these uncertain events by undertaking the following risk mitigation activities:

- an initial service visit is performed for central heating care and insurance cover. If, at the initial visit, faults that cannot be rectified are identified, the fixed-fee service and insurance contract will be cancelled and no further cover provided;
- an annual or biennial safety and maintenance inspection is performed to ensure that issues are identified before they develop into significant maintenance or breakdown issues; and
- caps on certain maintenance and repair work are incorporated into fixed-fee service and insurance contracts to limit liability in areas considered to be higher risk in terms of prevalence and cost to repair.

The Group considers the adequacy of estimated future cash flows under the contracts to meet expected future costs under the contracts. Any deficiency is charged immediately to the Income Statement.

Service requests are sensitive to the reliability of appliances as well as the impact of weather conditions. Each incremental 1% increase in service and insurance requests would impact profit and equity by approximately £9 million (2009: £8 million). The contracts are not exposed to any interest rate risk or significant credit risk and do not contain any embedded derivatives.

41. Fixed-fee service and insurance contracts continued

The fixed-fee service claims and insurance claims notified during the year were £259 million (2009: £305 million) and £104 million (2009: £2 million) respectively and were exactly matched by expenses related to fixed-fee service and insurance contracts. All claims are settled immediately and in full. Due to the short lead time between claims being incurred and claims being rectified, there are £nil material provisions outstanding at the balance sheet date (2009: £nil).

	2010 £m	2009 £m
Total revenue	**1,098**	995
Expenses relating to fixed-fee service and insurance contracts	**851**	803
Deferred income (unearned premium)	**57**	55
Accrued income	**34**	21

42. Events after the balance sheet date

The Directors propose a final dividend of 10.46 pence per ordinary share (totalling £539 million) for the year ended 31 December 2010. The dividend will be submitted for formal approval at the Annual General Meeting to be held on 9 May 2011 and, subject to approval, will be paid on 15 June 2011 to those shareholders registered on 3 May 2011.

43. Principal undertakings

31 December 2010	Country of incorporation/formation	Percentage holding in ordinary shares and net assets	Principal activity
Subsidiary undertakings [(i)]			
Bastrop Energy Partners LP	USA	100	Power generation
Brae Canada Ltd	Canada	100	Investment company
British Gas Insurance Limited	England	100	Insurance provision
British Gas Services Limited	England	100	Business energy supply and services
British Gas Trading Limited	England	100	Energy supply
Caythorpe Gas Storage Limited	England	100	Gas storage
Centrica Barry Limited	England	100	Power generation
Centrica Brigg Limited	England	100	Power generation
Centrica Energy Limited [(ii)]	England	100	Proprietary energy trading
Centrica Energy (Trading) Limited [(iii)]	England	100	Proprietary energy trading
Centrica Energy Operations Limited	England	100	Power generation
Centrica KL Limited	England	100	Power generation
Centrica KPS Limited	England	100	Power generation
Centrica Langage Limited	England	100	Power generation
Centrica Norway Limited	England	100	Gas and oil exploration and production
Centrica PB Limited	England	100	Power generation
Centrica Renewable Energy Limited	England	100	Renewable energy holding company
Centrica Resources Limited	England	100	Gas and oil production
Centrica RPS Limited	England	100	Power generation
Centrica SHB Limited	England	100	Power generation
Centrica Storage Limited	England	100	Gas storage
Clockwork Inc [(iv)]	USA	100	Home services
CPL Retail Energy LP	USA	100	Energy supply
Direct Energy LP	USA	100	Energy supply
Direct Energy Business LLC	USA	100	Energy supply
Direct Energy Marketing Inc	USA	100	Wholesale energy trading
Direct Energy Marketing Limited	Canada	100	Energy supply and home services
Direct Energy Partnership	Canada	100	Energy supply
Direct Energy Resources Partnership	Canada	100	Gas production
Direct Energy Services LLC	USA	100	Energy supply and home services
Direct Energy US Home Services Inc	USA	100	Home/commercial services
Dyno Holdings Limited	England	100	Home services
Energy America LLC	USA	100	Energy supply
Frontera Generation LP	USA	100	Power generation
GB Gas Holdings Limited	England	100	Holding company
Hydrocarbon Resources Limited	England	100	Gas production
Paris Generation LP	USA	100	Power generation
The Centrica Gas Production LP	England	100	Gas production
Venture North Sea Gas Limited	Scotland	100	Gas and oil production
Venture North Sea Gas Exploration Limited	England	100	Gas and oil production
Venture North Sea Oil Limited	Scotland	100	Gas and oil production
Venture Production (Services) Limited	Scotland	100	Employee services
Venture Production Limited [(v)]	Scotland	100	Holding company
WTU Retail Energy LP	USA	100	Energy supply
Joint ventures and associates			
Barrow Offshore Wind Limited	England	50	Power generation
Braes of Doune Wind Farm (Scotland) Limited	Scotland	50	Power generation
GLID Wind Farms TopCo Limited	England	50	Renewable energy holding company
Lincs Wind Farm Limited [(vi)]	Scotland	50	Renewable energy holding company
North Sea Infrastructure Partners Limited	Scotland	49.9	Pipeline construction/operation
Lake Acquisitions Limited	England	20	Power generation
NNB Holding Company Limited	England	20	Power generation

(i) All principal undertakings are held indirectly by the Company. The information is only given for those subsidiaries which in the Directors' opinion principally affect the figures shown in the Financial Statements.
(ii) As at 31 December 2010 the company was called Accord Energy Limited and changed its name to Centrica Energy Limited with effect from 1 February 2011.
(iii) As at 31 December 2010 the company was called Accord Energy (Trading) Limited and changed its name to Centrica Energy (Trading) Limited with effect from 1 February 2011.
(iv) Holding company for the Clockwork group of companies acquired in 2010, previously called Direct Energy (CW) Inc.
(v) During 2010, Venture Production plc was re-registered as a private limited company.
(vi) Joint venture formed in 2010.

We have audited the parent Company Financial Statements of Centrica plc for the year ended 31 December 2010 which comprise the Company Balance Sheet and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice).

Respective responsibilities of Directors and auditors

As explained more fully in the Directors' Responsibilities Statement set out on page 48, the Directors are responsible for the preparation of the parent Company Financial Statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the parent Company Financial Statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the Company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

Scope of the audit of the Financial Statements

An audit involves obtaining evidence about the amounts and disclosures in the Financial Statements sufficient to give reasonable assurance that the Financial Statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the parent Company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Directors; and the overall presentation of the Financial Statements.

Opinion on Financial Statements

In our opinion the parent Company Financial Statements:

- give a true and fair view of the state of the Company's affairs as at 31 December 2010;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Opinion on other matters prescribed by the Companies Act 2006

In our opinion:

- the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006; and
- the information given in the Directors' Report for the financial year for which the parent Company Financial Statements are prepared is consistent with the parent Company Financial Statements.

Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept by the parent Company, or returns adequate for our audit have not been received from branches not visited by us; or
- the parent Company Financial Statements and the part of the Directors' Remuneration Report to be audited are not in agreement with the accounting records and returns; or
- certain disclosures of Directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

Other matter

We have reported separately on the Group Financial Statements of Centrica plc for the year ended 31 December 2010.

John Maitland
(Senior Statutory Auditor)
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
London
24 February 2011

31 December	Notes	2010 £m	2009 £m
Fixed assets			
Tangible assets	III	**38**	39
Investments in subsidiary undertakings	IV	**2,132**	2,122
		2,170	2,161
Current assets			
Debtors	V	**10,134**	9,882
Current asset investments	VI	**266**	1,259
Cash at bank and in hand		**93**	10
		10,493	11,151
Creditors (amounts falling due within one year)			
Borrowings	VII	**(50)**	(53)
Other creditors	VIII	**(5,606)**	(4,910)
		(5,656)	(4,963)
Net current assets		**4,837**	6,188
Total assets less current liabilities		**7,007**	8,349
Creditors (amounts falling due after more than one year)			
Borrowings	VII	**(3,622)**	(3,982)
Other creditors	VIII	**(69)**	(69)
		(3,691)	(4,051)
Provisions for liabilities	IX	**(6)**	(8)
Net assets		**3,310**	4,290
Capital and reserves – equity interests			
Called up share capital		**318**	317
Share premium account	X	**833**	778
Capital redemption reserve	X	**16**	16
Profit and loss account	X	**2,143**	3,179
Shareholders' funds	XI	**3,310**	4,290

The Financial Statements on pages 143 to 148 were approved and authorised for issue by the Board of Directors on 24 February 2011 and were signed on its behalf by:

Sam Laidlaw
Chief Executive

Nick Luff
Group Finance Director

The notes on pages 144 to 148 form part of these Financial Statements, along with notes 30 and 35 to the Group Financial Statements.

I. Principal accounting policies of the Company

Accounting principles

The Company Balance Sheet has been prepared in accordance with applicable UK Accounting Standards consistently applied and under the Companies Act 2006.

Basis of preparation

The accounts have been prepared under the going concern basis. No profit and loss account is presented for the Company as permitted by section 408(3) of the Companies Act 2006. The Company loss after tax for the year ended 31 December 2010 was £361 million (2009: £132 million loss).

Presentation of derivative financial instruments

In line with the Group's accounting policy for derivative financial instruments, the Company has classified those derivatives held for the purpose of treasury management as current or non-current, based on expected settlement dates.

Employee share schemes

The Group has a number of employee share schemes, detailed in note 35, under which it makes equity-settled share-based payments to certain employees. Equity-settled share-based payments are measured at fair value at the date of grant (excluding the effect of non-market-based vesting conditions). The fair value determined at the grant date is expensed on a straight-line basis together with a corresponding increase in equity over the vesting period, based on the Group's estimate of the number of awards that will vest and adjusted for the effect of non-market-based vesting conditions. The issue of share incentives by the Company to employees of its subsidiaries represents additional capital contributions, whereby an addition to the Company's investment in subsidiary undertakings is reported with a corresponding increase in shareholders' funds. The addition to the Company's investment in subsidiary undertakings is reduced on the issue of share incentives as these are recharged to the subsidiaries.

Fair value is measured using methods appropriate to each of the different schemes as follows:

LTIS – EPS award	Market value on the date of grant
LTIS – TSR award	A Monte Carlo simulation to predict the total shareholder return performance
Sharesave	Black-Scholes
ESOS	Black-Scholes using an adjusted option life assumption to reflect the possibility of early exercise
SAS, SIP, DMSS, RSS, ESPP and DBP	Market value on the date of grant

Foreign currencies

Transactions in foreign currencies are translated at the rate of exchange ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated into pounds sterling at closing rates of exchange. Exchange differences on monetary assets and liabilities and transactions are taken to the Profit and Loss Account.

Tangible fixed assets

Tangible fixed assets are included in the Balance Sheet at cost, less accumulated depreciation and any provisions for impairment. Cost includes the original purchase price of the asset and the cost attributable to bringing it to its working condition for its intended use. Tangible fixed assets are depreciated on a straight-line basis at rates sufficient to write off the cost, less estimated residual values, of individual assets over their estimated useful lives of up to ten years.

Leases

Rentals under operating leases are charged to the Profit and Loss Account on a straight-line basis.

Investments

Fixed asset investments are held in the Balance Sheet at cost, less any provision for impairment as necessary. Current asset investments are stated at the lower of cost and net realisable value.

Pensions and other post-retirement benefits

The Company's employees participate in a number of the Group's defined benefit pension schemes as described in note 36 to the Group Financial Statements. The Company is unable to identify its share of the underlying assets and liabilities in the schemes on a consistent and reasonable basis and therefore accounts for the schemes as if they were defined contribution schemes. The charge to the Profit and Loss Account is equal to the contributions payable to the schemes in the accounting period. Details of the defined benefit schemes of the Group (accounted for in accordance with the Group's accounting policies detailed in note 2 to the Group Financial Statements) can be found in note 36 to the Group Financial Statements.

Taxation

Current tax, including UK corporation tax, is provided at amounts expected to be paid (or recovered) using the tax rates and laws that have been enacted or substantively enacted by the balance sheet date.

Deferred tax is recognised in respect of all timing differences that have originated, but not reversed, at the balance sheet date where transactions or events that result in an obligation to pay more tax in the future, or a right to pay less tax in the future, have occurred at the balance sheet date. Timing differences are differences between the Group's taxable profits and its results as stated in the Financial Statements that arise from the inclusion of gains and losses in tax assessments in periods different from those in which they are recognised in the Financial Statements.

A deferred tax asset is regarded as recoverable and therefore recognised only when, on the basis of all available evidence, it can be regarded as more likely than not that there will be suitable taxable profits in the foreseeable future from which the reversal of the underlying timing differences can be deducted.

I. Principal accounting policies of the Company continued

Deferred tax is measured at the average tax rates that are expected to apply in the periods in which the timing differences are expected to reverse, based on tax rates and laws that have been enacted or substantively enacted by the balance sheet date.

Deferred tax is measured on an undiscounted basis.

Financial instruments and borrowings

The Company's accounting policies for financial instruments and borrowings are consistent with those of the Group, and are disclosed in note 2 to the Group Financial Statements. The Company's financial risk management policies are consistent with those of the Group and are described in the Directors' Report – Governance on pages 46 to 48 and in note 4 to the Group Financial Statements.

The Company is exempted by FRS 29 from providing detailed disclosures in respect of its financial instruments because the Company is included within the Group's consolidated accounts and its financial instruments are incorporated into the disclosures in the notes to the Group Financial Statements.

II. Directors and employees

Details of Directors' remuneration, share-based payments and pension entitlements in the Remuneration Report on pages 58 to 63 form part of these Financial Statements. Details of employee share-based payments are given in note 35. Details of the remuneration of key management personnel are given in note 40.

III. Tangible assets

	2010	2009
	Plant, equipment and vehicles £m	Plant, equipment and vehicles £m
Cost		
1 January	**101**	84
Additions	**11**	19
Disposals	**(1)**	(2)
31 December	**111**	101
Accumulated depreciation		
1 January	**62**	49
Charge for the year	**12**	13
Disposals	**(1)**	–
31 December	**73**	62
Net book value		
31 December	**38**	39

IV. Investments in subsidiary undertakings

	2010	2009
	Investments in subsidiaries' shares £m	Investments in subsidiaries' shares £m
Cost		
1 January	**2,122**	2,091
Additions and disposals (i)	**10**	31
31 December	**2,132**	2,122

(i) Additions and disposals represent the net change in shares to be issued under employee share schemes in Group undertakings. Direct investments are held in Centrica Holdings Limited, Centrica Trading Limited and Centrica Beta Holdings Limited, all of which are incorporated in England. Principal undertakings are listed in note 43 on page 141. The Directors believe that the carrying value of the investments is supported by their underlying net assets.

V. Debtors

	2010			2009		
	Due within one year £m	**Due after more than one year £m**	**Total £m**	Due within one year £m	Due after more than one year £m	Total £m
Amounts owed by Group undertakings	**9,947**	**–**	**9,947**	9,729	–	9,729
Derivative financial instruments [(i)]	**5**	**151**	**156**	6	125	131
Other debtors	**6**	**–**	**6**	14	–	14
Prepayments and other accrued income	**14**	**11**	**25**	8	–	8
	9,972	**162**	**10,134**	9,757	125	9,882

(i) Derivative financial instruments comprise foreign currency derivatives held for trading of £36 million (2009: £37 million), interest rate derivatives held for trading of £3 million (2009: £3 million), interest rate derivatives held for hedging of £105 million (2009: £70 million) and foreign currency derivatives held for hedging of £12 million (2009: £21 million). The fair value of these derivatives is equivalent to the carrying value.

VI. Current asset investments

	2010 £m	2009 £m
Short-term investments	**266**	1,259

£52 million (2009: £48 million) of investments were held by the Law Debenture Trust, on behalf of the Company, as security in respect of the Centrica Unapproved Pension Scheme (refer to note 36 to the Group Financial Statements).

VII. Borrowings

	2010		2009	
Amounts falling due	**Within one year £m**	**After one year £m**	Within one year £m	After one year £m
Bank loans and overdrafts	**50**	**215**	53	374
Bonds	**–**	**3,407**	–	3,608
	50	**3,622**	53	3,982

The Company's financial instruments and related disclosures are included within the consolidated accounts of the Group. As permitted by FRS 29, Financial Instruments: Disclosures, further detailed disclosure in respect of the Company's financial instruments is not included. Disclosures in respect of the Group's borrowings are provided in note 26 to the Group Financial Statements.

VIII. Other creditors

	2010		2009	
	Due within one year £m	**Due after more than one year £m**	Due within one year £m	Due after more than one year £m
Trade creditors	**13**	**–**	17	–
Amounts owed to Group undertakings	**5,502**	**4**	4,839	4
Derivative financial instruments [(i)]	**27**	**65**	16	60
Taxation and social security	**4**	**–**	1	–
Accruals and deferred income	**60**	**–**	37	5
	5,606	**69**	4,910	69

(i) Derivative financial instruments comprise foreign currency derivatives held for trading of £76 million (2009: £61 million), interest rate derivatives held for trading of £16 million (2009: £5 million) and interest rate derivatives held for hedging of £nil (2009: £10 million). The fair value of these derivatives is equivalent to the carrying value.

IX. Provisions for liabilities

	1 January 2010 £m	Profit and loss charge £m	Utilised in the year £m	Reserves movements £m	**31 December 2010 £m**
Other provisions	8	1	(3)	–	**6**
Deferred tax	–	(1)	–	1	**–**
	8	–	(3)	1	**6**

Potential unrecognised deferred corporation tax assets amounted to £3 million (2009: £9 million), primarily relating to other timing differences.

Other provisions principally represent estimated liabilities for contractual settlements and National Insurance in respect of employee share scheme liabilities. The National Insurance provision was based on a share price of 331.60 pence at 31 December 2010 (2009: 281.10 pence). The majority of the amounts are expected to be utilised between 2011 and 2015.

X. Reserves

	Share premium £m	Capital redemption reserve £m	Profit and loss account £m	**Total £m**
1 January 2010	778	16	3,179	**3,973**
Loss for the year (i)	–	–	(361)	**(361)**
Losses on revaluation of cash flow hedges	–	–	(1)	**(1)**
Dividends	–	–	(668)	**(668)**
Employee share schemes:				
Increase in treasury shares	–	–	(20)	**(20)**
Value of services provided	–	–	48	**48**
Exercise of awards	–	–	(37)	**(37)**
Gains on revaluation of available-for-sale securities	–	–	4	**4**
Deferred tax on gains on revaluation of available-for-sale securities	–	–	(1)	**(1)**
Share issue	55	–	–	**55**
31 December 2010	833	16	2,143	**2,992**

(i) As permitted by section 408(3) of the Companies Act 2006, no profit and loss account is presented. The Company's loss for the year was £361 million (2009: loss of £132 million) before dividends paid of £668 million (2009: £635 million).

The Profit and loss account can be analysed further as follows:

	Cash flow hedging reserve £m	Treasury shares £m	Share-based payments reserve £m	Other £m	**Profit and loss account £m**
1 January 2010	2	(15)	74	3,118	**3,179**
Loss for the year (i)	–	–	–	(361)	**(361)**
Losses on revaluation of cash flow hedges	(1)	–	–	–	**(1)**
Dividends	–	–	–	(668)	**(668)**
Employee share schemes:					
Increase in treasury shares	–	(20)	–	–	**(20)**
Value of services provided	–	–	48	–	**48**
Exercise of awards	–	13	(44)	(6)	**(37)**
Gains on revaluation of available-for-sale securities (net of taxation)	–	–	–	3	**3**
31 December 2010	1	(22)	78	2,086	**2,143**

(i) Includes a £nil profit on re-measurement of interest rate derivatives and bonds designated in hedges (2009: £2 million) and a £6 million loss on re-measurement of foreign currency derivatives (2009: £137 million). Further details of the Company's interest rate and foreign currency derivatives are included within the financial instrument disclosures in notes 4, 22 and 23 to the Group Financial Statements.

XI. Movements in shareholders' funds

	2010 £m	2009 £m
1 January	**4,290**	5,007
Loss attributable to the Company	**(361)**	(132)
Loss on revaluation of cash flow hedges	**(1)**	(18)
Deferred tax on revaluation gains	**–**	6
Dividends paid to shareholders	**(668)**	(635)
Employee share schemes:		
Increase in treasury shares	**(20)**	(7)
Value of services provided	**48**	38
Exercise of awards	**(37)**	(24)
Gains on revaluation of available-for-sale securities (net of taxation)	**3**	4
Share issue	**56**	51
Net movement in shareholders' funds for the financial year	**(980)**	(717)
31 December	**3,310**	4,290

The Directors propose a final dividend of 10.46 pence per share (totalling £539 million) for the year ended 31 December 2010. The dividend will be submitted for formal approval at the Annual General Meeting to be held on 9 May 2011. These Financial Statements do not reflect this dividend payable, which will be accounted for in shareholders' equity as an appropriation of retained earnings in the year ending 31 December 2011.

Details of the Company's share capital are provided in the Group Statement of Changes in Equity and note 30 to the Group Financial Statements.

XII. Commitments

(a) Other commitments
At 31 December 2010, the Company had commitments of £162 million (2009: £151 million) relating to contracts with outsource service providers.

(b) Lease commitments
At 31 December 2010, lease commitments over land and buildings included non-cancellable operating lease payments due under one year of £1 million (2009: £nil), within one to five years of £1 million (2009: £1 million) and guaranteed operating commitments of a subsidiary undertaking of £7 million (2009: £7 million).

The Group's estimates of reserves of gas and liquids are reviewed as part of the half-year and full-year reporting process and updated accordingly. A number of factors affect the volumes of gas and liquids reserves, including the available reservoir data, commodity prices and future costs. Due to the inherent uncertainties and the limited nature of reservoir data, estimates of reserves are subject to change as additional information becomes available.

The Group discloses proven and probable gas and liquids reserves, representing the central estimate of future hydrocarbon recovery. Reserves for Centrica-operated fields are estimated by in-house technical teams composed of geoscientists and reservoir engineers. Reserves for non-operated fields are estimated by the operator, but are subject to internal review and challenge.

As part of the internal control process related to reserves estimation, an assessment of the reserves, including the application of the reserves definitions is undertaken by an independent technical auditor. An annual reserves assessment has been carried out by DeGoyler and MacNaughton for the Group's global reserves. Reserves are estimated in accordance with a formal policy and procedure standard.

The Group has estimated proven and probable gas and liquids reserves in Europe, North America and Trinidad and Tobago.

The principal fields in Europe and Trinidad and Tobago are South Morecambe, Chiswick, Cygnus, NCMA Poinsettia, Statfjord, Ensign and York fields associated with Upstream UK, and the Rough field associated with Storage UK. The European and Trinidad and Tobago reserves estimates are consistent with the guidelines and definitions of the Society of Petroleum Engineers, Society of Petroleum Evaluation Engineers and World Petroleum Council Petroleum Resources Management System using accepted principles.

The principal fields in North America are Foothills, Medicine Hat, Entice and Central Alberta located in the province of Alberta, Canada. The North American reserves estimates have been evaluated in accordance with the Canadian Oil and Gas Evaluation Handbook (COGEH) reserves definitions and are consistent with the guidelines and definitions of the Society of Petroleum Engineers and the World Petroleum Council.

Estimated net proven and probable reserves of gas (billion cubic feet)	Europe	North America	Trinidad and Tobago (iv)	**Total**
1 January 2010	2,018	377	–	**2,395**
Revisions of previous estimates (i)	9	(20)	–	**(11)**
Purchases of reserves in place (ii)	72	221	169	**462**
Extensions, discoveries and other additions (iii)	181	–	–	**181**
Production (v)	(254)	(40)	(8)	**(302)**
31 December 2010	**2,026**	**538**	**161**	**2,725**

Estimated net proven and probable reserves of liquids (million barrels)	Europe	North America	Trinidad and Tobago (iv)	**Total**
1 January 2010	58	5	5	**68**
Revisions of previous estimates (i)	1	–	–	**1**
Purchases of reserves in place (ii)	16	1	–	**17**
Extensions, discoveries and other additions	1	–	–	**1**
Production (v)	(12)	–	–	**(12)**
31 December 2010	**64**	**6**	**5**	**75**

(i) Includes minor reserves revisions to a number of fields in Europe and North America.
(ii) Reflects the acquisition of additional equity in the Statfjord field in Europe, Foothills properties in North America and Suncor Trinidad properties.
(iii) Recognition of reserves associated with the Cygnus, Chiswick and Rhyl fields.
(iv) The Trinidad and Tobago reserves are subject to a production sharing contract and accordingly have been stated on an entitlement basis (including tax barrels).
(v) Represents total gas and oil produced from the Group's reserves.

Liquids reserves include oil, condensate and natural gas liquids.

Results

Year ended 31 December	2006 (restated) (i), (iii) £m	2007 (restated) (i), (iii) £m	2008 (restated) (i), (ii), (iii) £m	2009 £m	**2010 £m**
Group revenue from continuing operations (i), (iii)	16,065	15,893	20,872	21,963	**22,423**
Operating profit from continuing operations before exceptional items and certain re-measurements:					
Downstream UK	284	840	712	1,011	**1,216**
Upstream UK	686	663	881	525	**771**
Storage UK	228	240	195	168	**169**
North America	173	187	215	153	**234**
Adjusted operating profit – operating profit before exceptional items, certain re-measurements and impact from fair value uplifts from Strategic Investments	1,371	1,930	2,003	1,857	**2,390**
Share of joint ventures' and associates' interest and taxation	(1)	(2)	(3)	(11)	**(78)**
Other	13	1	(8)	(5)	**–**
Depreciation of fair value uplifts to property, plant and equipment (iv)	–	–	–	(27)	**(118)**
	1,383	1,929	1,992	1,814	**2,194**
Operating profit/(loss) from discontinued operations:					
European operations (v)	9	20	(52)	105	**(2)**
The Consumers' Waterheater Income Fund (vi)	50	39	–	–	**–**
OneTel (vii)	(11)	–	–	–	**–**
Exceptional items and certain re-measurements after taxation	(862)	383	(1,048)	(288)	**726**
Profit/(loss) attributable to equity holders of the parent	(155)	1,505	(137)	844	**1,935**
	Pence	Pence	Pence	Pence	**Pence**
Earnings/(loss) per ordinary share (ii)	(3.8)	36.5	(3.3)	16.5	**37.6**
Adjusted earnings per ordinary share (ii), (viii), (ix)	17.3	27.2	21.7	21.7	**25.2**

Assets and liabilities At 31 December	2006 (restated) (ii) £m	2007 (restated) (ii), (x) £m	2008 (restated) (ii), (x) £m	2009 £m	**2010 £m**
Goodwill and other intangible assets	1,501	1,539	2,181	2,822	**3,454**
Other non-current assets	4,171	4,942	6,341	9,650	**9,815**
Net current assets/(liabilities)	(134)	747	2,163	330	**283**
Non-current liabilities	(3,918)	(3,868)	(6,313)	(8,675)	**(7,820)**
Net assets of disposal groups held for sale	–	–	–	128	**87**
Net assets	1,620	3,360	4,372	4,255	**5,819**
Debt, net of cash, cash equivalents and securities:					
Net debt (excluding non-recourse debt)	(1,527)	(795)	(511)	(3,136)	**(3,312)**
The Consumers' Waterheater Income Fund (non-recourse) debt	(483)	–	–	–	**–**
	(2,010)	(795)	(511)	(3,136)	**(3,312)**

Cash flows Year ended 31 December	2006 £m	2007 £m	2008 £m	2009 £m	**2010 £m**
Cash flow from operating activities before exceptional payments	850	2,447	371	2,850	**2,906**
Payments relating to exceptional charges	(113)	(90)	(74)	(203)	**(223)**
Net cash flow from investing activities	(720)	(964)	(1,122)	(4,520)	**(1,839)**
Cash flow before cash flow from financing activities	17	1,393	(825)	(1,873)	**844**

(i) Group revenue and cost of sales have been restated to report gas sales revenue of Centrica Storage net of cost of sales to better reflect the nature of the transactions.
(ii) Restated to capitalise borrowing costs on the adoption of IAS 23 (Amendment) and to reflect the change in British Gas Services Limited's revenue recognition policy.
(iii) Restated to present the European Energy segment, with the exception of the Group's operations in Germany, as a discontinued operation, as explained in note 38. The operating profit of the Group's operations in Germany is reported within the Upstream UK – Industrial and commercial segment. Also restated to present the operating profit of British Gas New Energy within Downstream UK – Residential energy supply and to include the operating profit of joint ventures and associates pre-interest and tax.
(iv) The depreciation of British Energy fair value uplifts is shown net of taxation.
(v) Discontinued in 2009.
(vi) Discontinued in 2007.
(vii) Discontinued in 2005.
(viii) Adjusted earnings per ordinary share excludes depreciation of fair value uplifts to property, plant and equipment from Strategic Investments after taxation and certain re-measurements and exceptional items.
(ix) Figures for 2006 through to 2007 have been adjusted to reflect the bonus element of a Rights Issue undertaken during 2008.
(x) Restated to classify the non-current portions of derivative financial instruments from current assets and liabilities to non-current assets and liabilities. 2006 has not been restated on this basis as it is considered impracticable to do so.

REGISTERED OFFICE OF THE ISSUER

Centrica plc
Millstream
Maidenhead Road
Windsor
Berkshire SL4 5GD
United Kingdom

JOINT BOOK-RUNNING MANAGERS

Barclays Capital Inc. 745 Seventh Avenue New York, New York 10019 United States of America	**BNP Paribas Securities Corp.** 787 Seventh Avenue New York, New York 10019 United States of America	**Citigroup Global Markets Inc.** 388 Greenwich Street New York, New York 10013 United States of America	**Deutsche Bank Securities Inc.** 60 Wall Street New York, New York 10005 United States of America
HSBC Securities (USA) Inc. 452 Fifth Avenue New York, NY 10018 United States of America	**J.P. Morgan Securities LLC** 383 Madison Avenue New York, New York 10179 United States of America	**RBS Securities Inc.** 600 Washington Blvd. Stamford, CT 06901 United States of America	**Société Générale** 29, boulevard Haussmann 75009 Paris France

LEGAL ADVISER TO THE ISSUER

as to US and English law

Linklaters LLP
One Silk Street
London EC2Y 8HQ
United Kingdom

LEGAL ADVISER TO THE JOINT BOOK-RUNNING MANAGERS

as to US law

Davis Polk & Wardwell London LLP
99 Gresham Street
London EC2V 7NG
United Kingdom

INDEPENDENT AUDITORS

PricewaterhouseCoopers LLP
1 Embankment Place
London WC2N 6RH
United Kingdom

FISCAL AND PAYING AGENT

Citibank, N.A., London Branch
Canada Square
Canary Wharf
London E14 5LB
United Kingdom

Merrill Corporation Ltd, London
13ZCP41901

Centrica plc

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