centrica

INTEGRATED ENERGY

Annual Report and Accounts 2012

INTEGRATED ENERGY IS WHAT WE DO.

It means constantly exploring new ways to source, procure and generate an affordable supply of energy.

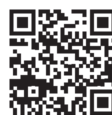
It means integrating innovation and technology into the home, giving our customers access to energy and services, whenever they need it.

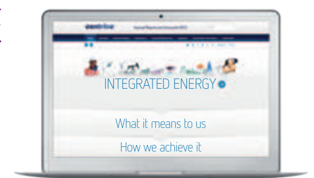
It means working with governments, regulators and partners to make the right things happen at the right time.

Most important of all, it means empowering our customers to take control of their energy needs as we work towards a low carbon future.

INTEGRATED ENERGY FROM CENTRICA.

ONLINE





Use your smartphone or tablet to scan this QR code for instant access to the Centrica Annual Report 2012 online

Introduction

You can find here a short summary of our business, providing an overview of the Annual Report together with the Group's financial performance.

2 Centrica at a Glance
4 Performance Highlights

Directors' Report – Business Review

We discuss here how we have delivered our vision and strategy in 2012 and take the opportunity to introduce the next step of our strategic direction.

5 Chairman's Statement
9 Chief Executive's Review
 9 Marketplace
 10 Our vision and strategic priorities
 12 Our business model
 14 Review of the year
18 Key Performance Indicators
20 Our Businesses
22 Operating Review
36 Group Financial Review
39 Corporate Responsibility Review
44 Principal Risks and Uncertainties

Directors' Report – Governance

Read here to find out about our standards of governance in relation to Board leadership and effectiveness, remuneration, accountability and relations with shareholders.

52 Corporate Governance Report
61 Remuneration Report
76 Independent Auditors' Report – Group

Financial Statements

Here you can understand the details behind our financial performance.

78 Group Financial Statements
82 Notes to the Financial Statements
135 Independent Auditors' Report – Company
136 Company Balance Sheet
137 Notes to the Company Financial Statements
143 Gas and Liquids Reserves
144 Five Year Record

Directors' Report – Appendix

This provides more detailed performance measures for the business units and corporate responsibility. The Directors' biographies and statutory Directors' Report disclosures are also included.

146 Performance Measures
152 Biographies of the Board of Directors and Senior Executives
154 Other Statutory Information

Shareholder Information

If you need help with managing your shareholding or you want to know more about our financial calendar and share register, then this information can be found here.

156 Financial Calendar
157 Shareholder Information
161 Glossary
163 Index

DELIVERING OUR VISION

Read about our strategic priorities on page **10**

OUR INTEGRATED BUSINESS MODEL

See how we deliver at every stage of the energy chain on page **12**

CENTRICA AT A GLANCE

The markets we operate in

The energy world is constantly evolving.

DOWNSTREAM

British Gas is the leading residential energy and services provider in Britain and Direct Energy is one of North America's largest energy and energy related services providers.

UPSTREAM

Centrica Energy has upstream gas and oil operations in the UK, Norway, the Netherlands, North America and Trinidad and Tobago. The Company also owns gas-fired power stations and has interests in nuclear and renewable generation in the UK. Centrica Storage operates more than 70% of the UK's total gas storage capacity. Securing our customers' energy needs, sustainably and affordably, is at the core of what we do.

Our strategic priorities

We have refreshed our strategy to ensure we deliver our vision.

INNOVATE to drive growth and service excellence

INTEGRATE our natural gas business, linked to our core markets

INCREASE our returns through efficiency and continued capital discipline

Our business model

A resilient, integrated business model is key to our success.

WE SOURCE IT

by finding and developing new gas reserves across the world.

WE GENERATE IT

through our fleet of gas-fired power stations and wind farms.

WE PROCESS IT

at our onshore gas terminals, making it safe for our customers to use.

WE STORE IT

at our Rough storage field, the largest gas storage facility in the UK.

WE TRADE IT

in the UK, North America and Europe to secure gas and power for our customers.

WE SUPPLY IT

to our residential and commercial customers in the UK and North America.

WE SERVICE IT

through our energy services and installation businesses.

WE SAVE IT

by offering a range of low carbon products and services to our customers.

Our vision is to be the leading integrated energy company with customers at our core

Measuring our progress

Our key performance indicators monitor our progress and keep our focus on delivery.

We monitor our performance by measuring and tracking key performance indicators (KPIs) that we believe are important to our longer-term success. Long-term sustainable performance of these KPIs is linked to the remuneration arrangements of our Executive Directors and senior executives.

FINANCIAL KPIs

- Adjusted operating profit
- Adjusted basic earnings per share
- Total shareholder return
- Dividends per share

NON-FINANCIAL KPIs

- Lost time injury frequency rate
- Process safety
- Customer trust
- Employee engagement

Responsibility

The impact our business activities have on society and the environment.

Our corporate responsibility ambition is to be the most trusted energy company. We need to be trusted by our customers, governments, regulators and investors by effectively managing our social and environmental impacts. In achieving a broad foundation of stakeholder trust, we can ensure long-term sustainable business success.

Go to centrica.com to see our responsibility process in more detail.

Our principal risks

To achieve our priorities, we need to be aware of the principal risks that affect our business.

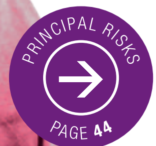
The risks we face in a rapidly changing energy landscape continue to evolve over time. A number of measures helped to mitigate those factors in 2012 while 2013 presents our organisation with more challenges. Robust governance and a clear risk strategy prepare us for any uncertainties ahead.

PRINCIPAL RISKS

- Health, safety, security and environment
- Brand and reputation
- Legislation and regulation
- Strategic growth
- Commodity costs
- Change management
- Information security
- People

KEY PERFORMANCE INDICATORS PAGE 18

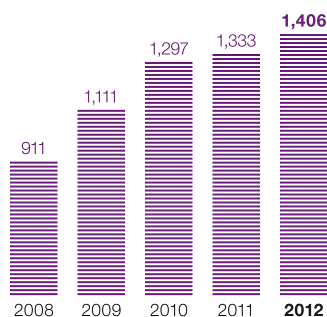
CORPORATE RESPONSIBILITY PAGE 39


PRINCIPAL RISKS PAGE 44

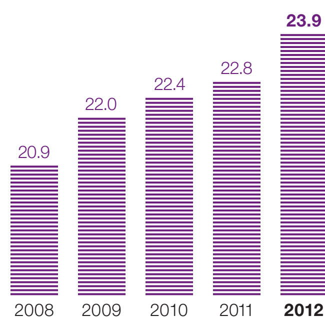
Introduction

PERFORMANCE HIGHLIGHTS

Adjusted earnings
£m

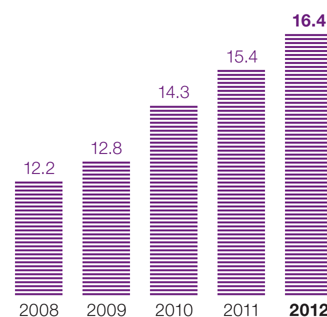


Group revenue‡
£bn



‡ From continuing operations

Dividend per share
pence



- Adjusted earnings up 5% to £1,406 million; 27.1 pence adjusted basic EPS
- Statutory earnings £1,273 million
- Cooler weather saw average domestic gas consumption increase by 12%
- Centrica Energy and Direct Energy benefiting from enhanced scale
- Adjusted Group tax charge of £1.1 billion
- Share repurchase of £500 million announced and full year dividend up 6%
- £2.7 billion invested in 2012

Financial highlights	**2012**	2011
Revenue from continuing operations	**£23.9bn**	£22.8bn
Total adjusted operating profit	**£2,743m**	£2,415m
Total adjusted taxation charge	**£1,110m**	£891m
Total adjusted effective tax rate	**44%**	40%
Adjusted earnings	**£1,406m**	£1,333m
Adjusted basic earnings per share (EPS)	**27.1p**	25.8p
Full-year dividend per share	**16.4p**	15.4p
Group capital and acquisition expenditure	**£2,727m**	£1,601m
Statutory results		
Operating profit from continuing operations	**£2,625m**	£1,414m
Profit from continuing operations before taxation	**£2,442m**	£1,268m
Earnings	**£1,273m**	£421m
Basic earnings per ordinary share	**24.6p**	8.2p

Earnings include £481m of exceptional charges relating to provisions for North American wind power purchase agreements, restructuring charges, an impairment relating to our decision not to proceed with nuclear new build and a restriction on the rate of tax relief on UK oil and gas decommissioning costs.

Unless otherwise stated, all references to operating profit or loss, taxation and earnings numbers throughout the report are adjusted figures, as reconciled to their statutory equivalents in the Group Financial Review on pages **36** to **38**

CHAIRMAN'S STATEMENT

Centrica is one of the UK's most important companies

Sir Roger Carr
Chairman

Our strategic vision is to be the leading integrated energy company, with customers at our core.

Review of the year

It is now three years since we defined our strategic objectives to build a more sustainable, vertically integrated, cost effective and customer focused business with meaningful geographic diversity. We were clear that to achieve this objective we would need to grow British Gas, acquire upstream assets on value creative terms and expand the scale of our North American activity.

I am pleased to confirm that in 2012 we demonstrated, through strong operational performance and acquisition, our considerable progress in achieving these strategic goals.

In the UK the year brought many challenges, with periods of colder weather compared to the very mild conditions of 2011 contributing to higher energy bills, and with material changes in the regulatory environment. The management team dealt with all of the turbulence with great professionalism and commitment.

British Gas took the lead in simplifying tariffs and implemented changes consistent with Ofgem's proposals for retail market reform. In parallel we continued to innovate with smart metering, to help consumers manage their energy usage, and to support customers with free insulation to reduce their consumption.

A relentless focus on cost management helped British Gas implement the lowest tariff increase of all the major energy suppliers, necessitated by higher wholesale energy costs, Government driven green energy costs and the imposition of additional infrastructure charges. Nevertheless, the very real concerns of hard pressed consumers, fuelled by external commentary, has impacted public trust in the industry and in British Gas as the nation's largest energy supplier in particular.

Centrica is one of the UK's most important companies, employing around 40,000 people, keeping homes warm and well lit, securing future energy supplies, innovating and investing and paying substantial amounts of tax to the Treasury each year. We also have over 700,000 individual shareholders, all of whom benefit from the dividends the Company pays. Through our larger shareholders, many of them pension funds, our dividends also feed into the retirement savings of millions of people. It is important therefore that the Group continues to grow and invest. The 5% increase in adjusted earnings we achieved in 2012 enabled us to invest more and to continue to grow our dividend in real terms. The importance of winning recognition for our contribution to the UK economy and building public trust continue to be priority items on our agenda.

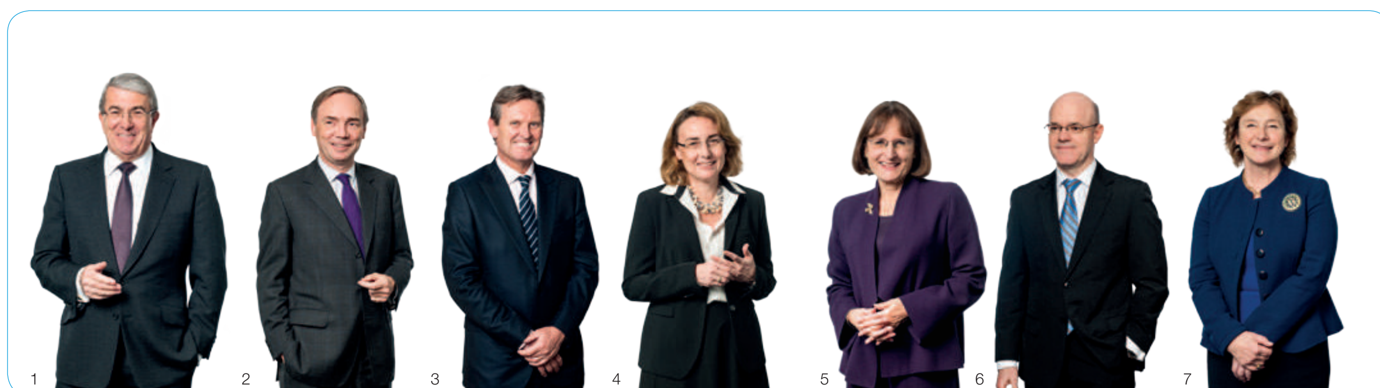
Upstream we invested around £2 billion in helping secure gas supplies for the UK. In parallel, we achieved first power from our Lincs offshore wind farm and worked with our partners in extending the life of our existing nuclear fleet. We took the decision not to participate in new nuclear construction with EDF due to higher anticipated costs and a lengthened construction schedule. This will enable us to return some of the capital we had raised for this purpose through a £500 million share repurchase programme.

In North America, a carefully executed strategy of operational efficiencies, organic growth and customer acquisition helped us to further expand our business – and we are well on the way to doubling profitability since 2009. With a change in the centre of gravity in our North American activities we moved the corporate headquarters from Toronto to Houston and our ambition to extend further our role in this market remains a strategic priority. The impact of shale gas in North America cannot be overstated and whilst its immediate effect has been to lower wholesale gas prices in the US market, there is no doubt it will influence global energy markets over time.

Our strategic vision is to be the leading integrated energy company, with customers at our core. The way in which we achieve this must reflect the changes in markets and sources of supply together with a constant assessment of costs and return for shareholders.

Directors' Report – Business Review
Directors' Report – Governance
Financial Statements
Directors' Report – Appendix
Shareholder Information

CHAIRMAN'S STATEMENT CONTINUED



Our aim in 2013 and beyond will be to focus on three strategic priorities – innovate to drive growth and service excellence, integrate our natural gas business linked to our core markets and increase our returns through efficiency and continued capital discipline.

We will achieve these goals by differentiating our UK business through our systems and innovation to provide a competitive edge and investing upstream for value, while maintaining our structural hedge. In North America we will grow our customer base and service business and seek to enhance our midstream and upstream position by acquisition when strategic fit and returns are attractive.

We believe that under the leadership of Sam Laidlaw we have developed a strong platform on which we can build a rewarding future for both customers and shareholders. This has been achieved with the considerable commitment of the management team and the skills and enthusiastic support of colleagues on both sides of the Atlantic.

The period ahead will bring new challenges. In order to ensure the organisation of our management team is appropriate for the task ahead, with effect from 1 July 2013 the Group will migrate from a regional structure to an international functional structure. Chris Weston will assume responsibility for downstream operations and Mark Hanafin will assume responsibility for upstream operations across the Group.

After a successful career spanning 12 years with Centrica, Phil Bentley will be stepping down from his role as Managing Director of British Gas, and Board member of Centrica, on 30 June 2013 and will leave the Company by 31 December 2013.

Phil Bentley has made a substantial contribution to the development of the business, initially as Finance Director and for the last six years as Managing Director of British Gas.

In his most recent role he has been instrumental in restructuring, reinvigorating and materially improving the performance of the business by raising customer service, lowering costs and increasing productivity. As Chairman, and on behalf of the Board, I thank him for all that he has achieved and wish him every success for the future.

I am confident that the bench strength we enjoy, the mindset we have, the new management structure and business model we have created will continue to deliver strong cashflows, enabling us to invest in customer service, supply security and shareholder reward.

Corporate culture

The Centrica business model is both wide ranging and complex, but its culture is simple and straightforward – professionalism, openness and transparency in the way we do things, together with integrity and honesty in how we do them.

An organisation is dependent upon its management and structure for the execution of strategy and its culture for the way in which its results are achieved.

Our Board members

1. Sir Roger Carr
Chairman

2. Sam Laidlaw
Chief Executive

3. Phil Bentley
Managing Director, British Gas

4. Margherita Della Valle
Non-Executive Director

5. Mary Francis CBE
Senior Independent Director

6. Mark Hanafin
Managing Director, Centrica Energy

7. Lesley Knox
Non-Executive Director

8. Nick Luff
Group Finance Director

9. Andrew Mackenzie
Non-Executive Director

10. Ian Meakins
Non-Executive Director

11. Paul Rayner
Non-Executive Director

12. Chris Weston
Managing Director, North America

Senior Executives

13. Grant Dawson
General Counsel & Company Secretary

14. Jill Shedden
Group Director, Human Resources

Business Review – Chairman's Statement

GOVERNANCE PAGE **52**
BIOGRAPHIES PAGE **154**

As a customer-facing business, respect for the individual, commitment to good service and adherence to the highest standards of behaviour in the customers' homes or place of work are at the heart of what we do. Our core values seek to ensure our people are welcome and trusted wherever they go.

We employ around 40,000 people working in many countries and different environments from offshore rigs, to onshore plants, in administrative locations, on the road, in office premises and in customers' homes. Caring for the welfare of our people wherever they are is our absolute priority.

In our health and safety policy no corners may be cut, nor costs trimmed, if it is at the expense of our people, customers, suppliers or contractors. This message is transmitted direct from the boardroom through management and reinforced in clear procedures, rigorous training and our incentive reward structure.

As a Board our focus is not simply on how much money the Company makes but how the Company makes money.

Corporate practice

In keeping with best practice, we oversee the Group worldwide through a unitary Board and six separate Committees – Audit, Nominations, Remuneration, Corporate Responsibility, Executive and Disclosure. Each Committee has agreed terms of reference and schedules a series of meetings throughout the year with disciplined agendas. Each Committee is professionally chaired and populated by an appropriate mix of Non-Executive and/or Executive Directors.

In addition to normal business, the work of the Committees is supported by training sessions on topics of particular relevance when Non-Executives require a more detailed understanding. Training is given by both members of the Centrica management team and external advisors.

The Corporate Responsibility Committee is also informed by an external advisory body of specialists in energy and consumer affairs who are able to give objective comment on policy, performance and governance standards of the Company from an outsider's perspective.

Each Committee reports to the Board after every meeting to ensure a comprehensive briefing is given to Board members on progress in all areas.

Board composition

The Board comprises myself as Non-Executive Chairman and eleven other Directors of which six are Non-Executive.

We have sought to ensure we have a balanced Board where individual merit and relevance are the key entry requirements but collectively we have an appropriate mix of gender, nationalities and skills to ensure constructive debate and thoughtful decision making. In addition, we believe it is important to maintain a blend within the Non-Executive group where some are in full time executive employment and others are pursuing a portfolio non-executive career path.

In addition to myself as Chairman, our current Non-Executives comprise one Australian, one Italian and four British nationals – three are women and three men, three in full time executive employment and three who have a number of non-executive roles in both public and private companies.

Our most recent appointments to the Board over the last 24 months have brought both current operational experience and fresh perspective, and reinvigorated the debate and discussion.

Diversity

Centrica is strongly committed to the merits of diversity in all its forms at Board level and throughout the Group.

Twenty five percent of the Board are women. As a founding Chairman of the 30% Club, I have long believed that the attainment of any role must be by merit, but that gender diversity can be an added value. Centrica is committed to maintaining its current level of women on the Board and would increase the percentage if the skills of the individual were appropriate and in keeping with the business need. This commitment is not a function of governance box-ticking but a belief that it is in the best interests of the business.

Our success in achieving a desirable mix at the Executive Committee level has been less successful with currently only one woman on a Committee of seven. We are working hard to address this issue through a variety of measures and I am confident we will increase the appointment of women in executive roles at the highest level.

Directors' Report – Business Review
Directors' Report – Governance
Financial Statements
Directors' Report – Appendix
Shareholder Information

CHAIRMAN'S STATEMENT CONTINUED

Our business principles

Our Group-wide business principles create a framework to help us make decisions in line with a consistent set of operating behaviours based on trust, integrity and openness.

1. **Demonstrating integrity in corporate conduct.**
2. **Ensuring openness and transparency.**
3. **Respecting human rights.**
4. **Enhancing customer experiences and business partnerships.**
5. **Valuing our people.**
6. **Focusing on health, safety and security.**
7. **Protecting the environment.**
8. **Investing in communities.**

Board composition planning

Over the last two years we have completed the first phase of refreshing the Board in keeping with the requirement for ensuring independence of mind and relevance of skills. Our last three appointments have included two with full time executive roles to bring relevant operational and financial experience to the Board and one with a broader non-executive skillset drawn from her experience in finance and as a non-executive and chairman of other boards. These appointments have assisted a generational change in Board membership and provided required replacement chairmanship skills in both remuneration and audit.

Following the announcement by BHP Billiton in February 2013 of the appointment of Andrew Mackenzie as CEO it is with regret that we have accepted Andrew's resignation as a Non-Executive Director of Centrica with effect from 10 May 2013. Andrew will not, therefore, seek re-election as a Director at the Annual General Meeting to be held on 13 May 2013.

In light of the increased content of upstream activity and our wider presence in North America, we have commenced a search for an additional Non-Executive with strong upstream credentials in North America. It is hoped that this appointment will be made in the first half of 2013.

Sadly two of our Non-Executives, Mary Francis and Paul Rayner, will complete their nine-year term of office in 2013. Both have made a material contribution to the Board and both will ultimately be a loss to the business. To preserve corporate memory and avoid undue disruption at one time, I intend to stagger their departure such that Paul Rayner remains on the Board to 31 December 2013 and Mary Francis continues in her capacity as Senior Independent Director during 2014. Whilst technically this exceeds their nine-year term, the Board has confirmed that they remain independent in character and judgement and I believe taking this approach to be in the best interests of the Company.

With these changes in mind, the role of Chairman of the Audit Committee, which has been undertaken by Paul Rayner, will be handed over to Margherita Della Valle at the time of the half year results in 2013. Mary Francis will remain Chairman of the Corporate Responsibility Committee for the duration of 2013.

A search will be initiated for the replacement of both Paul Rayner and Mary Francis in the second half of 2013 with a specification of skills and background to be determined in keeping with the demand of the business model at that time.

Board evaluation

Our policy over many years has been to conduct a thorough review of Board process, practice and culture on an annual basis with the input of an external facilitator at least once every three years.

At the end of 2011 we appointed Independent Board Evaluations (IBE) to conduct an external review and carefully considered their findings that they recommended to 'make a good board great'. The main observation was on the importance of allocating sufficient time for strategic discussion over the course of the year's Board meetings rather than concentrating our efforts at an annual offsite strategic review session. IBE also recommended sharing more detail of the individual Committee meetings at Board updates and encouraging all Executive Directors to participate more fully in Board discussion on areas outside their day to day responsibility.

In 2012 we adopted all of these recommendations to good effect, resulting in fuller participation by all Board members and a more regular review of the strategic development of the Group in a rapidly changing external environment. In December 2012, we conducted an internal Board evaluation comprising a written questionnaire followed by discussion in order to evaluate the success of the changes made and identify points to be addressed in the next twelve months. Based on the responses, all Directors concluded that there had been considerable improvement in both the quality and frequency of strategic discussion. All were now satisfied with the progress made and the contribution of all Board members. Looking forward, there were no issues on process or divisions on strategy.

Sir Roger Carr
Chairman
27 February 2013

CHIEF EXECUTIVE'S REVIEW: MARKETPLACE

World gas markets are evolving and we have to evolve with them

Sam Laidlaw
Chief Executive

Securing our customers' energy needs, sustainably and affordably, is at the core of what we do. But the energy world is changing. By 2020:

- almost three quarters of the UK's gas will be imported;
- more of the UK's electricity will be generated from capital intensive, low carbon technologies;
- every home in the UK will have a smart meter; and
- in the US, shale will provide well over a third of natural gas production, having already transformed the US energy market.

Our vision remains to be the leading integrated energy company, with customers at our core. We are refreshing our strategy to deliver that vision.

We will deploy our skills and capabilities so that we can benefit from the trends in our markets, growing and strengthening the business to fulfil our responsibilities to shareholders, customers and stakeholders.

IN MORE DETAIL

Refreshed strategic priorities to deliver our vision on page **10**

Business model built for the evolving energy world on page **12**

Review of the year on page **14**

OUR VISION AND STRATEGIC PRIORITIES

We have been working hard for the past three years to realise our strategic priorities

Strategy delivered over the last three years

GROW BRITISH GAS

Leading the transition to low carbon homes and business

- Stable profits and strong customer retention in the residential business and reduced customer churn
- Increased profitability in British Gas Services
- Clear leadership established in systems, online and smart

DELIVER VALUE FROM OUR GROWING UPSTREAM BUSINESS

Securing sustainable energy for our customers

- Significantly larger and more geographically diverse business
- Increased gas and oil reserves and production up by around 50%
- Strong nuclear performance with life extensions creating additional value

BUILD AN INTEGRATED NORTH AMERICAN BUSINESS

With leading positions in deregulated markets

- Increased scale in both upstream and downstream
- Improved return on capital in North American downstream
- Upstream resource trebled and production doubled

DRIVE SUPERIOR FINANCIAL RETURNS

Through operating performance and our unique investment choices

- Earnings per share growth of 25%
- Dividend per share growth of 28%
- Total shareholder return of 36% (FTSE 100: 21%)

We are now in a strong position to realise the next step of our strategic direction

Our refreshed strategic priorities

STAKEHOLDER MANAGEMENT

GOOD GOVERNANCE

INNOVATE to drive growth and service excellence

Leading integrated energy company with customers at our core

INTEGRATE our natural gas business, linked to our core markets

INCREASE our returns through efficiency and continued capital discipline

SUSTAINABILITY

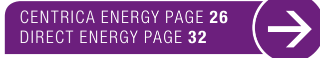
RISK MANAGEMENT

READ MORE ABOUT OUR NEW STRATEGIC PRIORITIES ON PAGES 16 TO 17

OUR BUSINESS MODEL: AN INTEGRATED ENERGY LANDSCAPE

The energy chain demonstrates how Centrica plays a major part in every aspect of energy from sourcing it to saving it. Each link in the energy chain is critical to our success and helps us to deliver our vision to be the leading integrated energy company, with customers at our core.

WE SOURCE AND GENERATE IT


CENTRICA ENERGY PAGE **26**
DIRECT ENERGY PAGE **32**

We invest in gas and oil reserves from the seas around the UK to secure vital long-term energy resources. We have natural gas assets in the UK, Norway, the Netherlands, North America and Trinidad and Tobago.

We generate power through our fleet of combined cycle gas turbine power stations, with eight stations in the UK and three plants in Texas. We also generate power through our equity interest in EDF Energy Nuclear Generation which operates eight UK nuclear power stations.

Our five UK onshore and offshore wind farms generate renewable power. Lincs offshore wind farm generated its first power in the second half of 2012 and in 2013 it will provide energy to more than 200,000 homes. In North America, we secure the electrical output from numerous Texan wind farms.

66.8mmboe

gas and liquids produced

28TWh

power generated

31 million

customer accounts

WE PROCESS, STORE AND TRADE IT

CENTRICA ENERGY PAGE 26
CENTRICA STORAGE PAGE 30
DIRECT ENERGY PAGE 32

With the UK increasingly dependent on imported gas, our storage capability helps ensure security of gas supply to homes and businesses. Our Rough storage facility is the largest in the UK, making up more than 70% of national storage capacity and meeting around 10% of peak day demand. We store gas at Rough for a large number of customers, including utilities, gas traders and gas producers.

Our UK onshore gas terminals ensure high quality gas enters the UK's transmission system. The Barrow terminals process gas from our Morecambe fields in the East Irish Sea while the terminal at Easington, in East Yorkshire, processes gas from the Rough storage facility and from early 2013, a newly constructed facility at Easington will process gas from the York field.

In the UK and North America, we trade gas and power to ensure British Gas and Direct Energy customers have a reliable and competitive energy supply. We have extended our presence to include liquefied natural gas (LNG) imports. Shipping LNG – where the gas is cooled to liquid form for ease of transport – now plays an important part in the way we secure the UK's energy needs.

WE SUPPLY, SERVICE AND SAVE IT

BRITISH GAS PAGE 22
DIRECT ENERGY PAGE 32

We supply energy to millions of homes and businesses in the UK and North America, and provide peace of mind with central heating, boiler and cooling maintenance and breakdown cover products.

By rolling out smart meter technology, we are ending the need for estimated bills, providing customers with accurate, real-time information on energy consumption and costs. We offer an increasing number of innovative low carbon, energy efficient products and services, including installing solar panels, insulation and ground and air source heating. We are also installing solar canopies to charge the first fully electric cars in the UK.

We save energy by helping customers to improve energy efficiency, offering free insulation and embracing new technologies – with smart meters playing a vital role as the enabling technology in the smart connected home. Our recently launched 'Remote Heating Control' product means customers can monitor and control their central heating systems from outside the home via the internet.

REVIEW OF THE YEAR

It is important that Centrica makes a fair and reasonable return so that we can continue to make our contribution to society and to invest. In 2012, we incurred a tax charge of over £1 billion and invested over £2 billion to secure new sources of energy for the UK, well in excess of our profits.

Strong performance in 2012 allows us to contribute our fair share

Centrica performed well in 2012 in a challenging environment, delivering year on year adjusted earnings growth of 5%. This reflects a combination of organic growth and enhanced scale from recent acquisitions and investments, in the UK, Norway and North America, as well as a continued focus on cost efficiency across the Group. As a result we have been able to grow the full-year dividend by more than the rate of inflation for the 13th year in succession, in addition to launching a £500 million share repurchase programme in early 2013.

Downstream at British Gas, we are facing increased costs in supplying energy, most of which are external to the Group. In this tough economic climate, we are committed to doing everything we can to help our customers. We have made sure that energy choices are simple and transparent, and we lead the way in standards of customer service, innovation, help for the vulnerable and energy efficiency. The weak economy continues to have an adverse impact on British Gas Business. However we were able to deliver strong double-digit profit growth in British Gas Services, largely through tight cost control coupled with continuing high standards of service.

Upstream at Centrica Energy, we continue to invest to secure energy supplies for the UK. We completed three acquisitions of gas and oil assets, delivering a step change in annual production and strengthening the geographic spread of our portfolio. In power, our Lincs offshore wind farm has generated first power and will be fully operational later in 2013. While market conditions remain challenging for gas-fired plants the nuclear fleet performed well, with increased output and seven year life extensions for Hinkley Point B and Hunterston B. In nuclear new build, while significant progress has been made, there remains uncertainty about overall project costs and the construction schedule. These factors, in particular the lengthening time frame for a return on the capital invested in a project of this scale, has led us to conclude that participation is not right for Centrica and in February 2013 we announced our decision not to participate.

In Centrica Storage, we delivered an increase in profit through strong operational and commercial performance. In North America, at Direct Energy we delivered further profit and customer growth in an environment of low gas prices and we have successfully integrated recent acquisitions into the business. We continue to see North America as an attractive market to deploy capital, both upstream and downstream, for growth and for value.

We remain on track to deliver our Group-wide £500 million cost reduction programme, sharpening the business and maintaining our competitive edge. At the same time we have retained our absolute focus on safety which continues to be a core priority across all our activities. Our downstream businesses have continued their significant reduction in accident rates. Upstream operations had no significant process safety events in 2012 and continue to implement their rigorous programme of process safety management systems. At a Group level we have developed a more comprehensive process to provide greater assurance of HSE compliance to the Board and Executive. This strong safety culture is reflected in our performance, with the lost time injury frequency rate (LTIFR) falling by 20%.

Overall, Centrica is delivering consistent earnings growth and it is this which allows us to make our fair contribution to the economy and society through investment, employment, tax payments and dividends.

Helping our customers in difficult times

Taking the lead in making energy choices simple and transparent

In February 2013, Ofgem announced that it was preparing for final proposals and a statutory consultation to be published around the end of March 2013 on its reforms

"WE HAVE TAKEN THE LEAD DURING 2012 IN HELPING MORE HOUSEHOLDS SAVE ENERGY AND SUPPORTING THE PEOPLE WHO NEED THE MOST HELP."

Sam Laidlaw
Chief Executive

to make the household energy market simpler, clearer and fairer for consumers. These follow on from initial findings published in March 2011 and updated proposals announced in October 2012. The headline proposals are a welcome step forward for the industry and will help to improve customer trust, engagement and understanding. However, it is important that these positive developments do not have the unintended consequence of restricting choice and innovation. We have already implemented a number of changes consistent with the headline proposals, including simplifying our tariff structures and publishing price comparison information to make it easy for customers to ensure they are on the most appropriate British Gas tariff for them.

Customer service, cost efficiency and innovation remain at the heart of everything we do. British Gas operating costs fell year on year, but not at the expense of service, as our Net Promoter Score (NPS) increased once again, to +30, and we were awarded the top five star rating for customer service from Consumer Focus. Our improved online platform handled 13% more transactions than in 2011, achieving a better customer experience and lower costs. Our new 'Remote Heating Control' product allows customers to monitor and control their energy use when they are away from the home, and we have now installed over 800,000 smart meters for homes and businesses – substantially more than any other UK energy supplier.

We also spend more than any other energy supplier on those who are most in need of support. In 2012, 400,000 of our most

HOW DO WE MEASURE UP AGAINST OUR PRIORITIES?

Our key performance indicators can be found on page **18**

vulnerable customers received the Warm Home Discount, now worth £130 off their annual bill. We are also at the forefront of measures to help people use less energy, installing insulation for nearly 700,000 customers during the year.

Despite the squeeze on household budgets, British Gas Services performed well. We improved retention rates across our product range demonstrating the value which customers place on our services. However, in current economic conditions it is difficult to attract new customers and we also saw a reduction in boiler installation volumes, down 10% from last year. The economic impact was seen more clearly in British Gas Business, leading to lower profitability and a reduction in the number of accounts served in a highly competitive market. We are therefore taking steps to put this business on a stronger footing for long-term growth, including introducing new systems to improve levels of customer service, at lower cost. Over time, we also expect to achieve growth in business services, particularly through Energy Performance Contracts.

Innovation in North America

In North America, greater competition has been welcomed by regulators and customers in our core markets, Texas and the US North East. Acquisitions and organic growth have increased the size of our business and we now have 3.5 million residential energy customer accounts and around 6 million residential energy and services accounts in total.

We continue to focus on providing attractive and innovative products to our residential and business customers, building on our Group-wide expertise in competitive markets. Our prepaid 'Power to Go' product in Texas continues to grow, while in the US North East the introduction of 'Free Power Saturdays' has encouraged customers to rephase their electricity use to off-peak times. We are specifically tailoring offers for small business customers while continuing to deliver high levels of service. Our energy services business gives us the ability to differentiate ourselves from our competitors with additional higher margin propositions.

In Ontario, restrictions on competition continue to make it difficult for us both to retain customers and attract new ones. We no longer view this business as core and are managing costs to continue serving our existing customers as efficiently as possible.

Securing sustainable and affordable energy supplies

The Group invested £2.7 billion of capital in 2012, helping to secure supplies for the UK. Around £2 billion of that was invested in North Sea gas and oil assets, including the completion of three acquisitions. This materially increased the scale and

REVIEW OF THE YEAR CONTINUED

geographic diversity of the business and Norway is now a core part of our portfolio, with a number of attractive producing, development and exploration assets. Over the past three years we have developed significant capabilities in upstream and midstream, leaving us well placed for future growth.

We achieved first gas from our Ensign, Seven Seas and Atla development projects during the year, with first gas expected from York and Rhyl in the coming weeks. In early 2013, we had positive results from exploration drilling at Rodriquez and Whitehaven. However we recorded a lower level of drilling success in 2012 than in previous years, including a development well failure at Ensign which resulted in a pre-tax write-off of £73 million. Construction has now begun at the £1.4 billion Cygnus project. Cygnus is the largest gas discovery in the Southern North Sea in the last 25 years and will create 4,000 jobs during the construction phase, predominantly in the UK. At peak production it will be able to meet the demand of nearly 1.5 million UK homes.

We achieved first power from our 270MW Lincs offshore wind farm in the year. When fully operational by the second half of 2013 it will be able to meet the annual demand of more than 200,000 homes. We were also granted planning consent for 580MW at the Race Bank offshore wind farm project. We are willing to commit £200 million for the project, and are in discussion with a financial partner and the Government concerning the economic framework. Investment in the existing nuclear fleet is ongoing, with the expectation for nuclear plant life extensions for the AGR fleet now seven years on average, compared to the five previously assumed. In gas-fired generation we have recently sanctioned a turbine blade upgrade at our 1.2GW South Humber power station. We also have strong capabilities in gas storage, and two potentially attractive projects, Baird and Caythorpe. However the market remains challenging for new gas storage projects and we will only invest if the returns are appropriate for the level of risk undertaken.

However, as with all our investment options, we will only deploy capital where

SOURCING AND PROCURING THE RIGHT ENERGY AT THE RIGHT PRICE

Read about Centrica Energy's activities on page **26**

we see attractive value, aligned to our core competencies. In this context, we announced in October that we would not proceed with plans to build two dedicated biomass plants, following recent clarification on the regulatory framework indicating a Government preference for coal conversion. Earlier this month, we also announced that we would not participate in the construction of up to four new nuclear reactors in the UK. While we believe that nuclear power has an important role to play in the UK's energy mix, the likely cost and timescale of this project led us to conclude that it was not in the best interests of Centrica shareholders for us to participate.

New strategic priorities to reflect changing market conditions

World gas markets are evolving and we have to evolve with them. Shale gas in North America and LNG globally have transformed the landscape. Gas will continue to play a major role in the UK, both in heating the overwhelming majority of homes and businesses and as part of a diverse fuel mix for power generation, with the UK Government's Electricity Market Reform and Gas Strategy both indicating a long-term role for gas-fired generation. However, the sources of UK gas are changing, with North Sea reserves declining and becoming more expensive to develop. This places more reliance on imported pipeline gas and particularly LNG, and leaves the UK increasingly exposed to global gas prices.

At the same time, the nature of low carbon power investments in the UK is changing, with affordability for consumers increasingly the focus of attention. Projects are becoming larger in scale, with higher capital costs and longer construction times, while the fixed price nature of the Contract for Difference mechanism means that output will no longer act as a hedge against downstream price volatility.

Against this backdrop, our vision is to be the leading integrated energy company, with customers at our core. We have refreshed our strategic priorities to position Centrica to best advantage in this demanding but exciting new world:

- Innovate to drive growth and service excellence
  - Lead with great service and efficient operations
  - Enable our customers to control their energy use in a simpler, smarter, more efficient way
  - Grow in selected markets, building on our leading capabilities
- Integrate our natural gas business, linked to our core markets
  - Grow and diversify our exploration and production portfolio for value
  - Develop our midstream business to integrate along the gas value chain
  - Maintain a low carbon power hedge and invest where we see value
- Increase our returns through efficiency and continued capital discipline
  - Further develop organisational capability
  - Continuously focus on safety
  - Deliver value to shareholders

These strategic priorities apply across our businesses in the UK, North America and internationally. In order to reinforce delivery of the priorities we are moving to an

Business Review – Chief Executive's Review

international functional organisation with a new management structure, aligned to our core competencies downstream and upstream. And we will do all this with the clear objective of increasing our returns, through efficiency and continued capital discipline. Chris Weston will lead the international downstream business, as we build on our distinctive capabilities in service, systems, energy services and efficiency, in the UK and North America. Mark Hanafin will lead the international upstream business as we continue to develop opportunities along the gas value chain and invest where we see attractive value. Both Chris and Mark have extensive experience in the UK and North America, and are therefore well placed to take on the task ahead.

Innovate to drive growth and service excellence

Underlying household energy consumption in the UK will continue to fall as appliances and homes become more efficient. However with the UK increasingly exposed to global gas prices, and non-commodity costs expected to rise year on year, affordability will remain an important issue. By contrast, the low gas price environment in North America makes affordability less of an issue, and favourable market conditions in the United States offer a good opportunity for growth. On both sides of the Atlantic, the roll-out of smart meters will give customers a new level of control over their energy use and we need to be innovative in the way we help them meet their evolving energy needs.

In the UK, we have developed a leading online platform and leading customer systems. We will also take advantage of our strong positions in energy services and smart meters to develop exciting new propositions, with offerings increasingly tailored to the needs of individual customers. Through relentless focus on service excellence, innovation and cost efficiency, we aim to maintain stable margins in residential energy supply, and target continued expansion in residential services. In business energy we have laid the groundwork for future growth, although in the near term market conditions remain challenging.

In North America too, service, innovation and cost efficiency will remain a core focus. But the continued liberalisation of markets in the United States, and the undeveloped nature of energy services provision, offer an opportunity to grow our customer base, both organically and through acquisition. We will continue to evaluate both bolt-on and larger acquisitions but remain focused on returns and will only transact where we see value. We will use our UK expertise and experience to develop our protection plan offerings in North America and we will increase the level of energy and services bundling over time. Over the next three to five years we are targeting a doubling of profitability in the North America downstream business, through a combination of organic growth and acquisitions, with Direct Energy downstream becoming a more material part of the Group.

Integrate our natural gas business, linked to our core markets

In an increasingly global market, we must secure gas from a wider range of sources and will consider at which stages of the supply chain we can add value, expanding the scope of our activities where appropriate. The aim is to connect sources of energy to our customers, building an integrated international business focused on the Atlantic basin.

The UK and Norway will remain an important part of our upstream investment and activity, as we look to maintain an appropriate energy hedge. We will invest in assets with a link to existing hubs while looking to divest non-core assets. However, with the development of North Sea fields becoming increasingly expensive, particularly in the UK, we will refresh our focus on value. In North America we will consider both conventional and unconventional assets, and there is also potential for gas exports later in the decade. Overall, we will invest where we see value across our international portfolio, delivering annual production in the range 75mmboe to 100mmboe. In addition, we will look to build on our existing midstream capabilities and positions along the gas value chain, focusing on asset optimisation and gas contracting with an emerging LNG presence, provided we can do so in a capital efficient manner.

Our focus in UK power generation will be to preserve our existing power hedge, investing where we have a competitive advantage and see attractive returns. We retain a number of offshore wind opportunities, at Race Bank and in the Irish Sea. However, we will only invest for value and will seek to reduce our equity ownership through partnering where appropriate. We also retain options to build new CCGTs. However spark spreads remain at historically low levels and much will depend on the final outcome of Electricity Market Reform and the implementation of a capacity market in the UK.

Increase our returns through efficiency and continued capital discipline

In 2013, Centrica faces new challenges, including the loss of free carbon allowances. But we will continue to benefit from our cost reduction programme, from organic growth and also from the full-year impact of acquisitions, both upstream in gas and oil production and in North America. In this context, it is vital that we continue to focus on operational efficiency, reducing costs wherever possible for the benefit of customers and shareholders. All this must be done without in any way compromising our strong focus on health and safety.

Centrica has a robust balance sheet and generates strong cash flows and we retain a number of investment opportunities across the Group. This combination, allied to our expertise and experience both upstream and downstream, defines Centrica's core capabilities. However, we will maintain capital discipline, as evidenced by our recently announced £500 million share repurchase programme, only investing where we see value. Our aim now is to use those strengths to innovate and grow while adapting to a rapidly evolving energy world, serving our customers and delivering value to shareholders.

Sam Laidlaw
Chief Executive
27 February 2013

KEY PERFORMANCE INDICATORS

We monitor our performance by measuring and tracking key performance indicators (KPIs) that we believe are important to our longer-term success. Long-term sustainable performance of these KPIs is linked to the remuneration arrangements of our Executive Directors and senior executives.

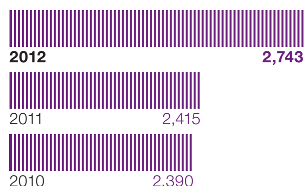
FINANCIAL

Adjusted operating profit

Operating profit is our key measure for financial performance. For remuneration purposes, operating profit is adjusted to a post-tax basis and by a charge on capital to set the economic profit performance targets.

Target for 2013
To continue to drive towards our three-year economic profit target range of £2.6 billion to £3.4 billion.

Adjusted operating profit £m



£2,743m

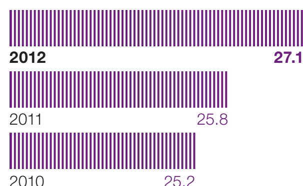
Adjusted operating profit
2011: £2,415m

Adjusted basic earnings per share (EPS)

EPS is an industry standard determining corporate profitability for shareholders. EPS is adjusted to reflect better the performance of the business. 2012 saw growth in our EPS despite the challenging economic conditions during the year.

Target for 2013
To deliver real growth in adjusted EPS over successive three-year periods.

Adjusted basic earnings per share pence



27.1p

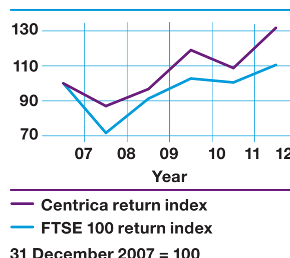
EPS
2011: 25.8p

Total shareholder return (TSR)

The Board believes that TSR is a valuable KPI to assess the Company's performance in the delivery of shareholder value. Centrica has outperformed the FTSE 100 Index by 19% over the previous five years.

Target for 2013
To deliver improved levels of relative TSR as a measure of performance over a sustained period.

Total shareholder return indices (unaudited)



19%

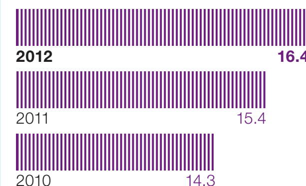
TSR outperformance over five years
2011: 5%

Dividend per share

Dividend per share indicates the level of earnings distributed to Centrica shareholders. The 2012 dividend shows an increase of 6% on the 2011 dividend.

Target for 2013
To deliver real growth each year. Dividends paid contribute to relative TSR.

Ordinary dividend pence



16.4p

Total dividend
2011: 15.4p

Unless otherwise stated, all references to operating profit or loss, taxation and earnings numbers throughout the report are adjusted figures, as reconciled to their statutory equivalents in the Group Financial Review on pages 36 to 38

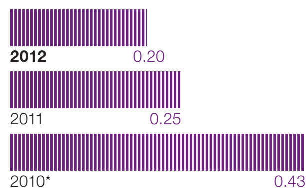
NON-FINANCIAL

Lost time injury frequency rate (LTIFR)

Safety is one of our core priorities. We continue to raise our standards of performance through strong leadership and on-going programmes to raise awareness and reinforce a positive and proactive safety culture across all our businesses. Initiatives across the Group in 2012 led to a 20% reduction in our LTIFR per 100,000 hours worked.

Target for 2013
To continue to pursue a best practice safety culture and to at least maintain, and if possible further improve, our LTIFR.

LTIFR per 100,000 hours worked



* 2010 figure does not include third-party managed contractors and is not directly comparable to 2011 and 2012 data.

0.20

LTIFR
2011: 0.25

Process safety

We have introduced a separate process safety measure which focuses on the integrity of operating systems and processes that handle hazardous substances and therefore emphasises the importance of a positive safety culture.

There were no significant process safety events in 2012.

Target for 2013
To continue to develop process safety strategies and training and to improve performance on all process safety metrics.

0

Significant events
2011: 2

Customer trust

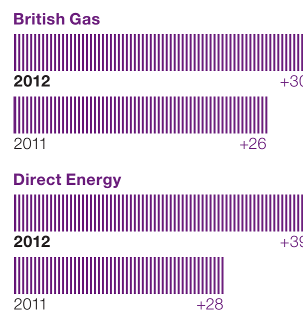
We track our performance using net promoter scores (NPS) for our two customer-facing businesses: British Gas in the UK and Direct Energy in North America.

From 2012 we have introduced low, median and high performance ranges for NPS.

British Gas NPS improved in 2012 with an annual average score of +30, despite higher call volumes as a result of colder weather. Direct Energy NPS rose to +39. Both results were within the high performance range.

Target for 2013
To remain within the high performance range.

Net promoter scores



Employee engagement

We use a Group-wide employee survey to measure engagement and to receive feedback on how we can create a positive and challenging environment. We did not conduct a survey in 2011 but undertook a review on how we measure employee engagement and how to use it as a tool to drive business performance. The survey in 2012 resulted in a mean score of 4.72 out of 6.

Target for 2013
To continue to strive towards top quartile performance measured against an identified high performance benchmark range.

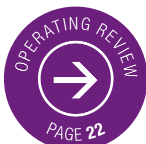
4.72 out of 6

Employee engagement
2011: not applicable

OUR BUSINESSES

£13,716m

Revenue (2011: £12,315m)



£1,093m

Adjusted operating profit (2011: £1,005m)

British Gas is Britain's leading residential energy and services provider. Our energy business supplies gas and electricity to millions of homes and businesses in Britain, winning awards for high quality customer service and innovation.

British Gas' services business installs, repairs and maintains boilers and heating systems. Our engineers also service electrical systems, appliances, plumbing and drains. We help our business customers reduce their energy consumption and cut costs, with a range of value-added services.

British Gas is committed to an energy efficient future – whether it's cutting consumption with insulation measures or the latest advances in solar panels and electric vehicles. We offer our customers the most up-to-date technology – including smart meters and automated heating and security systems. We bring innovative home improvement projects to local communities. By focusing on our customers' needs, British Gas keeps homes and businesses across Britain warm and working.

5 star

Customer service rating from Consumer Focus

25 million

Customer accounts

30,305

Employees

£4,321m

Revenue (2011: £4,459m)

£1,230m

Adjusted operating profit (2011: £1,023m)

Centrica Energy is an international business delivering growth and shareholder value through a balanced mix of gas and oil production, power generation and energy trading.

Our upstream oil and gas business operates in the UK, the Irish Sea, the Norwegian and Dutch sectors of the North Sea, as well as in Trinidad and Tobago. In 2012, we added 170mmboe to our reserves.

Our power generation business has a fleet of gas-fired power stations, offshore wind farms and a 20% share in the power generated by EDF Energy's UK nuclear power plants.

Our midstream business operates in the UK and European energy markets, trading in energy produced both inside and outside the business. It also supplies British Gas with electricity and gas.

21,489GWh

Power generated

56.7mmboe

Gas and liquids produced

1,788

Employees

£164m

Revenue (2011: £164m)

£89m

Adjusted operating profit (2011: £75m)

Centrica Storage operates the Rough offshore gas storage facility in the Southern North Sea and the associated Easington Terminal.

The business stores gas in the Rough field on behalf of a number of customers, including utilities, gas traders, gas producers and other Centrica businesses. Gas is taken from the National Transmission System at Easington, piped offshore and is injected into a subsea reservoir, to be delivered back when it is required to meet seasonal peak demands.

Our Rough storage facility is the largest in the UK, able to meet approximately 10% of the UK's current peak day demand and representing over 70% of UK storage capacity.

Recent major works at Easington will allow us to process gas from Centrica's York project and, potentially, from other third parties in the future.

70%

We own over 70% of the UK's gas storage capacity

0

Lost time incidents in three years

306

Employees

£5,741m

Revenue (2011: £5,886m)

£331m

Adjusted operating profit (2011: £312m)

Direct Energy is one of North America's largest energy and energy related services providers. We provide choice and support in managing energy use and costs through our portfolio of innovative products and services. We operate under four lines of business.

Direct Energy Residential offers a wide range of fixed and variable natural gas and electricity pricing plans in addition to time-of-use and prepaid products using smart meter technologies.

Direct Energy Business provides natural gas and electricity sales as well as energy efficiency management and services.

Direct Energy Upstream manages natural gas production, power generation, midstream gas storage and transportation across North America.

Direct Energy Services is North America's largest provider of heating and cooling, plumbing and electrical services.

6 million

Customer accounts

10.1mmboe

Gas and liquids produced

6,336GWh

Power generated

6,243

Employees

BRITISH GAS

" WE CONTINUE TO LEAD THE INDUSTRY IN SMART METERING, ENERGY EFFICIENCY, HELP FOR THE VULNERABLE AND IN ENSURING THAT OUR ENERGY PROPOSITION IS SIMPLE, FAIR AND TRANSPARENT. "

Phil Bentley
Managing Director, British Gas

2012 was an important year for British Gas – our 200th anniversary. In 1812, our founding company brought gas lighting to London's streets for the first time.

In 2012, we are still innovating. Today's technology looks very different but our principles of service excellence for our customers are the same – that's why we look after millions of homes in Britain.

One new innovation is smart meters. The British Gas roll-out programme is bringing significant benefits to customers. Smart meters bring with them ground-breaking new products and services – energy efficiency reports, time-of-use tariffs and itemised billing.

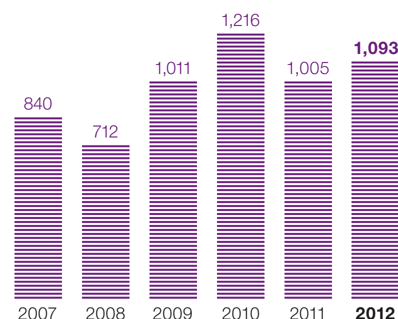
New technology reaches its full potential only with an unrelenting commitment to service excellence. British Gas continues to lead the industry in service – whether it's our award winning online presence and smartphone applications, downloaded more than 650,000 times, or our unique 'Model Visit' and 'Model Call'. British Gas established a Customer Board in 2011 which continues to play a role in ensuring we put customers at the heart of everything we do. By putting the customer front and centre we are growing existing sales channels and opening new ones.

British Gas is evolving from a supplier of electricity and gas to a provider of complete energy products and services. From remote heating controls to revolutionary energy efficiency services for business customers, we're making the connected home and connected business a reality, adding significant value to our business.

We have seen positive growth in our residential energy and services divisions. Although we face higher external costs – wholesale commodity, transportation and environmental – we have minimised the impact through the careful management of our own costs. We are leading the industry in energy efficiency measures and advice, helping our customers to reduce consumption.

For 200 years we have brought innovation to Britain's energy industry. We are delivering the profits that enable investments in alternative forms of energy and new gas fields to keep homes and businesses warm and well lit. We will continue to do so, making a successful British Gas good news for Britain.

Adjusted operating profit‡
£m



For the year ended 31 December	2012	2011
Adjusted operating profit‡ (£m)		
Residential energy supply	**606**	544
Residential services	**312**	269
Business energy supply and services	**175**	192
Customer numbers (year end, '000)		
Residential energy customer accounts	**15,656**	15,881
Residential services product holdings	**8,402**	8,484
Business energy supply points	**924**	999

‡ From continuing operations

Good performance against a challenging economic backdrop

British Gas performed well in 2012, in a weak economy and with continuing increases to the cost of supplying energy. This is having a real impact for both residential and business customers and, against this backdrop, it is important that we continue to focus on improving customer service and reducing costs. We also continue to lead the industry in smart metering, energy efficiency, help for the vulnerable, and in ensuring that our energy proposition is simple, fair and transparent.

In residential energy supply, we delivered margins in line with our through-cycle expectations, in a period where all suppliers were faced with higher wholesale gas prices and higher non-commodity costs, including the cost of upgrading the UK's gas and electricity grids and meeting carbon reduction targets. Weather conditions were cooler than usual, following unusually mild temperatures in 2011. Average gas consumption was therefore higher compared to the prior year, partially offset by efficiency measures taken by our customers, including the take-up of our free insulation offers and the installation of more efficient central heating systems. As a result of higher consumption and costs, the average gas and electricity bill increased year on year and was made up as follows:

For a 2012 average annual gas and electricity bill of £1,188* the costs are:

External	
Wholesale energy	£568
Delivery to customer	£283
Environmental and social policies	£112
Taxes	£72
Internal	
Operating costs	£104
Profit	£49

* Based on British Gas 2012 financial results and consumption and is an average of all payment types/tariffs/regions.

In residential services, we again delivered double digit profit growth despite the challenging economic climate, primarily driven by cost efficiencies, while continued high service levels resulted in strong customer retention. The weak economy and competitive pressures continue to have an adverse impact on our business energy supply division, and we are investing in back office systems to reduce cost and enhance customer service.

The health and safety of our employees and customers remains a core priority. Our lost time injury frequency rate (LTIFR) was 0.23 per 100,000 hours worked (2011: 0.29), a 21% reduction over the past year. We are also focused on maintaining high levels of employee engagement and recognising the commitment our people make to delivering excellent customer service. This was reflected in British Gas being nominated in The Sunday Times 'Best Big Companies to Work For' for the fourth year in a row.

Helping our customers in difficult times

In February 2013, Ofgem announced that it was preparing for final proposals and a statutory consultation to be published around the end of March 2013 on its reforms to make the household energy market simpler, clearer and fairer for consumers. These follow on from initial findings published in March 2011 and updated proposals announced in October 2012. The headline proposals are a welcome step forward for the industry. However, it is important that the proposals on product range, restricting each supplier to four tariff types, do not restrict customer choice or market innovation. British Gas has already implemented changes consistent with many of the headline proposals. We have simplified our tariffs, including a new standing charge and single rate structure as part of a commitment to phase out two-tier tariffs. We have also been publishing price comparison information on our annual statements since March, allowing customers to check whether they are on the most appropriate British Gas tariff, while we were awarded five stars by Which? in July for clarity of billing and account management. More recently, we have built the capability to provide a personalised price comparison on each customer's bill, based on their actual consumption.

We continued to deliver high levels of customer service in 2012. In residential energy, our average call answering and handling times were lower than in 2011 while the volume of calls received fell and in October, Consumer Focus awarded us their top 5 star customer service rating. In residential services, our customer service metrics remained strong, despite higher call volumes as a result of the colder weather. Meanwhile complaints fell, and customer churn was at its lowest ever level. The overall British Gas Net Promoter Score (NPS) increased from +26 to +30.

AROUND 15,000 OF OUR CUSTOMERS ARE NOW USING 'REMOTE HEATING CONTROL'

During the year we launched our award winning 'Remote Heating Control' product which allows customers to monitor and control their central heating system via the internet or a smart phone. For our smart meter customers, we also launched the 'Smart Energy Report' to provide visibility of how their energy is being used and to help them reduce their consumption.

BRITISH GAS CONTINUED

HOW DID WE MEASURE UP?
BRITISH GAS PERFORMANCE MEASURES CAN BE FOUND ON PAGES **146** AND **147**

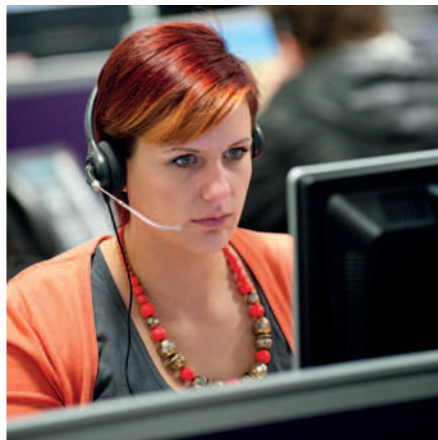
During 2012 we further developed our online platform. We now have 3.4 million online registered customers, a 20% increase since last year, and over a third of all energy bills are now sent electronically. Seven out of ten customer own meter reads are submitted online and we have over one million accounts on EnergySmart which helps customers monitor and manage their energy usage. We have launched leading applications for both Apple and Android smart phones and have seen more than 650,000 downloads to date. Around a quarter of all website contacts are now made through mobile devices.

We continue to help our most vulnerable customers and maintain the widest eligibility criteria among all energy suppliers for the Warm Home Discount, which helped 400,000 customers during the year. In October, we announced 'Better Homes for Britain', a five year partnership with Shelter to help one million British households living in private rental property improve the standard of their homes. We also lead the industry in energy efficiency. Since 2008, British Gas has installed 1.7 million insulation measures to homes across the UK through the CERT and CESP programmes. Under these schemes, British Gas was required to meet a variety of carbon emissions reduction targets by 31 December 2012. Overall we expect to fulfil our total carbon saving targets in the first quarter of 2013, although finding customers who qualify as being in the 'Super Priority Group' has proved challenging and this particular sub-target will not be fully met. However, Ofgem has indicated that mitigating actions undertaken after 31 December will also be taken into account when assessing delivery.

Customer accounts stabilised despite competitive market conditions

A slight fall in wholesale electricity prices at the end of 2011 allowed us to implement a 5% reduction in our standard domestic electricity tariff in January, re-establishing British Gas as the cheapest major electricity supplier on average in Britain. However, like the rest of the industry, we are facing higher external costs. Wholesale gas prices are 13% higher for winter 2012/13 than for winter 2011/12, while the cost of upgrading the UK's gas and electricity grids and meeting carbon reduction targets increased by £50 per customer in 2012. As a result, in October we announced a rise in domestic gas and electricity prices by an average of 6%, which was implemented in November.

The number of residential energy customer accounts on supply reduced by 1% during the year, to 15.7 million (2011: 15.9 million). This reflected a short term increase in customer churn following the implementation of the price rise, although churn of 9% over the year was at its lowest ever level reflecting good customer service.



Our competitive pricing position has now improved following the implementation of price rises by all major suppliers and we have seen a return to growth in the early weeks of 2013. We have 5 million customers enrolled in the Nectar loyalty programme, which reduces our cost to serve and improves the customer experience by incentivising the use of our online platform, including the submission of meter reads and payment by direct debit.

The number of residential services product holdings fell slightly to 8.4 million (2011: 8.5 million), with weak economic conditions making sales of new contracts challenging. Retention rates improved however, with strong levels of customer service supporting attractive customer propositions. We decided in the second half of the year to strengthen our Plumbing and Drains product by expanding the cover to include the water supply pipe. As a result we are no longer selling a separate water supply pipe product and our product holdings have been restated accordingly. The economic environment continued to impact boiler installation volumes, which fell 10% to 94,000 (2011: 105,000), although operating profit increased as we focused on reducing our cost base. We continue to develop new affinity relationships to enable us to offer energy and services products to a wider customer base. In July, we signed a broad strategic partnership with the RAC covering a number of areas, including roadside breakdown, joint procurement and affinity marketing, and the first sales were made in November. In electric vehicles, we are the preferred supplier of home charging solutions for five major car manufacturers.

The number of business energy supply points fell by 8% over the year, to 924,000 (2011: 999,000) due to the challenging economic and competitive environment which is putting pressure on contract renewal rates and margins. However, we have recently received the letter of intent to award the renewal of a significant electricity contract from the Government Procurement Service comprising 70,000 sites for a term of four years. A new management team is in place and we continue to invest in our back office

systems to reduce costs, sharpen our competitive position and enhance our customer service. In business services we have made good progress. We have now been selected as preferred contractor on seven multi-year energy performance contracts with public sector organisations and have a strong pipeline for the year ahead.

More normal weather and cost reduction programme driving profit growth

After an unseasonally warm 2011, total British Gas gross revenue increased to £13,857 million (2011: £12,403 million) reflecting higher gas sales volumes. Total British Gas operating profit increased to £1,093 million (2011: £1,005 million). We continue to make good progress on our cost reduction programme and are on track to deliver £300 million of cost savings across British Gas by the end of 2013. We are seeing the benefit of previous investment in industry-leading IT systems and have achieved savings through a range of initiatives, including a pay freeze for employees and changes to the defined benefit pension schemes. During 2012, we closed our Southampton call centre, outsourced a number of roles in British Gas Services and British Gas Business, reduced IT costs through new working practices, offshored and transitioned to new data centres and agreed improved commercial terms with suppliers. As a result, including the impact of investment in growth areas, operating costs were 1% lower in 2012 than in the prior period and, despite the weak economy, the bad debt charge as a proportion of revenue fell as the benefits of improved systems and processes were realised.

In residential energy, gross revenue increased to £9,121 million (2011: £7,930 million) reflecting higher consumption and retail tariffs. After a warm 2011, cooler weather in 2012 saw average domestic gas consumption increase by 12%, more than offsetting underlying energy efficiency reductions. Average electricity consumption was broadly flat compared to 2011. Residential energy operating profit increased to £606 million (2011: £544 million). Commodity and transportation and distribution costs both increased, while environmental costs rose by 22% to £732 million (2011: £599 million). The residential energy operating margin was 6.6% (2011: 6.9%), in line with our through-cycle expectations.

In residential services, gross revenue increased slightly to £1,674 million (2011: £1,644 million) with a rise in revenue from insulation jobs more than offsetting a decline in installations revenue. Operating profit increased by 16% to £312 million (2011: £269 million), while the operating margin increased to 18.6% (2011: 16.4%) driven by cost efficiencies and an improved contribution from our new markets activity.

In business energy supply and services, gross revenue increased to £3,062 million (2011: £2,829 million) with operating profit falling by 9% to £175 million (2011: £192 million), reflecting the challenging external environment. Business services revenue increased by 12% compared to 2011.

Leading the transition to smart connected homes and businesses

We continue to lead the industry in smart metering and have now installed over 800,000 smart meters in homes and businesses. We welcomed the Government's confirmation of the standards for the smart meter roll-out and we are the only supplier currently installing fully compliant Phase 3 meters in customers' homes. Smart meters are a key enabler for a range of technologies and by going early on the roll-out we have gained invaluable experience. We are also starting to see the benefit of smart meters delivering an enhanced customer experience, including significantly lower contact rates, fewer complaints and higher retention. We have made a number of investments in smart technology companies, including AlertMe, which enables a range of home automation applications and Power Plus Communications, which specialises in smart applications in complex buildings. During the year we launched our award winning 'Remote Heating Control' product which allows customers to monitor and control their central heating system via the internet or a smart phone. Around 15,000 customers are now using the product and, as part of a bundle, it is also driving higher sales conversion of central heating systems. For our smart meter customers, we also launched the 'Smart Energy Report' to provide visibility of how their energy is being used and to help them reduce their consumption.

We will continue to lead the transition to smart connected homes and businesses, offering attractive propositions, which will improve customer engagement and deliver lower costs for the business.

Innovate to drive growth and service excellence

Performance in 2012 in a challenging economic and competitive environment has demonstrated that our business model remains sound. In residential energy supply it will be increasingly important to differentiate our offering through service excellence and innovation. Our scale and leadership in customer service, cost efficiency and systems leave us well placed to continue to deliver a fair level of margin in this business. In residential services, our focus remains on offering attractive customer propositions and delivering service excellence, while also working to reduce costs further during 2013. We expect to deliver continued profit growth in services, although not at the high levels achieved in 2012. In business energy supply, the environment remains challenging. We are investing in our back office systems to reduce costs and improve service and, over time, we expect business services to make a more material contribution. Looking to the future, smart meters are a key enabler in the trend towards the 'smart connected home'. British Gas' leadership in smart metering and technology will enable us to capitalise on this trend, deepening customer relationships and differentiating our energy and services offer to drive long-term growth.

CENTRICA ENERGY

" THE GAS MARKET IS BECOMING INCREASINGLY GLOBAL. WE AIM TO BUILD AN INTEGRATED INTERNATIONAL BUSINESS FOCUSED ON THE ATLANTIC BASIN. "

Mark Hanafin
Managing Director, Centrica Energy

2012 saw Centrica Energy make significant steps in delivering growth and value in its upstream gas and oil, power generation and midstream businesses.

In upstream gas and oil, we added 170mmboe to our reserves. The majority of these were added in Norway, helping to treble the size of our reserve base in this important region for growth. We also deepened our involvement in Norway by extending our Memorandum of Understanding with Statoil, enabling us to continue working together on gas exploration opportunities in Norway and the UK. This announcement was welcomed by the Prime Minister as helping to forge a strategically important relationship between the two nations.

The £1.4 billion development of the Cygnus field, the biggest gas discovery in the Southern North Sea for a quarter of a century, is now underway. Cygnus is expected to create around 4,000 jobs in the development phase, underlining the importance of the energy sector for UK economic growth. In other UK North Sea projects, we achieved first gas at the Ensign and Seven Seas fields in 2012.

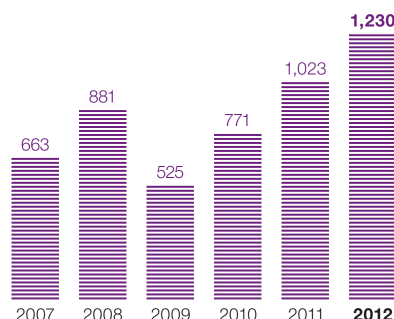
2012 also saw important developments in offshore wind. We received planning consent for 580MW at the Race Bank wind farm to be built off the Lincolnshire coast – close to our 270MW Lincs development. Lincs achieved first power and is due for completion in 2013. The continued development in renewables and a strong operating performance by the nuclear fleet delivered significant value for the Group and helped to offset the challenging conditions currently facing our gas-fired generation fleet.

Health, safety and environmental issues remain a core priority and we have continued to focus on the management of our major accident hazards. We have been progressively improving competence, reporting and accountability to ensure we are effectively managing process safety controls.

Despite the difficult external conditions in 2012, Centrica Energy is well positioned to deliver growth and value across its portfolio.

centrica energy

Adjusted operating profit‡
£m



For the year ended 31 December	2012	2011
Adjusted operating profit‡ (£m)		
Gas	**919**	769
Power	**311**	254
Gas and power		
Gas production (mmth)	**2,441**	2,160
Liquids production (mmboe)	**16.3**	12.5
Proven and probable reserves (mmboe)	**525**	410
Power generated (TWh)	**21.5**	26.7

‡ From continuing operations

A more balanced upstream business

Centrica Energy made significant progress during 2012 on its strategy to deliver value and growth. In upstream gas and oil, we integrated three North Sea acquisitions in 2012. This delivered a step change for the business, increasing production and significantly enhancing the scale and balance of our portfolio. In power, although the operating environment for gas-fired generation remains challenging, the business benefited from strong nuclear operational performance.

We have achieved a number of key project milestones, bringing reserves into production and generating first power from our 270MW Lincs offshore wind project. We have also made important steps to develop future cornerstone assets, with good progress at the Valemon gas field and the sanctioning of the £1.4 billion Cygnus gas field, one of the largest remaining development opportunities in the UK North Sea.

Total Centrica Energy operating profit increased by 20% to £1,230 million (2011: £1,023 million) with increased profit in both gas and power. This increase in profit was in part helped by the delivery of a series of cost initiatives in 2012 and the business is on track to deliver its contribution of cost savings to Group targets. These savings have not compromised on our continued focus on health, safety and environmental practices. Centrica Energy continues to progress its process safety programme, which focuses on the integrity of operating systems and processes that handle hazardous substances. We had no significant process safety events in 2012. In terms of environmental practices, we are committed to operating responsibly and will continue to engage with stakeholders, to understand and manage the environmental and social issues associated with new and existing investments.

Increased gas and oil reserves and production

Between November 2011 and February 2012 we announced three North Sea acquisitions, all of which completed during 2012, for a total of £1.2 billion. Overall, we added 170 million barrels of oil equivalent (mmboe) of 2P reserves in the year, as a result of acquisitions, upgrades of existing hubs such as Rhyl and bringing new projects such as Maria into the development pipeline. After taking production into account, we ended the year at 525mmboe of 2P reserves (2011: 410mmboe). Our Norwegian business now forms a significant part of the portfolio following the acquisitions, accounting for 41% of our upstream gas and oil reserves, compared to 18% at the end of 2011.

Total production of gas and liquids increased by 18% to 56.7mmboe (2011: 48.2mmboe). Total gas production volumes increased by 13% to 2,441 million therms (mmth) (2011: 2,160mmth) and total liquids volumes increased by 30% to 16.3mmboe (2011: 12.5mmboe), reflecting the benefit of recent acquisitions. We now have less reliance on production from Morecambe, which in 2012 contributed 23% of total production (2011: 29%) primarily due to increases from the rest of the portfolio. Performance from South Morecambe improved in the second half of the year, after we took action to stabilise the quality of gas delivered to the grid during the field's maintenance shut-down in the summer. Gas production volumes from Norway more than trebled to 557mmth (2011: 164mmth) while liquids volumes increased to 8.9mmboe (2011: 4.7mmboe), reflecting acquisitions during the year.

In 2013 we will benefit from a full year of production from the acquisitions made during 2012, and with new fields coming into production offsetting the natural decline from our existing fields, total production volumes are expected to increase by a further 15%.

Adding value through gas and oil development, appraisal and exploration

We achieved first gas at Seven Seas and Atla in the second half of the year, following on from Ensign having delivered first gas in May. At Ensign we have now also delivered production from the second well, however due to mechanical issues the initial production rate is below our original expectations. First gas is expected from York and Rhyl in the coming weeks, with first gas from Kew scheduled for the fourth quarter of 2013. Good progress continues to be made on the Statoil-operated Valemon project with the detailed design having been agreed towards the end of 2012 and fabrication having started early in 2013. The field is on track to produce first gas in the fourth quarter of 2014.

In August we announced that the £1.4 billion Cygnus project, in which we own a 48.75% interest, had been sanctioned. Key contracts have now been placed and the fabrication of the jacket and platform deck started ahead of schedule. The development will create around 4,000 jobs, mostly in the UK and bring 53mmboe of our reserves into production from late 2015, providing enough gas at peak production to supply 1.5 million homes.

In Trinidad and Tobago, we made further progress on the Block 22 project with the award of front end engineering design contracts for upstream and subsea facilities as well as the contracting of a rig to drill two appraisal wells to prove up our resource base. We continue to explore development and partnership options for gas export.

Our appraisal drilling at Rhyl North towards the end of 2012 was successful, and led to our 2P reserves being revised upwards by 7mmboe to 14mmboe. In early 2013, exploration drilling at Whitehaven confirmed that the Rhyl reservoir extends further than originally anticipated, potentially leading to

CENTRICA ENERGY CONTINUED

The UK and Norway will remain an important part of our investment and activity

HOW DID WE MEASURE UP?
CENTRICA ENERGY PERFORMANCE MEASURES CAN BE FOUND ON PAGE **148**

additional reserve upgrades. Rhyl and Whitehaven will both utilise our existing Morecambe infrastructure. Appraisal drilling at the non-operated Maria North well, in which we own a 20% interest, showed potential gross recoverable reserves of the Maria field towards the upper end of the 70-150mmboe range published following the discovery in 2010. Accordingly we have revised our 2P reserves up by 10mmboe to 25mmboe. Appraisal drilling at Bligh and exploration drilling at Cooper both encountered hydrocarbons, but tight reservoirs meant that commercial flow rates were not achieved. We also experienced non-operated exploration failures in Trinidad and Tobago. However in early 2013 drilling at the Rodriguez prospect in Norway was successful, confirming the presence of gas condensate.

In June, we extended our Memorandum of Understanding (MoU) with Statoil to collaborate on gas-focused exploration opportunities in Norway and the UK. In October, the UKCS 27th Round awarded Centrica six licenses covering 13 blocks and part-blocks. Three of the blocks will be Centrica-operated, two of which are in the West of Shetland, a new area for the Company. Early in 2013 we were awarded nine blocks in the latest round of licences announced by Norway's Energy Ministry. We will be the operator of three of these blocks, which are close to some of our existing assets. Our exploration record over the last three years has been good, with a success rate of 40% and a net finding cost of £3.5 per barrel of oil equivalent (boe).

Higher gas and oil volumes and achieved prices with reduced unit costs

Upstream gas and oil profitability increased by 20% to £919 million (2011: £769 million), reflecting higher production volumes and higher achieved prices. The average achieved gas sales price increased by 6% to 54.7 pence per therm (p/th) (2011: 51.6p/th) while the average achieved oil and condensate price increased by 10% to £62.8 per boe (2011: £57.2/boe). On a per unit of production basis, depletion, depreciation and amortisation (DDA) costs and lifting costs both decreased slightly, to £9.8/boe (2011: £10.1/boe) and £9.7/boe (2011: £9.9/boe) respectively, with recent acquisitions incurring lower unit lifting costs. Overall production and overhead costs increased by 22% to £1,374 million (2011: £1,127 million) due to the impact of the North Sea acquisitions, new gas and oil fields coming into production, the expensing of a £73 million cost relating to the failure of a third development well at Ensign and inflationary cost increases. In addition we incurred exploration and appraisal costs of £139 million (2011: £97 million), reflecting a lower level of drilling success.

Continued strong performance from nuclear; challenging market conditions for CCGTs

The nuclear fleet recorded strong performance during the year, with our 20% share of output increasing by 8% to 12.0 terawatt hours (TWh) (2011: 11.2TWh). This reflects continued investment in the fleet, with no large unplanned outages during the year, underlining the quality of our original investment in the nuclear fleet. In addition, plant life extensions to the Hinkley Point B and Hunterston B nuclear power stations were announced in December, extending the life of these stations by seven years from 2016 to 2023. The expectation for nuclear plant life extensions for the AGR fleet in the UK is now for seven years on average, compared to the five years previously assumed, and this will deliver additional long-term value.

The market environment remains challenging for gas-fired plant with continued low market clean spark spreads. Reliability remained high at 97% (2011: 98%), however generation volumes fell by 40% to 9.0TWh (2011: 15.0TWh), with an average load factor of 26% (2011: 35%). The market conditions led to the mothballing of our 325MW King's Lynn power plant at the beginning of the year and we have now also withdrawn our 229MW Roosecote power station from service. Our plants at Barry and Brigg continue to operate in the STOR market, with contracts in place until the end of the first quarter of 2013 while our Peterborough plant has a contract which will commence in April 2013. Against this difficult market environment, we have been successful in minimising our costs and running the plants as efficiently as possible, with high levels of availability enabling running at peak times. In February 2013, we sanctioned a turbine blade upgrade at our 1.2GW South Humber power station, which will improve the efficiency of the plant.

Availability in our wind assets was 88% (2011: 92%), reflecting an outage at Inner Dowsing in the first quarter, with generated volumes down 11% to 533 gigawatt hours

(GWh) (2011: 596GWh). The load factor was 32% (2011: 36%).

Power profitability increased by 22% to £311 million (2011: £254 million). Nuclear profitability increased, benefiting from a higher achieved average price of £49.6/MWh (2011: £48.5/MWh), reflecting some benefit from forward hedging, as well as the strong operational performance. Wind profitability also increased, with the sale of 50% of our Round 3 wind farm interest to Dong, in line with our established business model to partner on offshore wind, resulting in a net profit of £32 million after taking into account a charge relating to the refusal of consent at our Docking Shoal project. Our CCGT fleet made a small loss in 2012, the last year of free carbon allowances, reflecting the weak market conditions.

Investing for value in power

In offshore wind, our 270MW Lincs project has now generated first power and is expected to be fully operational in the second half of 2013. We have invested over £3 million in a new operations base at Grimsby docks to serve Lincs and other potential Centrica Energy wind farm developments, a substantial investment in the local area.

We continue to progress towards a final investment decision on the Race Bank project, which is consented for 580MW. We are willing to commit £200 million for the project, and are in discussion with a financial partner and the Government concerning the economic framework. During 2012 we also established a joint venture with Dong Energy to co-develop the Round 3 Irish Sea wind farm zone.

Formal consultation and a programme of stakeholder engagement was undertaken throughout the year. A final investment decision is expected on the first project in 2016, subject to returns being suitably attractive.

In February 2013 we announced that we would not be exercising our option to participate in UK nuclear new build, taking into account the lengthening time frame for a return on capital invested in a project of this scale. The decision follows detailed appraisal of the project, with pre-development expenditure approaching the agreed £1 billion cap; accordingly Centrica's share of project costs have been written off, with the Group recording a total impairment of £231 million.

We have also decided not to proceed with planning applications to develop dedicated biomass power stations at Roosecote and Brigg, with recent clarification on the regulatory framework indicating a preference for co-firing and coal conversion. As the market becomes increasingly dependent on fixed price support mechanisms, we will leverage our competencies, investing only where we see value.

Integrate our natural gas business, linked to our core markets

The gas market is becoming increasingly global. We have made progress in diversifying our sources of gas, including agreements to import pipeline gas from Norway and LNG from Qatar through our regasification capacity at the Isle of Grain. We are looking to secure gas increasingly from a wider range of sources, expanding the scope of our activities where appropriate. Our aim is to connect sources of energy to our customers, building an integrated international business focused on the Atlantic basin.

The UK and Norway will remain an important part of our investment and activity, as we look to maintain an appropriate energy hedge. We have a number of large scale projects ongoing, including Cygnus and Valemon, and we retain a number of attractive potential development opportunities, particularly in Norway, including at Butch where appraisal drilling is planned in late 2013. Decisions are targeted during 2013 on further infill drilling opportunities in the East Irish Sea and North Sea. However, with UK North Sea developments becoming smaller in scale and relatively more expensive, we will increasingly look to diversify our production portfolio, linked to our core markets. This is likely to include further investment in North America, possibly in shale gas, and there is also the potential for gas exports later in the decade. We will invest where we see value across our international portfolio, delivering annual production in the range 75mmboe to 100mmboe. In midstream, we have significant capabilities and presence in European and North American gas markets where we have important strategic participation in pipeline capacity, regasification capacity and gas storage. We will also look to develop our asset-based midstream trading and optimisation business over time, with an emerging presence in LNG. However we will invest only where we see value, with rewards commensurate with the scale of investment and associated risks.

CENTRICA STORAGE

" CENTRICA STORAGE PLAYS A KEY ROLE WITHIN THE GROUP'S INTEGRATED ENERGY BUSINESS AND MAKES A VITAL CONTRIBUTION TO THE SECURITY OF ENERGY SUPPLIES FOR THE UK. "

Grant Dawson
Chairman, Centrica Storage

I am pleased to report that Centrica Storage achieved higher profits from our Rough gas storage facility in 2012 than in 2011.

Early in 2012 we benefited from the widening spreads between summer and winter gas prices which are a key driver of storage revenue. However, at this level the prices still remain below that needed to invest in new storage and that's why our Baird and Caythorpe projects have remained under review with no major physical works undertaken during the year.

We do, however, remain convinced that the UK will require more gas storage capacity in the future and therefore have continued to engage with various stakeholders, including the UK Government, on ways to support the investment needed. The Government's Energy Bill and Gas Generation Strategy have confirmed a clear and continuing role for gas in the UK's medium to long-term energy mix and we believe, reinforces the need for increased levels of seasonal gas storage in the UK. We are particularly encouraged by the commitment of the Department of Energy & Climate Change (DECC) to publish a review of the need for storage support in the first half of 2013.

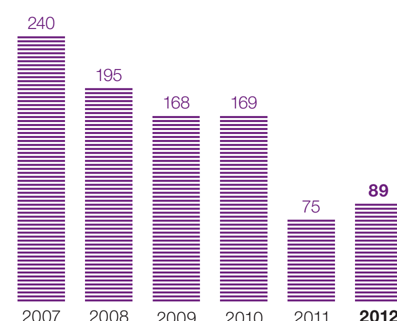
In the meantime we have continued to focus on strengthening the existing business by concentrating on our underlying business performance, processes and our overall efficiency.

At Centrica Storage 'Do Everything Safely' is one of our core priorities and I am encouraged that 2012 has been another strong year in terms of our safety record. I am particularly pleased that in September we passed three years without a single lost time incident right across the business. This was particularly challenging in 2012 as significant work was undertaken at our Easington Terminal, to build the reception and processing facilities for gas coming from Centrica Energy's York offshore field.

The first cold spell of the 2012 winter, in early December, saw our Rough storage facility once again withdrawing at full rates, demonstrating our key role within the Centrica Group's integrated energy business and also the vital contribution we make to the security of energy supplies for the UK.

centrica storage

Adjusted operating profit‡
£m



For the year ended 31 December	2012	2011
Average SBU price (pence)	31.0	30.0
Gross revenue (£m)	202	184
Adjusted operating profit‡ (£m)	89	75

‡ From continuing operations

HOW DID WE MEASURE UP?
CENTRICA STORAGE PERFORMANCE MEASURES CAN BE FOUND ON PAGE **148**

Strong performance in a challenging market environment

Centrica Storage performed well in 2012, with strong commercial performance securing the benefits of higher summer/winter price differentials seen in the first half of the 2012/13 storage year. The Rough asset achieved reliability of 92% in the year (2011: 96%), with performance in the first half similar to that experienced in the first half of 2011 but with the second half impacted by a small number of production outages. These outages had limited commercial impact and across the year asset availability was good when required to meet customer demand.

The high level of stock carry-over into 2012 combined with modest withdrawal in the first quarter of the year meant that the Net Reservoir Volume (NRV) was at relatively high levels again going into the 2012 injection season. A strong injection season over the summer was followed by the final quarter of 2012 experiencing withdrawals more in line with seasonal normal levels. As a result the NRV level carried into 2013 was above the five year average level but below the level at the start of 2012.

Health and safety remains one of our core priorities; this relentless focus has enabled the business to continue its strong record through 2012, with no lost time incidents recorded for more than three years, corresponding to over 5 million man hours of work without an incident.

Forward seasonal spreads have narrowed since the first quarter

The business saw higher summer/winter price differentials in the final quarter of 2011 and the first quarter of 2012 compared to the first quarter of 2011, which resulted in an achieved 2012/13 storage year Standard Bundled Unit (SBU) price of 33.9 pence (2011/12: 25.2 pence). However, price differentials subsequently narrowed, reflecting colder than normal weather in the summer months and an expectation of LNG availability for the winter. Forward spreads remain relatively narrow for the 2013/14 storage year, with price volatility remaining at subdued levels.

HEALTH AND SAFETY REMAINS ONE OF OUR CORE PRIORITIES; THIS RELENTLESS FOCUS HAS ENABLED THE BUSINESS TO CONTINUE ITS STRONG RECORD THROUGH 2012, WITH NO LOST TIME INCIDENTS RECORDED FOR MORE THAN THREE YEARS.

Improved operating profit

Gross revenue increased by 10% in 2012 to £202 million (2011: £184 million). This reflects the higher summer/winter price differentials and benefits from the high NRV carried into 2012. SBU revenue was 4% higher in 2012 with the calendar year SBU price increasing to 31.0 pence (2011: 30.0 pence). Operating profit increased by 19% to £89 million (2011: £75 million) benefiting from higher revenue and strong cost control, partially offset by inflationary pressures and additional depreciation resulting from previous investment in Rough. From 2013 the business will benefit from additional revenue streams associated with gas processing and condensate sales at the newly constructed York processing plant.

Challenging economics for new projects

We retain the option to invest in our Baird and Caythorpe gas storage projects. However, the continuing relatively low levels of summer/winter price differentials and reduced price volatility, combined with an uncertain longer term outlook, mean that market conditions remain challenging for these opportunities. With the country becoming increasingly dependent on imported gas we believe that more seasonal storage is required in the UK. However we will only invest in new projects if the returns are appropriate for the level of risk undertaken. We may require a support mechanism to underpin the investment and welcomed the announcement by DECC in December that it is planning to carry out further investigation into possible intervention mechanisms to encourage new storage investment. We look forward to the outcome of this review, with initial findings expected in spring of 2013.

DIRECT ENERGY

"WE HAVE BUILT A GOOD PLATFORM FOR GROWTH IN NORTH AMERICA, WITH STRONG CAPABILITIES IN ENERGY SOURCING AND SUPPLY, RISK MANAGEMENT, ENERGY SERVICES AND UPSTREAM GAS AND POWER."

Chris Weston
Managing Director, Direct Energy

Our focus for the year ahead is to make progress against our strategic priorities as we position ourselves to meet the energy and services needs of customers now and in the future.

We continue to build an integrated North American business with leading positions in competitive markets and are investing for growth across the four lines of business. We will also maintain our focus on cost reduction and seek efficiencies from increased scale across our operations, while remaining solidly committed to deepening customer relationships by delivering innovative products and services.

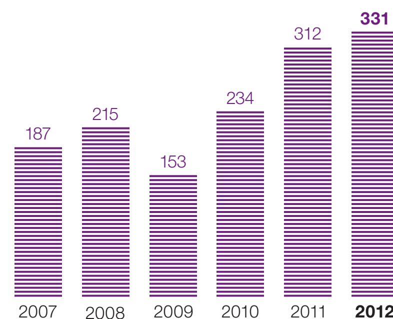
Strong organic growth and acquisitions have positioned Direct Energy as one of North America's largest energy and energy-related services providers. We will continue to focus investment in markets that provide an environment conducive to retail competition and the consumer benefits that come from having a choice of providers – particularly in the competitive retail markets in Texas and in the US North East.

We see continued progress and opportunity for innovation and differentiation through smart meter technologies, demand response and energy efficiency related products and services. Customers are responding favourably to our industry-leading prepaid product and flexible time-of-use offerings enabled by smart technology and we plan to expand this product range.

By operating across the entire energy value chain, from sourcing to supply, we create stability and value for our customers. As North America's importance grows with an increasingly global gas market, we will continue to pursue value-creating opportunities that enhance our existing portfolio of natural gas production, power generation and wholesale and retail energy services.

Our values of being simple, friendly and direct remain at the heart of our approach to customers as we strive to offer products and services that make a difference in people's lives.

Adjusted operating profit‡
£m



For the year ended 31 December	2012	2011
Adjusted operating profit‡ (£m)	**331**	312
Residential energy and services accounts (year end, '000)	**5,856**	5,647
Business energy electricity volumes (TWh)	**51.4**	46.4
Total net proven and probable reserves (mmboe)	**108**	109

‡ From continuing operations

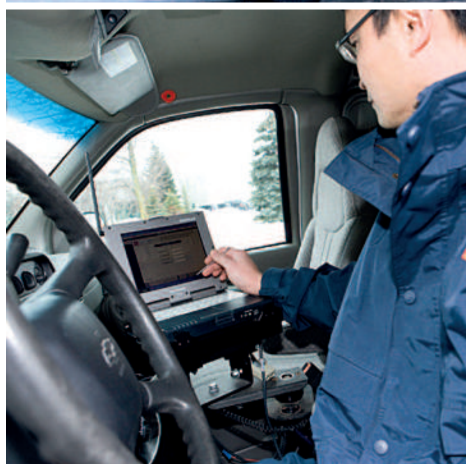
Further profit growth in a low gas price environment

Direct Energy delivered another strong performance in 2012, in a low gas price environment. Gross revenue decreased by 2% to £6,015 million (2011: £6,117 million) but operating profit increased by 6% to £331 million (2011: £312 million). There was no material impact resulting from currency movements during the year.

The business has benefited from organic customer growth in the US North East and the small business customer segment, and from the successful integration of recent acquisitions. We also continue to drive operational efficiencies throughout the business, and the move of our North American headquarters to Houston, combined with overall headcount reductions, has delivered significant benefits. We will continue to drive efficiencies, with further rationalisation of IT resources due to be undertaken in 2013. The health and safety of our employees and customers continues to be one of our core priorities. The LTIFR reduced by 45% to 0.11 per 100,000 hours worked (2011: 0.20) and we had no significant process safety events in 2012.

Benefiting from enhanced scale in residential energy supply

Direct Energy Residential made good progress during the year, with organic customer growth in the US North East, the successful integration of recent acquisitions and strong increased customer satisfaction levels across the business. Overall customer accounts increased to 3.5 million (2011: 3.4 million) despite incurring further customer losses as a result of the regulatory environment in Ontario. Gross revenue decreased by 2% to £2,357 million (2011: £2,416 million), while operating profit was broadly flat at £156 million (2011: £161 million) reflecting the decline in the Ontario business, offset by the positive impacts of customer growth and acquisitions in the US. We are also seeing the benefits from operational efficiencies and billing system rationalisation, with increased scale in the US North East.



WE EXPECT OUR DOWNSTREAM BUSINESS TO BECOME A MORE MATERIAL PART OF THE GROUP OVER THE NEXT THREE TO FIVE YEARS.

We will continue to look for opportunities to grow our business across North America by focusing on growing organically and through our successful bolt-on acquisition strategy, delivering scale and synergies.

In the US North East, our business is materially larger following the integration of Gateway and Vectren Source, both acquired in 2011, and the acquisition of a further 207,000 residential and 38,000 small business accounts from New York based energy retailers Energetix and NYSEG Solutions from Iberdrola USA, completed in August. The business also experienced organic growth in 2012 due to strong sales performance, despite the expected roll-off of low margin aggregation customers acquired as part of the Vectren Source acquisition. We now have 1.4 million customers in the region, up from 1.1 million at the end of 2011.

Our Texas residential business is also benefiting from increased scale, following the First Choice Power acquisition in 2011. Our prepaid 'Power to Go' product continues to attract customers, as well as being viewed positively by regulators, who welcome the expansion of choice for all customer groups. In October, we launched a 100% renewable tariff, providing environmentally conscious customers with wind power from Texas.

We delivered good sales performance in the US during the year, underpinned by a continued focus on channel efficiency, while our consolidated billing platform has helped reduce costs and bad debt. Churn reduction continues to remain a focus both in Texas and the US North East.

We no longer view our residential energy supply business in Ontario as core, following the implementation of the Energy Consumer Protection Act (ECPA), which makes it difficult to sell to new customers or retain existing ones. We continue to actively manage the decline of our customer base and have more than halved operating costs since 2010 through aggressive cost management. In total we lost 95,000 customer accounts in Ontario during 2012 and now have just over 200,000 customers in the region, around half the amount we had at the end of 2010. In 2012, Ontario contributed less than 20% of our residential energy operating profit and this is expected to fall to around 5% in 2013. In Alberta, profitability rose, with increases in regulated rates leading to higher churn levels in the

DIRECT ENERGY CONTINUED

Our values of being simple, friendly and direct remain at the heart of our approach

HOW DID WE MEASURE UP?
DIRECT ENERGY PERFORMANCE MEASURES CAN BE FOUND ON PAGE **149**

low margin regulated business and growth in the higher margin competitive customer base.

Focus on small businesses leading to volume growth in business energy supply

Direct Energy Business again delivered strong growth in the year, in a highly competitive market. Electricity volumes rose 11% to 51.4TWh (2011: 46.4TWh), while gas volumes increased by 11% to 793mmth (2011: 714mmth). Higher volumes in the small commercial business sector are driving much of the growth, and profit in this sector nearly doubled in 2012, reflecting strong sales and scale benefits resulting from recent acquisitions. The larger commercial segment is increasingly competitive, however our retention rates remain high in this sector.

Gross revenue in business energy supply decreased by 2% to £2,690 million (2011: £2,748 million), with the impact of lower commodity prices more than offsetting volume growth. Operating profit increased to £129 million (2011: £110 million) while operating margin increased to 4.8% (2011: 4.0%), reflecting the positive impact of operational efficiencies and a higher proportion of small business customers.

Strengthening the services platform

Direct Energy Services is performing well, gaining market share in a challenging economic environment, with many of our competitors experiencing losses or credit downgrades. Our nationwide on-demand franchise has provided scale advantages, while the acquisition of Home Warranty

of America (HWA), completed in March, provides the necessary licences to offer protection plan products across the United States. The number of contract relationships increased by 5% during 2012, mainly reflecting the HWA acquisition.

Our Canadian business was impacted by warmer than normal weather and industrial action by a number of our unionised technicians in the first half of the year. The labour issues have now been resolved, resulting in a significant improvement to our cost base and more flexible working arrangements, improving our service to customers.

Continued weak economic conditions, low consumer confidence and a slow housing market have impacted underlying growth in the US services business, leading to less lead generation and reduced demand for home services products. However we continue to focus on delivering high levels of customer satisfaction and our overall Net Promoter Score increased to +39 (2011: +28).

Gross revenue increased by 2% to £532 million (2011: £520 million) and operating profit increased to £33 million (2011: £28 million), with operational efficiencies and cost control driving much of this growth.

Solid upstream and wholesale performance in a low price environment

Direct Energy Upstream continues to face a low wholesale price environment, although the Henry Hub natural gas price recovered slightly during the second half of the year from the record low levels seen

in the first half. Alberta gas production volumes fell by 3% to 549mmth (2011: 567mmth), with the achieved gas price falling to C$3.8/MCF (2011: C$4.6/MCF). The price of liquids remains relatively high however, and the acquisition of the Carrot Creek assets, completed in January, meant that oil and liquids production volumes nearly doubled to 1.1mmboe (2011: 0.7mmboe). We added 10mmboe of reserves in North America over the year meaning that after taking account of production, 2P reserves remained broadly flat at 108mmboe (2011: 109mmboe).

Texas power generation volumes increased by 21% to 6,336GWh (2011: 5,247GWh), with good asset availability and optimisation performance. Texas experienced more normal weather conditions during the summer months, meaning that spikes in power prices were less extreme than in the exceptional conditions in 2011.

Overall, upstream and wholesale gross revenue was £436 million (2011: £433 million) while operating profit was flat at £13 million (2011: £13 million).

Well placed to further grow and develop our North American business

We have built a good platform for growth in North America, with strong capabilities in energy sourcing and supply, risk management, energy services and upstream gas and power. In 2013, we should continue to benefit from recent residential acquisitions, with integration now mostly complete, while we have created a more efficient operating base

THE HEALTH AND SAFETY OF OUR EMPLOYEES AND CUSTOMERS CONTINUES TO BE ONE OF OUR CORE PRIORITIES

in both energy and services. Upstream, natural gas prices continue to be constrained by the impact of shale but production expansion opportunities are available and we will pursue them if value can be created.

We continue to look for opportunities to grow our business across North America. Downstream, we will continue to focus on growing organically, through churn reduction and differentiation. We will also continue with our successful bolt-on acquisition strategy, delivering scale and synergies, and will consider larger opportunities where appropriate. Over the next three to five years we are targeting a doubling in profitability of our North America downstream business through organic growth and acquisition, with Direct Energy downstream becoming a more material part of the Group. We will also look for opportunities upstream, with the potential for exports over time. In each case, we will only invest where we see value and a good fit with our Group-wide capabilities.

GROUP FINANCIAL REVIEW

" THE GROUP INVESTED £2.7 BILLION OF CAPITAL IN 2012, MATERIALLY INCREASING THE SCALE AND GEOGRAPHIC DIVERSITY OF THE BUSINESS. "

Nick Luff
Group Finance Director

Group revenue from continuing operations was up 5% to £23.9 billion (2011: £22.8 billion).

Revenue increased in British Gas due to higher gas consumption as a result of colder weather and higher retail gas and electricity prices. Revenue decreased in Centrica Energy, with the impact of lower gas-fired power generation volumes and reduced midstream activity following the closure of our German wholesale business in 2011, more than offsetting the impact of higher gas and liquid volumes. Revenue in Direct Energy was broadly flat, reflecting higher average customer numbers and increased business energy consumption, offset by lower wholesale energy prices.

Throughout the Business Review, reference is made to a number of different profit measures, which are shown in the table below:

		2012			2011		
	Notes	**Business performance £m**	**Exceptional items and certain re-measurements £m**	**Statutory result £m**	Business performance £m	Exceptional items and certain re-measurements £m	Statutory result £m
Adjusted operating profit:							
British Gas		**1,093**			1,005		
Centrica Energy		**1,230**			1,023		
Centrica Storage		**89**			75		
Direct Energy		**331**			312		
Total adjusted operating profit	4b	**2,743**			2,415		
Depreciation of fair value uplifts from Strategic Investments, before tax	11	**(96)**			(105)		
Interest and taxation on joint ventures and associates	4b	**(85)**			(102)		
Group operating profit	4b,7	**2,562**	**63**	**2,625**	2,208	(794)	1,414
Net interest expense	8	**(183)**	**–**	**(183)**	(146)	–	(146)
Taxation	7,9	**(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 year		**1,350**	**(77)**	**1,273**	1,265	(844)	421
Depreciation of fair value uplifts from Strategic Investments, after taxation	11a	**56**			68		
Adjusted earnings		**1,406**			1,333		

Business Review – Group Financial Review

Total adjusted operating profit was up 14% to £2,743 million (2011: £2,415 million). In British Gas, profitability increased, with the impact of higher gas consumption and unit prices more than offsetting increased wholesale commodity, transportation and environmental costs in residential energy supply, and cost efficiency measures driving growth in residential services. In Centrica Energy, higher gas and liquids production resulting from acquisitions and higher achieved prices led to increased profitability in the gas segment, while higher nuclear power generation more than offset the impact of reduced gas-fired power generation volumes in the power segment. In Centrica Storage, improved seasonal price differentials during the final quarter of 2011 and the first quarter of 2012 led to higher profitability. In Direct Energy, profitability increased, with growth in services and business energy supply more than offsetting slightly lower profitability in residential energy supply, driven by less favourable market conditions in Ontario partially offset by the impact of recent acquisitions.

Net interest expense was £183 million (2011: £146 million), reflecting £1,196 million net issuance of debt during the year. The tax on adjusted profit from continuing operations was £1,029 million (2011: £810 million), reflecting a higher level of operating profit and an increased mix of more heavily taxed upstream operating profit. After adjusting for the tax impact of depreciation on the Venture fair value uplift and our share of taxation on joint ventures and associates, the adjusted tax charge from continuing operations was £1,110 million (2011: £891 million) and the resultant adjusted effective tax rate for the Group was 44% (2011: 40%). An effective tax rate calculation, split UK and non-UK, is shown in the table below.

Reflecting all of the above, profit from continuing operations after taxation was up 8% to £1,350 million (2011: £1,252 million) and after adjusting for fair value uplifts, adjusted earnings increased by 5% to £1,406 million (2011: £1,333 million). Adjusted basic earnings per share (EPS) increased to 27.1 pence (2011: 25.8 pence).

The statutory profit for the year was £1,273 million (2011: £421 million). The reconciling items between profit from business performance and the statutory profit are related to exceptional items, certain re-measurements and discontinued operations. The increase compared with 2011 was principally due to a net gain on certain re-measurements of £404 million (2011: net loss of £322 million). The Group reported a statutory basic EPS of 24.6 pence (2011: 8.2 pence).

In addition to the interim dividend of 4.62 pence per share, we propose a final dividend of 11.78 pence, giving a total ordinary dividend of 16.4 pence for the year (2011: 15.4 pence), an increase of 6%.

Group operating cash flow from continuing operations before movements in working capital was higher at £3,542 million (2011: £3,065 million), reflecting the contribution from Centrica Energy acquisitions. After working capital adjustments, tax, operational interest, and cash flows associated with exceptional charges and discontinued operations, this stood at £2,820 million (2011: £2,337 million).

The net cash outflow from investing activities was £2,558 million (2011: £1,400 million), as described in the business combinations and capital expenditure section on page 38. The increased outflow reflects the acquisitions of North Sea gas and oil assets.

The net cash inflow from financing activities was £190 million (2011: outflow of £907 million). The inflow reflects the net issuance of borrowings during the year exceeding dividends paid.

Reflecting all of the above, the Group's net debt at 31 December 2012 was £4,047 million (2011: £3,292 million). 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.

During the year net assets increased to £5,927 million (31 December 2011: £5,600 million), reflecting the impact of statutory profit for the year exceeding dividends paid.

Exceptional items

Exceptional charges from continuing operations of £534 million were included within Group operating profit during the year (2011: £331 million).

	UK £m	**Non-UK £m**	**2012 Total £m**	UK £m	Non-UK £m	2011 Total £m
Adjusted operating profit	**2,079**	**664**	**2,743**	2,042	373	2,415
Share of joint ventures / associates interest	**(44)**	**–**	**(44)**	(58)	–	(58)
Net interest expense	**(79)**	**(104)**	**(183)**	(71)	(75)	(146)
Adjusted profit from continuing operations before taxation	**1,956**	**560**	**2,516**	1,913	298	2,211
Tax on adjusted profit from continuing operations	**692**	**337**	**1,029**	682	128	810
Tax impact of depreciation on Venture fair value uplift	**40**	**–**	**40**	37	–	37
Share of taxation on joint ventures and associates	**41**	**–**	**41**	44	–	44
Adjusted tax charge from continuing operations	**773**	**337**	**1,110**	763	128	891
Adjusted effective tax rate	**40%**	**60%**	**44%**	40%	43%	40%

GROUP FINANCIAL REVIEW CONTINUED

Following a decrease in North American power prices, a charge of £89 million has been made to reflect the fair value of the obligation to purchase power above its net realisable value through onerous wind farm power purchase agreements.

On 4 February 2013, Centrica announced its decision not to proceed with nuclear new build investment. Accordingly, the Group has recorded an 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.

An exceptional restructuring charge of £214 million was recorded, mainly relating to staff reductions following the Group-wide cost reduction programme announced in 2012.

Taxation on the total of these charges generated a credit of £93 million (2011: £69 million). 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%. An exceptional tax charge of £40 million has been recognised from revaluing the related deferred tax provisions.

Certain re-measurements

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 IAS39 require the contracts to be 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 not typically 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 operating profit in the statutory results includes net gains of £597 million (2011: losses of £463 million) relating to these re-measurements, of which there are a number of elements. The profits arising from the physical purchase and sale of commodities during the year, which reflect the prices in the underlying contracts, are not impacted by these re-measurements. See note 2 for further details.

Business combinations and capital expenditure

On 30 April 2012, the Group completed the acquisitions of certain oil and gas production and development assets from Statoil and ConocoPhillips for a combined total cash consideration of £911 million. In addition, total tax liabilities of £169 million were assumed on completion of the acquisitions. During the year the Group also completed the acquisition of a portfolio of producing oil and gas assets from Total for total cash consideration of £133 million. These three acquisitions are included within the Centrica Energy gas segment.

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. The acquisition is included in the Direct Energy residential energy supply and business energy supply segments.

Further details on capital expenditure and business combinations are included in notes 4(e) and 30 respectively.

Events after the balance sheet date

On 4 February 2013, Centrica announced its decision not to proceed with nuclear new build investment. Accordingly, the Group has recorded an impairment of £231 million. The Group also announced on 4 February 2013 its intention to launch a £500 million share repurchase programme to return surplus capital to shareholders, which will be conducted over 12 months.

Further details on events after the balance sheet are described in note 36.

Risks and capital management

The Group's risk management processes are largely unchanged from 31 December 2011. Details of how the Group has managed financial risks such as liquidity and credit risk are set out in note 25.

Details on the Group's capital management processes are provided under sources of finance in note 12.

Accounting policies

UK listed companies are required to comply with the European regulation to report consolidated financial statements in conformity with International Financial Reporting Standards (IFRS) as adopted by the European Union. The Group's specific accounting measures, including changes of accounting presentation and selected key sources of estimation uncertainty, are explained in notes 1, 2 and 3.

Nick Luff
Group Finance Director
27 February 2013

MORE INFORMATION

Risk management and internal controls on page **58**

CORPORATE RESPONSIBILITY REVIEW

" OUR BUSINESS INVOLVES US IN A WIDE RANGE OF SOCIAL, ENVIRONMENTAL AND ETHICAL ISSUES. "

Mary Francis CBE
Chairman of the Corporate Responsibility Committee

Corporate Responsibility in Centrica is overseen by a Committee of the Board. This is our sixth report.

A continuing concern for all companies is the fact that public trust in business, especially in the UK, remains low. We believe strongly that a company's approach to corporate responsibility (CR) – being mindful of its long-term impact on the societies and environments in which it operates – has an important role to play in rebuilding public confidence.

Centrica's strong business performance in 2012 had a direct impact on its broader contribution to society. Through our dividend we were a major contributor towards retirement savings and through our investments of £2.7 billion we helped secure affordable energy supplies and create jobs. Our Cygnus gas field, for example, will create around 4,000 jobs during the development phase, whilst our Lincs offshore wind farm will supply low carbon electricity to some 200,000 homes. We continued to take a lead in helping households save energy and in offering energy choices that are simple, fair and transparent and during the year we spent more than any other supplier on helping those who are more vulnerable.

Centrica's corporate responsibility ambition is to be the most trusted energy company. In 2012, we focused on:

- treating customers with fairness;
- securing affordable energy supplies; and
- reducing carbon emissions.

In this review, we summarise our approach to corporate responsibility including governance, processes and material issues. Since corporate responsibility is an integral part of our decision-making, more detail about the way in which our individual businesses have contributed to the societies and environments in which they operate, can be found in the Operating Review on pages 22 to 35.

External assurance and performance indicators

We want our stakeholders to be confident that our metrics accurately reflect our performance. We therefore asked Deloitte LLP to review the most important key performance indicators that have a material impact on our business and to provide limited assurance, using the International Standard on Assurance Engagements (ISAE) 3000. Key performance measures are included in this review, with a full table available on pages 150 and 151.

Deloitte's full assurance statement and the Basis of Reporting are available in our online Annual Report at centrica.com/report2012/assurance.

Other significant aspects of our businesses and CR activities which include management of the supply chain, environmental management and community engagement and investment can be found online at centrica.com/responsibility

CORPORATE RESPONSIBILITY REVIEW CONTINUED

Governance, risk and stakeholder engagement

Centrica's business principles (see page 8) provide the basis for consistent decision-making across the Group. They set out the operating behaviours we require based on trust, integrity and openness.

To make sure we apply our values consistently and reconcile conflicting priorities responsibly, we have strong governance and internal control systems. Effective governance also helps ensure corporate responsibility is integral to our business activities.

The role and membership of the Corporate Responsibility Committee is set out on page 57 together with the key issues reviewed by the Committee during 2012.

Assessing material risks and opportunities

Our business involves us in a wide range of social, environmental and ethical issues. The individual business units are responsible for identifying material issues of concern to their stakeholders and assessing the potential impact of their operations on society and the environment. The Executive Committee and the corporate responsibility teams in each business contribute to these assessments, working closely with our business risk teams.

Stakeholder engagement

Engaging openly with stakeholders enables us to understand and respond to issues that concern people. During 2012 we kept in regular contact with stakeholder groups, including governments, regulators, investors, business partners, local communities and non-governmental organisations, to maintain a comprehensive understanding of their views about our business and its wider impacts.

The Corporate Responsibility Advisory Group set up in 2011 continues to provide valuable external feedback and guidance. Its members are drawn from our key stakeholder groups. The CR Advisory Group met twice in 2012 and advised on several issues including the environmental and social impacts of our approach to procurement, vulnerable customers and offshore wind. It also provided input into the development of the British Gas Community Engagement Strategy.

WE ARE DEMONSTRATING TRANSPARENCY BY PARTICIPATING IN FTSE4GOOD AND THE CARBON DISCLOSURE PROJECT

We continued our dialogue with socially responsible investment organisations and covered corporate responsibility issues at mainstream shareholder presentations. We participate in selected indices such as FTSE4Good and the Carbon Disclosure Project (CDP) demonstrating transparency and enabling us to benchmark our performance. In 2012 we were again included in the CDP Leadership 'Global 500' Index and were the top scoring UK utility company.

FTSE4Good

Corporate responsibility strategy

Our priorities in 2012 were treating customers with fairness, securing affordable energy supplies and reducing carbon emissions.

Our corporate responsibility priorities will be reviewed in consultation with internal and external stakeholders in the light of the Group's refreshed strategic priorities introduced in the Chief Executive's Review on page 11. Any changes will be set out in our online Corporate Responsibility Report to be released at the beginning of May 2013.

Treating customers with fairness

We continue to focus on building trust with our customers, government and other stakeholders. We need to be trusted by our customers for them to continue to choose us as their supplier and by governments and regulators for our views to carry weight.

In 2012, aware that trust among the UK public in the energy sector was low, we continued to act to restore faith in our business. We maintained our efforts to make energy buying simpler and easier to understand for all our customers through simplifying bills and tariff structures, moving to single tier pricing and providing special support for our more vulnerable customers. We also engaged fully with Ofgem, the UK regulator, notably in its Retail Market Review. We will build on these activities in 2013.

Affordability

Household budgets remain under pressure and rising energy bills have contributed to this. We have worked hard to help households save energy and to reduce our operating costs, both of which feed through to bill levels. A slight fall in wholesale electricity prices allowed us to decrease prices by 5% in January 2012. However, wholesale gas prices are now 13% higher than in winter 2011/12 while costs for upgrading the UK's grid and meeting carbon reduction targets have increased by around £50 per customer. As a result we had to increase our prices for domestic gas and electricity in November by an average of 6%.

Customer satisfaction

We have made significant improvements in standards of service in recent years. In the UK, call answering and handling times have improved, supported by initiatives such as the British Gas 'Look Who's Calling' training programme which teaches employees to better understand and respond to customers' needs. We track customer satisfaction by using Net Promoter Scores (NPS), which measure a customer's willingness to recommend us. The British Gas NPS increased in 2012 with an annual average score of +30 compared with +26 in 2011. Direct Energy

NPS ended 2012 at +39, a significant improvement on the 2011 score of +28.

We continue to work hard on resolving complaints and, in the UK, the number of complaints to our residential services business fell. In the UK, along with other suppliers, we are now reporting our complaints information quarterly to Ofgem.

Listening to customers

An important way of improving our service is to listen to our customers and act on their concerns. In the UK this has resulted in three areas of focus – fairness, simplicity and honesty. These in turn have led to practical changes in our service, such as the introduction of a tariff checker to enable customers to see if they are on the best tariff for their needs, simpler bills and more openness in the way we respond to complaints.

Vulnerable customers

We continued to provide targeted assistance to vulnerable customers in the UK, primarily by advising on energy efficiency and debt, discounted tariffs, products and services and energy and household grants, and through some direct financial support.

FOR FURTHER INFORMATION ON INITIATIVES DESCRIBED IN THIS SECTION SEE THE OPERATING REVIEWS FOR BRITISH GAS AND DIRECT ENERGY ON PAGES **22** AND **32**.

Securing affordable energy supplies

We continue to invest in securing energy supplies for the UK through investments in North Sea oil and gas assets. Our Cygnus project will, at peak production in 2015, supply nearly 1.5 million homes. Our offshore wind farm investments are progressing. We achieved first power from our Lincs offshore wind farm in 2012 and were granted consent for the 580MW Race Bank offshore wind farm project. We have increased diversification through agreements to import pipeline gas from Norway and LNG from Qatar.

New forms of energy, such as shale gas, wind and biomass can help the countries in which we operate to increase their opportunities for energy security and build a lower carbon future. However, they can also raise significant social and environmental concerns. We are working hard to ensure that all our gas production and energy generation activities are subject to consultation with both local communities and national level stakeholders. Such activities are carefully planned and managed to avoid adverse impacts. For example in 2012, we used specialised equipment to install cable ducts under the salt marsh for our Lincs offshore wind farm.

MORE INFORMATION CAN BE FOUND IN THE CENTRICA ENERGY AND DIRECT ENERGY OPERATING REVIEWS ON PAGES **26** AND **32**.

Protecting biodiversity at our Lincs offshore wind farm

We recently installed a second export cable to transfer power to the shore. Careful installation was essential due to the sensitive environment which included a protected salt marsh site. After extensive dialogue with stakeholders we received permission to use a new technology – a special trenching tool with wide tracks that reduced ground pressure for use in the sensitive environment. The cable corridor began to show signs of recovery after only a few weeks. We will monitor the site frequently during the next five years.

Achieving reductions in carbon emissions

Centrica gives priority to managing its impact on climate change. It does this through helping customers reduce their energy usage and through investing in lower carbon power generation. We also address our own behaviour through setting targets for reducing carbon emissions from our property, vehicle fleet and travel.

Helping our customers reduce carbon emissions

Using energy more efficiently continues to be the most effective way for customers to reduce the amount of energy they use and therefore their carbon emissions. We promote energy efficiency mainly through providing customers with insulation to reduce heat loss from their homes and the installation of more efficient boilers. British Gas also provides products based on low carbon technologies including solar panels, heat pumps and biomass boilers which allow customers to heat and light their homes whilst producing lower carbon emissions. Over the past three years, we have enabled carbon savings downstream that are the equivalent of a 1.8GW wind farm. The UK Government's Green Deal offers customers financial help to make their homes more energy efficient and British Gas will be helping to deliver this.

Lower carbon power generation

To reduce the carbon emissions from power generation, the use of fossil fuel energy sources, in particular coal, must be reduced. In the UK, there has already been a substantial move towards lower carbon gas power generation. Further reductions can be achieved through renewable generation such as offshore wind. Nuclear generation in the UK also has an important role to play in lower carbon electricity generation. Centrica plans to maintain its interest in lower carbon power generation and to continue to invest where we have an economic advantage and see attractive returns. Our low carbon investments continue to come on line with first power generated from our 270MW Lincs offshore wind farm in 2012.

CORPORATE RESPONSIBILITY REVIEW CONTINUED

Safety is one of our core priorities The Centrica Board has direct oversight of our health and safety performance

Although we wish to develop further offshore wind farms, getting the relevant permissions is not straightforward and in 2012 our proposed Docking Shoal project did not receive approval on environmental grounds.

While we are not continuing with the nuclear new build, we will continue to provide our customers with lower carbon power through our 20% off-take from the UK's existing nuclear power stations.

We aim to reduce the carbon intensity of the power we generate. In 2012 our Group carbon intensity was 197g CO_2/kWh, compared to 220g CO_2/kWh in 2011, a 10% reduction. This was significantly ahead of our 2012 target of 270g CO_2/kWh and was mainly due to mothballing some of our gas-fired power stations in the UK for commercial reasons. Our future carbon intensity is expected to rise as the markets adjust and so our long-term aim of 260g CO_2/kWh by 2020 remains valid.

Managing the emissions from property, fleet and travel

We are reducing our emissions from our property, fleet and travel by raising awareness among employees, making offices more energy efficient, investing in lower-carbon vehicles and providing alternatives to business travel. Our target is to cut emissions from buildings, company vehicles and travel in our core business by 20% by 2015, from the 2007 baseline. In 2012, we achieved a 2% reduction year on year, a 21% reduction against the baseline. Carbon emissions from these activities were 91,988 tonnes.

Absolute carbon

We also measure our absolute emissions, which include emissions from our gas and oil operations, our electricity generation and the energy we use in our business activities. Our absolute carbon emissions in 2012 (scope 1 and 2 based on the Greenhouse Gas Protocol) were 7.2 million tonnes as compared with 8.1 million tonnes in 2011.

MORE INFORMATION CAN BE FOUND IN THE CENTRICA ENERGY AND DIRECT ENERGY OPERATING REVIEWS ON PAGES **26** AND **32**.

Making safety a core value

Safety is one of the Group's core priorities. The Board has direct oversight of our health and safety performance. Our operations are inherently hazardous and we fully accept our responsibility to protect the health and safety of our employees, contractors, customers and the wider public.

Reinforcing a safety culture at Centrica

We continue to raise our standards of performance through strong leadership and on-going programmes to raise awareness and reinforce a positive and proactive safety culture across all our businesses. We have put particular emphasis on process safety in our upstream operations and the safety of the public and our engineers in our downstream businesses, through training and the introduction of more rigorous monitoring and assurance.

Our process safety metrics are reported regularly to the Executive Committee. We have had no significant process safety events in 2012.

To monitor the personal safety of our employees and directly-managed contractors, we track our standard lost time injury frequency rates (LTIFR) and total recordable injury rates (TRIR). Initiatives across the Group in 2012 led to a reduction in Group LTIFR to 0.20 per 100,000 hours worked, down from 0.25 in 2011. Our TRIR was 1.42 per 100,000 hours worked in 2012, an improvement of 14%.

We have continued our focus on road safety and reducing vehicle accidents and our low severity incident rate has reduced by 33% to 5.0 per million km driven. We did, however, have six incidents which we defined as high severity and, although these represented a 40% reduction on 2011, they still emphasise the need for ongoing rigour in our road safety programmes.

There were no fatal incidents among Centrica's employees or associated third parties in 2012. We were very concerned that there were a number of particularly serious injuries, including two serious incidents in British Gas and Direct Energy. We are reinforcing our investigations and reporting processes to provide greater visibility of these events. We look to share understanding and learning from the incidents across the Group.

Our employees

We had an average of 38,642 employees in 2012 with a retention rate of 89.7% (2011: 89.5%). We work hard to make Centrica a rewarding place to work and

MORE INFORMATION CAN BE FOUND IN THE OPERATING REVIEW ON PAGES **22** TO **35**.

have continued our focus on skills, development and employee engagement.

Skills and development

Continuous learning and development is essential to ensure employees have the opportunity to fulfil their potential and are equipped to help grow our business and implement our strategy. Developing our leaders is crucial. Our talent boards, general management programme and leadership master classes are designed to identify and nurture high-potential managers. In Centrica Energy, 'CE Way Labs' were held which helped embed the 'CE Way' culture and values and allowed people to share experiences. The 'CE Way' has also been linked to the performance management process.

Employee engagement

In 2012, as planned, we conducted a Group-wide employee engagement survey. This is an important process which informs management of the collective views of employees so that we can improve engagement in the future. Our overall engagement score, benchmarked against our peers, saw a slight decline but was still above median. Given the changes that had taken place in the business, this was not surprising and through the year we undertook a number of initiatives to engage our employees. These included our 'Extraordinary you' programme which brought together over 9,000 British Gas engineers through 104 events in 23 locations to focus on their critical role in delivering excellent customer service.

Employees receive regular updates on Company news and performance by a variety of methods. This includes newsletters, emails, online sites and face to face meetings with members of the Executive Committee.

Eligible employees are regularly encouraged to participate in employee share schemes and we continue to see good rates of participation.

Organisational change

We have had to make some organisational changes to reflect the changing nature of our business, which has resulted in some 2,459 employees leaving the Group. Achieving such change is never an easy process and we made every effort to support those affected, wherever possible seeking to redeploy people in the business or supporting them in finding other work.

CONTINUOUS LEARNING AND DEVELOPMENT IS ESSENTIAL TO ENSURE EMPLOYEES HAVE THE OPPORTUNITY TO FULFIL THEIR POTENTIAL

89.7%

Employee retention rate for 2012

Diversity

We aim to provide an inclusive and diverse workplace and are committed to equal opportunity. We will not tolerate discrimination against any group.

We give full and fair consideration to applications for employment made by disabled people. If an employee becomes disabled, wherever possible we offer support, retraining, equipment and facilities to help them stay with us. In addition, we operate policies to help ensure there are fair promotion opportunities for disabled employees.

We encourage the retention and recruitment of older people, recognising the valuable experience they bring. Improving women's representation at all levels is a priority. We focus on female leadership training, recruitment, flexible working and employee network groups.

Community investment

In 2012, we contributed £233.6 million directly to supporting vulnerable customers and community and social projects. The majority of our contributions were through mandatory programmes such as the Warm Home Discount and the Community Energy Saving Programme. We also contributed £9.3 million to charitable organisations using the London Benchmarking Group methodology, including establishing strategic partnerships such as between British Gas and Shelter.

Mary Francis

Mary Francis CBE
Chairman of the Corporate Responsibility Committee
27 February 2013

ONLINE

Read more about our CR activities at centrica.com

PRINCIPAL RISKS AND UNCERTAINTIES

"ASSESSING AND MANAGING RISK IS A FUNDAMENTAL PART OF DAY TO DAY BUSINESS MANAGEMENT ACROSS CENTRICA."

Nick Luff
Group Finance Director

The risks we face in a rapidly changing energy landscape continue to evolve over time. A number of measures helped to mitigate those factors in 2012.

2012 key risks

Our principal risks and uncertainties during 2012 are summarised below, together with a brief summary on how these have moved or been managed throughout the year.

Health, safety and environment

Safety is one of our core priorities and we continue to target risk and impact reduction. In 2012 we reduced the lost time injury frequency rate (LTIFR) and achieved significant safety milestones at a number of operations. For example, Centrica Storage had no lost time incidents recorded for more than five million man hours of work.

Brand and reputation

The Group continued to change and improve the offering to customers and provide more transparent billing, and continued to roll out an Energy Regulation Compliance Programme.

Legislation and regulation

Our contact programme with key stakeholders helps us respond to new initiatives and external market changes. As part of the Retail Market Review (RMR), we are engaging with Ofgem over their proposals, and we are also engaging with the Department of Energy & Climate Change (DECC) with reference to Electricity Market Reform (EMR).

Strategic growth

The Group continued to pursue a range of options across the gas value chain and undertook significant investment through upstream and North American acquisitions, including assets in the North Sea of £1.2 billion to secure an affordable energy supply.

Commodity prices

We continued to seek long-term supply arrangements and develop our asset portfolio. Increased wholesale and other costs forced us to raise gas and electricity prices in November. However, we worked to make tariffs easier to understand.

Competition

Affordability is a key issue for customers. We invested significantly in systems to ensure our customer service levels continue to improve and remain competitive. British Gas extended eligibility under the Warm Home Discount and developed offers with affinity partners, such as Sainsbury's Energy.

Organisational change

We successfully moved our North American headquarters from Toronto to Houston. We made plans to recruit 1,000 British Gas energy apprentices in connection with the significant investment in smart energy. In respect of the upstream business we will create significant numbers of jobs in construction and across the supply chain for the Cygnus project, to develop the largest gas discovery in the Southern North Sea for 25 years.

Supply chain

We reviewed and refined governance processes and many suppliers signed our responsible procurement clauses. Furthermore, we linked supplier audit activity to low cost country sourcing.

Information security, intellectual property and assets

We operate in a complex computing environment and the threat of cyber attack against our industry remains high. We invested in the transition of our data centres and improved our system of internal controls.

2013 presents our organisation with more challenges. Strong governance and a clear risk strategy equip us for uncertainties ahead.

2013 principal risks and uncertainties

The following risks could impact our future performance. The list is not exhaustive and items are not prioritised. The list, and the nature of the risks, may change during the year.

Health, safety, security and environment (HSSE)

What are the risks?
We face four principal categories of HSSE risks associated with our operations:

- an incident resulting in one or more fatalities or multiple injuries at an owned, operated or other facility where the organisation has an interest;
- an incident which results in significant environmental damage or compliance breach;
- an incident which results in a fatality or major injury to members of the public; and
- a security event, requiring activation of our crisis management plan and/or business continuity plan.

Such risks may result in widespread distress and harm, significant disruption to operations and damage to our reputation. The cost related to the recovery, clean up and/or resultant litigation could have a material financial impact.

Actual incidents, precautionary plant closures or suspension of activities on HSSE grounds could lead to loss of production or service and impact profits. Our operations have many inherent hazards, particularly related to exploration and production, power generation and offshore activities.

We also have non-controlled interests in organisations with inherently high hazards, relating to the exploration and production of oil and gas and nuclear power generation.

How do we manage these risks?
The Board and Executive Committee oversee HSSE risk and consider it one of our core priorities. We provide regular training to all our employees and colleagues, including those in our customer-facing businesses and those working to ensure the safe operation of our assets.

We remain committed to understanding, managing and reducing the environmental and ecological impacts of our activities through innovation, technology and cultural change.

In 2012, business unit Health, Safety & Environment (HS&E) plans were put into place alongside the Group audit programme. These risks are tracked by control effectiveness assessments and performance metrics. We reviewed our HS&E audit operating model to ensure the 2013 risk-based audit programme accurately assesses compliance and provides assurance to the Board and Audit Committee. Security intelligence and operating procedures, as well as crisis management and business continuity plans, are regularly reviewed.

PRINCIPAL RISKS AND UNCERTAINTIES CONTINUED

Brand and reputation

What are the risks?

As highlighted in the Corporate Responsibility Review, our ambition is to be the most trusted energy company. Failure to follow our global business principles of operating professionally, fairly and with integrity could harm our reputation, as could real or perceived customer service failings. Rising prices, increased political pressures and deep recessionary impacts have all increased the level of media coverage.

We need to ensure that we clearly communicate our future strategy to key stakeholders, in order to avoid an adverse reaction and loss of confidence in the Group.

Social media now allows consumers and pressure groups to mount damaging direct action and other campaigns more readily than before.

Failure to restore public confidence could impact Group revenues. Public exposure to criticism could damage our brand, increase governmental or regulatory intervention and reduce access to financial capital.

How do we manage these risks?

The Group supports transparency, fairness and competition and has taken action to make bills clearer and to work with our customers to improve awareness about energy efficiency. We meet regularly with the media, government, NGOs, investment community, regulators and consumer groups as part of our relationship management strategy. Although some sections of our key stakeholders hold an 'anti energy' position, our Honest Conversation and Customer Board initiatives are recognised by industry critics as helping stakeholders understand the energy market.

The Group, through gas and power assets, offices and call centres and the 10 million visits engineers make to homes in the UK and North America every year, is very much part of local communities. We act as a responsible company within these communities and continue to help vulnerable customers.

In Ontario, Direct Energy launched a new customer promise with a commitment to see all customers without heat the very same day. This was based on the success of a similar service developed in the UK. Direct Energy is also a key supporter of a programme to provide people going through financially difficult times with assistance in paying their household bills.

Legislation and regulation

What are the risks?

Energy markets in the UK, North America and mainland Europe are closely regulated. Legal or regulatory changes could impact our ability to achieve financial goals.

New financial regulation was introduced in the US and Europe as a result of the global financial crisis. As part of this we are still awaiting finalisation of the rules and regulations in Europe and in the US, under the Dodd-Frank Act. These could adversely affect the manner in which we currently deal in the commodity markets. Governments and regulators, often under public pressure, have also stepped up levels of enforcement and intervention.

Retail sector competitiveness continues to face regulatory scrutiny, as the costs of higher wholesale commodity prices are passed on to customers, just as disposable incomes are falling and deepening recessionary impacts continue to be felt. In the UK, Ofgem's updated RMR proposals could introduce significant risk to our downstream business and reduce innovation and affordable choice for customers.

In North America, the legal and regulatory framework is primarily set at a provincial or state level, making generalisations difficult and our entry into new markets needs to be assessed on a case by case basis.

Public statements made by governing political bodies can cause concern. One of the challenges would be the abolition of existing or future 'green' subsidies, as occurred in the UK solar industry and in other energy sources around the world, such as the end of free carbon allowances in 2012 which will impact our upstream business.

Such developments may have a material adverse effect on our business, operations, financial condition and ability to meet long-term growth aspirations, especially if any case of compliance failure receives extensive media coverage.

How do we manage these risks?

We proactively engage stakeholders, including governments and regulators in the UK and North America, to help shape these proposals and manage the risks they present. The Centrica Policy Group met regularly during 2012, setting Group-wide positions on each issue.

In 2012, we formed a Corporate Reputation Group to discuss threats from legislative and regulatory proposals. We also continued to roll out our Energy Regulation Compliance Programme.

Business Review – Principal Risks and Uncertainties

Strategic growth

What are the risks?

Strategic issues, including capital investment in mergers, acquisitions, disposals, market position, climate change, sustainable development and new technologies, are affected by the global economy. As we implement our refreshed strategic priorities to deliver our vision to be the leading integrated energy company with customers at our core, we face an increasingly uncertain environment. Challenges include the intensifying uncertainty in the world economy reflected by concerns over further economic deterioration, pressure from higher wholesale prices, increased competition, reduced demand and recessionary impacts, all of which contribute to making market conditions challenging.

The economic condition of the countries and markets in which the Group operates, namely the UK and North America, are of concern, with the extent and timing of recovery uncertain. The UK entered a double-dip recession during 2012, with the threat of an unprecedented triple-dip in 2013. The US experienced the potential for a 'fiscal cliff' and the proximity of further 'fiscal cliffs' in 2013 exists with the possibility, from the interconnected global financial systems, of this not only impacting our overseas operations but also the Group as a whole.

Decisions on the future of energy markets also pose risks to our existing and future operations. The UK Government's preference for converting coal power stations to co-firing biomass rather than building dedicated biomass facilities led us to end our investment in dedicated biomass power station projects. The US President's re-election indicated continued support for all domestic energy sources – shale, power generation including nuclear, renewable, carbon capture and storage – although specific details remain uncertain.

The rise of the digital economy is adding to competitive pressures and with the internet entering a second phase dominated by mobile devices, the barriers to market entry are falling and customer loyalties can change swiftly. In the UK market, a significant number of our customers have changed in line with this, as they now choose to deal with us through accessing digital channels, such as the British Gas website and smartphone applications. Smart meters represent one of the biggest changes in the retail energy market since the 1970s and British Gas will operate not only in an energy market but in an energy services and advisory market open to non-traditional players.

How do we manage these risks?

The Group pursues a range of strategic investment options across the gas value chain and in different geographies, to both deepen our customer relationships and secure the Group's future energy requirements.

In 2012, we invested £2.7 billion to secure energy supplies and increase energy reserves. In addition, our investment in the Cygnus project, when complete and at peak production, will meet the energy needs of nearly 1.5 million UK homes. We continue to seek industry partnerships to supply the UK with gas and three such supply deals have been signed since 2011.

In North America, the Group continues to deliver on its priorities. The residential, business and services footprint has grown, helping the upstream business perform well despite low gas and power prices.

We aspire to lead in the roll-out of smart meters to give consumers insight into how smart products will transform the way they understand their energy use. We are market leader in the supply for electric vehicle charge points and the Group continues to offer expertise in energy efficiency through domestic energy efficiency surveys and home insulation. Furthermore, the Group is mindful of the need to keep abreast of emerging technologies and the potential impact on the smart connected home of the future and as such we maintain links with technology experts to give us further advantage.

PRINCIPAL RISKS AND UNCERTAINTIES CONTINUED

Commodity costs

What are the risks?

Volatile commodity costs affect our ability to price competitively and meet profit targets. The Group buys a significant proportion of the gas to supply Britain's needs. This position sets the Group apart from the other counterparts in the UK market. To maintain supply and protect against possible price increases much of this is procured in advance in order to ensure a balanced supply and demand portfolio. Mild weather could reduce demand, leaving the Group with a surplus of gas which would have to be sold back to the wholesale market at a loss. This could contribute to customer bills not dropping when wholesale prices later fall.

There has been a significant impact from shale gas in North America where an immediate effect has been to lower wholesale gas prices in the US and weaken the traditional links between gas and oil prices. Such an emerging energy source could influence global energy markets over time, with the surplus of gas affecting the current liquefied natural gas (LNG) sector in particular.

Investment decisions key to Group strategic growth plans, particularly in respect of upstream assets such as gas fields or power stations, are based on evaluations underpinned by forecasts of longer-term commodity price development. These reflect prevailing market prices and are supplemented by assessments of underlying industry fundamentals.

Assets, including goodwill, may be impaired if discounted future cash flows from an asset are insufficient to cover its cost on the balance sheet. The excess asset cost on the Group balance sheet will be provided against and charged to the Group income statement. The cash flows of assets are sensitive to changes in:

- commodity prices;
- discount rates;
- reserve estimates/useful economic life;
- capital expenditure/operating expenditure assumptions (including changes in decommissioning estimates); and
- operational performance.

There are also a number of contractual capacity contracts, the economic value of which depends on volatile spread relationships.

How do we manage these risks?

The Group has an active hedging programme and tracks supplier risks through robust governance frameworks. Strategic investment decisions are made within a capital allocation framework designed to ensure that proposals are rigorously evaluated prior to acquisition and that they meet Board-approved financial criteria over the life of the project. The gas supply relationships with Statoil, Qatargas and Gazprom, the acquisition of additional assets and the securing of new licences for exploration blocks are examples of how we continue to develop our portfolio.

Change management

What are the risks?

The level of change experienced by our business is significant, deriving from:

- capital projects;
- IT change programmes; and
- organisational change.

We assess large capital projects as a means of growth. Such large-scale initiatives carry complexity and could result in the Group entering new markets, whilst exposing us to the risk of build quality issues, cost and timetable overruns, unsuccessful development of partnership opportunities and health, safety, security and environmental failures.

Internal IT change programmes are equally large and complex. Work on existing systems carries the risks of:

- trying to deliver too much change and over-stretching resources;
- change being completed but systems integrity being undermined and threatening business continuity; and
- cost overruns and/or expected benefits not being realised.

Organisational change stems from internal restructuring as we drive to make our business as efficient and effective as possible, without detriment to our levels of customer service. Our recent announcements mean that the Group will face a period of increased change activity in 2013.

How do we manage these risks?

Change is a constant in any successful organisation. The Group continues to change and adapt to remain competitive and provide the best service at the lowest cost. We address difficult decisions and challenging situations head on in order to provide energy to Britain's homes and businesses.

Change activity is managed through a combination of project/programme boards and regular review at both a business unit and executive level. In 2012, we created a project management directorate to improve governance of large capital projects in our upstream business.

We also assess carefully the overall cumulative impact of the level of change across the organisation at any one time.

Information security

What are the risks?

Effective and secure information systems are essential for efficient management and accurate billing of customers, upstream operations and energy trading and hedging activities. The confidentiality, integrity and availability of our information systems could be affected by:

- accidental or deliberate exposure of share-price sensitive information, customer or employee and contractor personal data;
- viral effect of employees, crusader consumers or 'hacktivist' groups using social media channels that expose the Group to legal liabilities, damage our reputation or disclose confidential information;
- accidental or deliberate changes to financial and other data the Group relies on;
- lack of availability of systems due to inadequate infrastructure and data-recovery processes; and
- an external online attack that renders the Group unable to conduct normal business activities and/or results in the loss or exposure of personal data, intellectual property or other confidential information or the disruption of control systems.

The threat of cyber attacks against our industry continues to escalate to similar levels experienced by government agencies and financial institutions. There could be multiple sources of motivation for these attacks. These risks, however, which could arise from inadequate or inconsistent implementation of IT security controls, could seriously affect the Group's reputation, lead to legal action and/or outages that could cause financial and operational loss. The US and EU data privacy proposals increase the implications of such risks materialising, due to proposals around public notification of any data breach and the scale of associated fines for non-compliance.

How do we manage these risks?

Controls include network segregation, monitoring, storage system access restrictions, regular third party security reviews and vulnerability assessments of infrastructure and applications. Our Group Information Systems (IS) risk team monitors and reviews adherence to the IS risk policy and works with the UK Government to exchange information and threat intelligence between government agencies and the energy sector.

Business continuity plans are in place to manage significant outages or interruptions. To improve efficiency, the Group continues to invest in systems, supported by strong project management, to minimise the associated implementation risk. In 2012, the Group continued to implement IS programmes, with specific efforts in North America to consolidate the systems of new acquisitions.

PRINCIPAL RISKS AND UNCERTAINTIES CONTINUED

People

What are the risks?

Key to our ability to successfully deliver business plans and strategic growth is the attraction, retention and succession planning of senior management and individuals with key skills. This applies to customer service, the delivery of new systems and in particular to areas where there is strong competition for technical and project management capability, such as our upstream business.

As we continue to change, the business must be organised in the most effective and efficient way possible to ensure its cost base is as low as possible, so that we can offer customers competitive prices and products. This includes both cultural and behavioural change as well as ambitious technical-change programmes.

As part of this, the Group also needs to maintain good relations with trade unions, primarily the Centrica Energy upstream business operational workforce and British Gas engineers. There is a risk that industrial relations with the GMB and/or UNISON fail or become ineffective as a result of a breakdown in negotiations over employment terms or as a response to widespread union unrest in the UK.

Failure to maintain a high calibre, engaged and stable workforce could compromise achievement of the Group's strategy and could have a material adverse effect on its business, results of operations and overall financial condition.

How do we manage these risks?

We regularly review our organisation to make sure that people are empowered to make the right decisions at the right time and to look for ways to work better, smarter and safer.

We regularly review the capability of the organisation to deliver our strategic objectives. An extensive exercise has been undertaken in critical areas to ensure we have the right capabilities to deliver our plans for growth and innovation.

In 2012, reward reviews were carried out in specific areas to retain key skills and prevent the possibility of an escalation in attrition.

The Group invests in developing all employees, including technical, behavioural and leadership skills. The Group engages with unions on restructuring and issues that could impact terms and conditions and provides channels for employees to discuss concerns. Human Resources is involved in merger and acquisition activity to ensure that, following integrations, we retain key attributes and recruit the right talent, especially in an emerging market.

FURTHER INFORMATION

Risk management processes on pages **58** to **60**.

Financial risk management on pages **111** to **114**.

HS&E reporting and activities on page **42**.

Governance

Contents

51 Directors' Report – Governance

52 Corporate Governance Report

52 The Board

54 Board Performance

54 Board Committees

- 55 Audit Committee
- 56 Nominations Committee
- 56 Remuneration Committee
- 57 Corporate Responsibility Committee
- 57 Executive Committee
- 57 Disclosure Committee

58 Relations with Shareholders

58 Risk Management and Internal Control

60 Going Concern

60 Directors' Responsibility Statement

60 Disclosure of Information to Auditors

60 Independent Auditors

61 Remuneration Report

61 Letter to Shareholders

62 Remuneration Summary

64 Remuneration Policy

- 64 Total Remuneration Package
- 66 Executive Directors' Remuneration
- 67 Non-Executive Directors' Remuneration

68 Remuneration Statement

- 68 Remuneration Committee
- 68 Executive Directors' Remuneration
- 69 Non-Executive Directors' Remuneration
- 69 Statutory Disclosures
- 70 Remuneration Tables
- 75 Changes since 1 January 2013

76 Independent Auditors' Report – Group

Board of Directors' and Senior Executives' biographies can be found on pages 152 and 153 and Other Statutory Information can be found on page 154 within the Appendix to the Directors' Report.

CORPORATE GOVERNANCE REPORT

"AN ORGANISATION IS DEPENDENT UPON ITS MANAGEMENT AND STRUCTURE FOR THE EXECUTION OF STRATEGY AND ITS CULTURE FOR THE WAY IN WHICH ITS RESULTS ARE ACHIEVED."

Sir Roger Carr
Chairman

This year, the Company is reporting in accordance with the UK Corporate Governance Code (the Code) introduced in June 2010 which sets out standards of good practice in relation to board leadership and effectiveness, remuneration, accountability and relations with shareholders. A copy of the Code is available from the UK Financial Reporting Council (FRC). The Company complied fully with the provisions set out in the Code throughout the year.

The Chairman's Statement on pages 5 to 8 discusses the Company's corporate culture and practice as well as Board composition, diversity, succession planning and evaluation. Details of the Company's business model and strategies for delivering objectives are set out in the Business Review on pages 9 to 50. The Company's Corporate Governance Report is set out on pages 52 to 60.

During the last few years, there have been a number of reviews and consultations on governance matters. Centrica takes an active interest in such developments and will continue to do so. In September 2012, the FRC published a revised Code which the Company fully supports. While the Company will be reporting in accordance with the revised guidance in its 2013 Annual Report, the Board have taken into account the revised provisions when preparing this Report.

The Board

Board of Directors

The Board believes that good corporate governance contributes to Centrica's performance. A clearly defined framework of roles, responsibilities and delegated authorities is in place and this supports the Board's aim to deliver sustainable growth for the benefit of shareholders, employees and customers. The findings of the recent Board evaluation continue to demonstrate that the Directors consider that the Board leads and controls the Group effectively, has a robust governance structure and that no individual or small group of individuals dominate the Board's decision-making.

The powers of the Directors are set out in the Company's Articles of Association (Articles), which are available on the Company's website. The Articles may be amended by special resolution. In addition, the Directors have responsibilities and duties under legislation, in particular the Companies Act 2006.

The Board has a schedule of matters specifically reserved for its approval which it reviewed against best practice in December 2012 and concluded that no changes were necessary. A summary is shown below and the full schedule is available on the Company's website.

The Board is responsible for:

- development of strategy and major policies;
- the Group's corporate governance and system of internal control;
- reviewing performance;
- approving interim dividend payments and recommending final dividend payments;
- approval of the annual operating plan, financial statements and major acquisitions and disposals;
- the Group's corporate responsibility arrangements including health, safety and environmental matters; and
- the appointment and removal of Directors and the Company Secretary.

The Board recognises that its Non-Executive Directors have other interests outside of Centrica and so, each year, the Chairman and each Non-Executive Director provide assurance to the Board that they remain fully committed to their respective roles. The Board considers these assurances and is satisfied that each can dedicate the necessary amount of time to attend to the Company's affairs.

Governance – Corporate Governance Report

Board meetings

The Board holds regular scheduled meetings throughout the year and in 2012 there were eight scheduled meetings of the Board.

The Board continuously assesses and reviews key priorities and business issues for the Group over the short, medium and longer term. Comprehensive papers are presented to the Board which facilitate meaningful debate on the performance and future direction of the Company.

All Directors are expected to attend all Board and relevant Committee meetings. Details of attendance by Directors at Board meetings during 2012 are set out in the table below and their attendance at Committee meetings, where appropriate, is included on pages 55 to 57. Where a Director was not in attendance, this was due to other prior work commitments. Directors who were unable to attend specific Board or Committee meetings reviewed the relevant papers and provided their comments to the Chairman of the Board or Committee, as appropriate. In addition, any Director who misses a meeting will, as a matter of course, receive the minutes of that meeting for future reference.

	Number of meetings	Meetings attended
Sir Roger Carr (Chairman)	8	8
Sam Laidlaw	8	8
Phil Bentley	8	8
Margherita Della Valle	8	7
Mary Francis	8	8
Mark Hanafin	8	8
Lesley Knox	8	7
Nick Luff	8	8
Andrew Mackenzie	8	7
Ian Meakins	8	7
Paul Rayner	8	8
Chris Weston	8	8

As part of its responsibilities, the Board approves and monitors the development of the Group's strategy. In addition to the discussions at the scheduled Board meetings, in 2012 the Board held two additional meetings devoted specifically to strategy. In 2012 the Board conference reviewed the progress against our strategic priorities and debated the challenges within our current markets. The Board discussed options for the new strategic direction for the Group and started to develop the priorities introduced on page 11. Key strategic considerations included:

- the competitive landscape and market conditions;
- a further interim assessment of our investment in new nuclear;
- an assessment of growth options across the Group and investment opportunities in exploration and production, midstream (including UK gas storage), power generation and downstream; and
- a review of different capital allocation options, including an assessment of long-term financial performance and capacity under various scenarios of the business and the optimal use of capital, including whether any capital should in future be returned to shareholders.

Board constitution and appointments

The Board comprises a good balance of Executive Directors and independent Non-Executive Directors which promotes thorough consideration of the important issues facing Centrica and the Group's performance. The roles of Chairman and Chief Executive are separate, formalised in writing and have been approved by the Board. They are available on the Company's website, together with an explanation of the roles of the Non-Executive Directors.

As discussed in the Chairman's Statement, the Non-Executive Directors play a key governance role and bring an external view to the Board's deliberations through their knowledge, experience and insight from other sectors. As part of its annual review of corporate governance, the Board considered the independence of each Non-Executive Director, other than the Chairman, against the criteria in the Code and determined that each Non-Executive Director remained independent. During the year the Non-Executive Directors, including the Chairman, met independently of management. In addition, the Senior Independent Director met with the independent Non-Executive Directors in the absence of the Chairman to appraise the Chairman's performance.

A formal, rigorous and transparent process is followed during the selection and subsequent appointment of new Directors to the Board. However, there have been no changes to the composition of the Board during 2012. Board composition planning, however, is discussed in the Chairman's Statement on page 7.

The Companies Act 2006 and the Articles require the Board to consider any potential conflicts of interest. The Board considers and, if appropriate, authorises each Director's reported actual and potential conflicts of interest regularly. The conflicts of interest register is reviewed at least annually by the Board. Each Director abstains from approving their own reported conflicts.

The Board has agreed that each Director shall stand for re-appointment at each Annual General Meeting (AGM).

Details of the Directors of the Company are set out in the Chairman's Statement on pages 6 and 7 with their biographies on pages 152 and 153. Details of Directors' service contracts or letters of appointment, in the case of Non-Executive Directors, emoluments and share interests are set out in the Remuneration Report on pages 61 to 75.

Directors' indemnities and insurance

In accordance with the Articles, the Company has granted a deed of indemnity, to the extent permitted by law, to Directors and the General Counsel & Company Secretary. Qualifying third party indemnity provisions (as defined by section 234 of the Companies Act 2006) were in force during the year ended 31 December 2012 and remain in force. The Company also maintains directors' and officers' liability insurance for its Directors and Officers.

ONLINE

Use your smartphone or tablet to scan this QR for instant access to the Directors' biographies

CORPORATE GOVERNANCE REPORT CONTINUED

Board performance

Board evaluation

The Board considers the annual review of the Board, its Committees and Directors as an essential part of good corporate governance, with the use of an external facilitator at least once every three years. Over the last ten years, the Company has employed Egon Zehnder on two occasions, JCA Group and in 2011, Independent Board Evaluations (IBE). On each occasion, the Board has received positive reports and has adopted recommendations to improve Board, Committee and individual Director performance.

A full discussion on the implementation of IBE's findings during 2012 and the internal evaluation conducted in December 2012 can be found in the Chairman's Statement on page 8.

Board development

All new Directors appointed to the Board receive a comprehensive induction programme tailored to meet their individual needs. The Chairman and General Counsel & Company Secretary are responsible for delivering an effective induction programme for newly appointed Directors, specially tailored to meet the individual's requirements. This will comprise briefings from members of the Executive team on key areas of the business including the internal audit function, an overview of the Group's risk management processes, the key risks facing the business and a briefing in respect of the corporate governance framework within Centrica.

Ongoing development and training is also provided to all Directors at Board and Committee meetings. During the year, Directors received regular updates and presentations on changes and developments to the business and to the legislative and regulatory environments in which the Group operates. In particular, the Board was briefed on the following key issues during 2012:

- the impact of changes in Government policy on the green agenda and social costs;
- progress with and the impact of the Retail Market Review (RMR) and Electricity Market Reform (EMR);
- Centrica's improved approach to managing major capital projects;
- demonstrations of the latest developments in British Gas smart technology;
- progress within the Goup's FSA regulated businesses (British Gas Insurance and UK Midstream);
- company law, corporate governance, reporting and remuneration reporting developments; and
- health, safety and environmental governance and strategy.

The Directors have full access to the advice and services of the General Counsel & Company Secretary, who is responsible for advising the Board through the Chairman on corporate governance matters. They are also able to seek independent professional advice at the Company's expense in respect of their duties.

Board committees

The Board operates six Committees to oversee the standards of the Group: Audit, Nominations, Remuneration, Corporate Responsibility, Executive and Disclosure. The Committees are supported in the same way as the Board in order to ensure information flows in a timely, accurate and complete manner.

All of the independent Non-Executive Directors are members of the Audit, Remuneration and Nominations Committees, with the exception of Andrew Mackenzie who is not a member of the Audit Committee. The Board reviews annually each Committee's terms of reference and membership against best practice as well as taking into account any relevant changes in circumstances. In December 2012, the Board approved minor revisions to the terms of reference for the Audit Committee. All other terms of reference remain unchanged. The full written terms of reference for the Committees can be found on the Company's website.

Minutes of Committee meetings are made available to all Directors and the Chairmen of each Committee provide regular updates to the Board.

A chart setting out the Company's Board and Executive Committees' structure is below. The responsibilities of each Board Committee, its membership and the key issues considered by each one during 2012 are set out in the following Committee reports.

Board governance structure

Audit Committee

The Audit Committee's key function is to review the effectiveness of the Company's financial reporting and internal controls together with the procedures for the identification, assessment and reporting of risks.

The Committee is authorised by the Board to:

- monitor the integrity and audit of the Financial Statements;
- review the internal financial controls, internal control and risk management systems;
- monitor and review the effectiveness of Internal Audit;
- establish and oversee appropriate whistleblowing and fraud prevention arrangements; and
- establish and oversee the relationship with the external auditors, including any non-audit services.

Key issues reviewed by the Audit Committee

During 2012, the Committee considered:

- the 2011 preliminary results, 2011 Annual Report and 2012 half year results;
- the critical accounting judgements (see note 3 of the Financial Statements on pages 83 to 85), including the impairment reviews of power stations, upstream oil and gas assets, planned gas storage facilities, onerous contracts, nuclear new build investment and goodwill;
- Directors' judgements on exceptional items (see note 7 of the Financial Statements on page 92);
- progress on aligning assurance activities to improve the quality and delivery of internal controls and assurance;
- the Internal Audit strategy and scope of activities;
- the independence, objectivity and fees of the external auditors and scope of audit and non-audit services;
- the new UK Corporate Governance Code; and
- adherence across the Group to key regulatory and compliance regulations, including compliance with the undertakings in respect of Centrica Storage Limited.

Membership and attendance during the year:

	Number of meetings	Meetings attended
Paul Rayner (Chairman)	4	4
Margherita Della Valle	4	4
Mary Francis	4	4
Lesley Knox	4	4
Ian Meakins	4	3

The Board has determined that each member of the Committee is independent. In accordance with the Code, Paul Rayner and Margherita Della Valle are identified as having recent and relevant financial experience. As noted in the Chairman's Statement on page 8, it is intended that Margherita Della Valle will assume chairmanship of the Audit Committee in July 2013.

The Committee members participated in two training sessions during the year: one in July 2012 facilitated by members of Centrica Energy's management team focusing on the management of Centrica Energy's midstream and trading risks and one in November 2012 in respect of the Direct Energy residential business.

The Committee considers annually the scope, fee, performance and independence of the external auditors as well as whether a formal tender process is required. In accordance with the transition provisions of the revised Code, the Group will perform an external audit tender process before 2017. During the year, at the Committee's request, PricewaterhouseCoopers (PwC) performed a detailed review of their audit and submitted a formal proposal for re-appointment. To assess the effectiveness of the external auditors, the Committee considered feedback on the audit process gathered through a survey. This included questions on the fulfilment of the external audit plan and any variations, the external auditors' qualifications and resources, the robustness of the auditors in handling key accounting and audit judgements and the insightfulness of recommendations included in the external auditors' internal control report.

The Board considers it of prime importance that the external auditors remain independent and objective and as a safeguard against this being compromised, the Committee implemented and monitors a policy on the independence of external auditors, a copy of which is available on the Company's website. The policy details the appointment of external auditors, the setting of audit fees and the rotation of audit partner and staff. The policy also restricts the types of non-audit work that can be undertaken by the external auditors. The award of non-audit work, within permitted categories, is subject to pre-clearance by the Committee if the fee exceeds specified thresholds. The Committee is provided with reports of all non-audit assignments awarded to the external auditors and a full breakdown of non-audit fees incurred. A summary of fees paid to the external auditors is set out in note 32 to the Financial Statements on pages 120 and 121.

In accordance with International Standards on Auditing (UK & Ireland) 260 and Ethical Statement 1 issued by the Accounting Practices Board, and as a matter of best practice, the external auditors have confirmed their independence as auditors of the Company, in a letter addressed to the Directors.

PwC has been the external auditor of the Group since the demerger of Centrica in 1997. The Committee makes recommendations through the Board to the shareholders to consider at the AGM, or at any time during the year, on the appointment, re-appointment or removal of the external auditors. There are no contractual obligations restricting the Group's choice of external auditors. Following the above review and having given full consideration to the performance and independence of the external auditors, the Committee has recommended to the Board that a resolution to re-appoint PwC be proposed at the 2013 AGM and the Board has accepted and endorsed this recommendation.

CORPORATE GOVERNANCE REPORT CONTINUED

Nominations Committee

The Nominations Committee ensures there is a formal and appropriate procedure for the appointment of new Directors to the Board. The Committee is responsible for leading this process and making recommendations to the Board.

The Committee is authorised by the Board to:

- make appointment recommendations to the Board for the appointment, re-appointment or replacement of Directors;
- devise and consider succession planning arrangements for Directors and other senior executives; and
- regularly review the structure, size and composition of the Board and to recommend any proposed changes to the Board.

Key issues reviewed by the Nominations Committee

During 2012, the Committee considered:

- succession planning for the Executive Directors;
- a review of Non-Executive Directors whose length of service was more than six years;
- the relevant skills and criteria which would be required in respect of the search for a new Non-Executive Director with strong upstream experience in North America; and
- each of the Directors prior to the 2012 AGM and recommended that each of them be subject for re-election at the 2012 AGM.

Membership and attendance during the year:

	Number of meetings	Meetings attended
Sir Roger Carr (Chairman)	3	3
Sam Laidlaw	3	2
Margherita Della Valle	3	3
Mary Francis	3	3
Lesley Knox	3	2
Andrew Mackenzie	3	1
Ian Meakins	3	2
Paul Rayner	3	3

In addition to the above meetings, the Committee met with the Chief Executive and the Group Director, Human Resources to undertake an annual succession review for senior management.

THESE ISSUES ARE DISCUSSED IN MORE DETAIL WITHIN THE CHAIRMAN'S STATEMENT ON PAGES **5** TO **8**

Remuneration Committee

The principal role of the Committee is to determine and make recommendations to the Board on the Company's framework and policy for the remuneration of the Chairman of the Board, the Company's Executive Directors and other senior executives.

The Committee is authorised by the Board to:

- determine total individual remuneration packages, authorise any contract of employment/letter of appointment and other terms and conditions for the Board and senior executives;
- approve the design of, and determine targets for, any performance related pay schemes for the Executive Committee and approve the total annual payments; and
- review the design of all share incentive plans for approval by the Board and shareholders.

Key issues reviewed by the Remuneration Committee

During 2012, the Committee considered:

- total remuneration, including a review of base pay for 2012;
- annual earnings of Executive Directors;
- an amendment to the Centrica Unfunded Pension Scheme (CUPS) for the Executive Directors;
- potential amendments to the performance targets of the Long Term Incentive Scheme (LTIS) and Deferred and Matching Share Scheme (DMSS); and
- the impact of changing legislation on the operation of the existing share schemes and developments in government and best practice proposals on executive remuneration.

The Committee regularly considers a number of items which, for 2012, included the performance and objectives under the Annual Incentive Scheme, the vesting and allocation awards for the LTIS and DMSS and the annual valuation of CUPS.

Membership and attendance during the year:

	Number of meetings	Meetings attended
Lesley Knox (Chairman)	5	5
Sir Roger Carr	5	5
Margherita Della Valle	5	5
Mary Francis	5	5
Andrew Mackenzie	5	5
Ian Meakins	5	3
Paul Rayner	5	5

The Board has determined that each member of the Committee is independent. No Director is involved in the determination of, or votes on, any matters relating to his or her own remuneration.

THESE ISSUES ARE DISCUSSED IN MORE DETAIL WITHIN THE REMUNERATION REPORT ON PAGES **61** TO **75**

Corporate Responsibility Committee

The role of the Corporate Responsibility Committee is to ensure that Centrica effectively manages its impact on society, the environment and the wider economy.

The Committee is authorised by the Board to:

- endorse the Group's Corporate Responsibility (CR) strategy, policies, processes and standards, assist periodic reviews of them and oversee the effectiveness of management's implementation;
- monitor performance against agreed KPIs and targets;
- review the framework for managing CR across the Group and its effectiveness; and
- review the effectiveness of Centrica's communications about CR strategy and performance externally and internally.

Key issues reviewed by the Corporate Responsibility Committee

During 2012, the Committee focused on:

- reviewing key CR performance indicators, in particular on environmental, health and safety and customer engagement metrics as well as key CR strategic priorities;
- specific CR issues in relation to each business unit, including CR aspects of topical and emerging energy issues such as bio-energy and shale gas;
- development of key business activities, including progress on further improving the management of responsible procurement within the business;
- reviewing the assurance provided by Deloitte LLP in respect of the CR report; and
- feedback received directly from members of the British Gas Customer Board on initiatives to improve engagement with British Gas customers.

Membership and attendance during the year:

	Number of meetings	Meetings attended
Mary Francis (Chairman)	3	3
Sam Laidlaw	3	3
Phil Bentley	3	3
Grant Dawson	3	3
Margherita Della Valle	3	3
Andrew Mackenzie	3	3
Chris Weston	3	3

The Executive Committee has overall responsibility for implementing CR strategy across the Group.

THESE ISSUES ARE DISCUSSED IN MORE DETAIL WITHIN THE CORPORATE RESPONSIBILITY REVIEW ON PAGES 39 TO 43

Executive Committee

The Executive Committee is responsible for the day to day management of the Group's operations within the limits set out in the Group's delegation of authority. The Committee also has a schedule of matters specifically reserved for its approval, including Health, Safety and Environmental policies and standards.

Key issues reviewed by the 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 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.

Membership and attendance during the year:

	Number of meetings	Meetings attended
Sam Laidlaw (Chairman)	11	11
Phil Bentley	11	11
Grant Dawson	11	9
Mark Hanafin	11	10
Nick Luff	11	11
Jill Shedden	11	11
Chris Weston	11	11

Disclosure Committee

The Disclosure Committee 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 Company comply with applicable legal or regulatory requirements.

Key issues reviewed by the Disclosure Committee

During 2012, the Committee considered the release of the 2011 preliminary announcement, the interim management statements in May and November 2012, the 2012 half year results and the release of announcements in respect of specific projects. The Committee also undertook a full review of the Group's control of inside information and compliance with the Model Code.

Membership and attendance during the year:

	Number of meetings	Meetings attended
Sam Laidlaw (Chairman)	7	7
Grant Dawson	7	7
Nick Luff	7	7

CORPORATE GOVERNANCE REPORT CONTINUED

Relations with shareholders

The Board recognises and values the importance of maintaining an effective investor relations and communication programme. The Board is proactive in obtaining an understanding of shareholder views on a number of key matters affecting the Group and receives formal investor feedback regularly.

During 2012, Centrica hosted presentations for the announcement of the Group's 2011 preliminary results and 2012 interim results. Attended by both Executive and Non-Executive Directors, the presentations were made to institutional investors and analysts, including representatives of many of the Group's largest shareholders. The presentation materials are available on the Company's website.

The Chief Executive and Group Finance Director also held regular meetings with the Company's major shareholders during the year. The Chairman and the Senior Independent Director attended the meetings at which the annual and interim results were presented to major investors and analysts. The Chairman of the Remuneration Committee also met with a number of the Company's major shareholders during the year to discuss our remuneration arrangements and will further engage in advance of any future changes. The Chairman continues to meet major institutional shareholders regularly in order to gain a first-hand understanding of their concerns and key issues and provides regular updates to the Board. In addition, the Board receives annually an Investor Perception Survey which covers strategy, management, investment approach, valuation, business performance and balance sheet management.

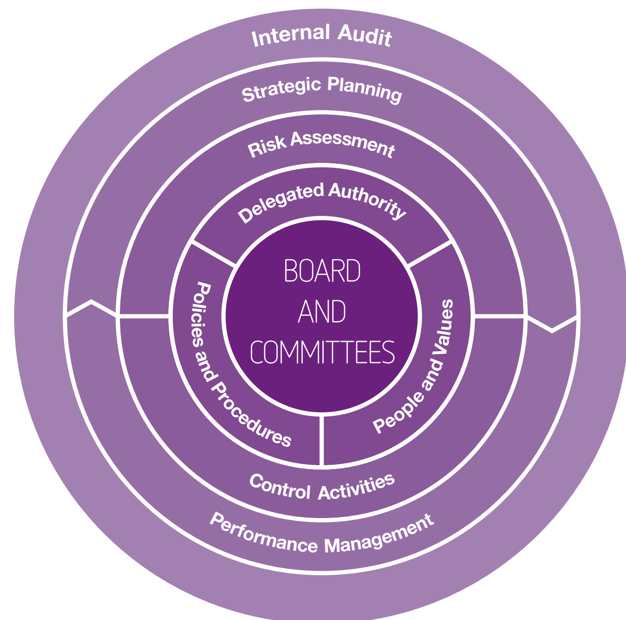
The Company's AGM provides all shareholders with the opportunity to develop further their understanding of the Company. Shareholders can ask questions of the full Board on the matters put to the meeting, including the Annual Report and the running of the Company generally. The Company intends to send to shareholders the Notice of AGM and any related papers at least 20 working days before the meeting. All Directors are invited to attend each AGM. At the AGM, the Chairman and the Chief Executive present a review of the Group's business. A poll is conducted on each resolution at all Company general meetings. All shareholders also have the opportunity to cast their votes in respect of proposed resolutions by proxy, either electronically or by post. Following the AGM, the voting results for each resolution are published and are available on the Company's website.

Mary Francis, the Senior Independent Director, is available to shareholders if they have concerns that contact through the normal channels has either failed to resolve or is deemed inappropriate.

Centrica's website contains up to date information for shareholders and other interested parties including annual reports, shareholder circulars, share price information, news releases, presentations to the investment community and information on shareholder services.

Risk management and internal control

The Board is responsible for the Group's system of internal control and risk management and considers this to be fundamental to the achievement of the Group's strategic objectives. The following diagram shows some of the key elements in the governance, risk and control framework by which Centrica's operations are conducted. The work of the Board and its Committees are at the heart of the process. The Board and its Committees set



objectives, performance targets and policies designed to achieve a balanced and transparent assessment of the risks facing the Group's operations and to measure the effectiveness of the key controls in place to manage them. The work of the Board is underpinned by clear delegations of authority, effective policies and procedures covering key areas of Group operation together with a set of business principles and processes which are communicated to Centrica's staff. In addition, mechanisms are in place to ensure that both strategic and operational risks are identified and assessed and that the controls designed to manage such risks are operating effectively. These mechanisms are reinforced through regular performance management and business reviews.

Lastly, it is important that the effectiveness of the framework is assessed impartially. There is, therefore, a programme of independent reviews by the internal audit function which is designed to cover the key processes and risks.

As with any such system, the processes are designed to manage rather than eliminate the risk of failure to achieve the objectives and can provide only reasonable, and not absolute, assurance against material misstatement or loss.

Details of the Group's principal risks and uncertainties are set out in pages 44 to 50 of the Business Review.

2012 developments

Centrica's risk management processes continue to evolve and during 2012 the following improvements were implemented:

- organisational changes including aligning a number of our risk, controls and audit functions to facilitate a more integrated approach to our risk and assurance activities. This will continue to evolve during 2013;
- the development and roll out of a risk universe, allowing for a more structured approach to risk identification which will eventually be used to drive a greater risk based approach to our audit planning activities;
- the focus on High Impact Low Probability (HILP) risk identification, with all business units updating and expanding upon their HILP registers for the Group's consideration;

Governance – Corporate Governance Report

- the publishing of a quarterly risk newsletter, covering both internal and external events, to identify emerging trends and to stimulate debate on changing or emerging risks which may cross over, or be related to our current and future activities;
- the introduction of a risk maturity model to assess the effectiveness of our risk processes across the different business units. This has enhanced the sharing of best practice amongst the risk community and allowed us to focus on mutual areas for improvement; and
- the assessment of the effectiveness of our risk management processes, a number of internal and external audits took place. These reviews identified a number of areas where we can further enhance our risk management activities and these will be developed further in 2013.

Group risk governance structure

Group Risk Management Committee

The Group Risk Management Committee (GRMC) plays a pivotal role in the governance of risks. Each of Centrica's business units has a Business Risk Management Committee or equivalent management committee whose role is to evaluate, report and advise on material risks and to consider the adequacy of controls and the actions planned to mitigate those risks. The most material risks are then reported to the GRMC so that it has a clear understanding of Centrica's aggregate risk profile and can ensure that control processes are in place for the monitoring and management of significant risks. The Audit Committee has a standing agenda item to consider the Group's key risks. The GRMC is chaired by the Chief Executive and membership reflects that of the Executive Committee. In 2012, the GRMC met four times.

Group Financial Risk Management Committee

A separate specialised process to manage financial risks is also required to achieve adequate levels of control. The role of the Group Financial Risk Management Committee (GFRMC) is therefore to focus specifically on financial risks as part of the overall risk management profile.

Additional monitoring of the Group's financial risks (market, credit, liquidity risks and operational risks within the trading operations) is performed by local Financial Risk Management Committees covering Europe and North America. Material financial risk exposures are then reported to the GFRMC for consideration. The GFRMC also monitors the design and implementation of financial risk policies and compliance with Group-wide financial risk limits and appetite. Quarterly overviews of the GFRMC's activities are provided to the GRMC.

The GFRMC is chaired by the Group Finance Director and membership comprises senior finance and risk personnel. The Committee met 12 times in 2012. Further details of the Group's Financial Risk Management are provided in note 25 to the Financial Statements on pages 111 to 114.

Centrica Controls Board

The Centrica Controls Board (CCB), whose members are the Group Finance Director, the Director of Corporate Finance, the Head of Risk, Controls and Audit and finance directors for each business unit, is responsible for ensuring that appropriate internal controls are in place over key operational and financial reporting processes and related IT systems. The CCB met twice in 2012 and is chaired by the Group Finance Director. The responsibilities of the CCB are discharged through the Centrica Controls Steering Group (CCSG) and the Information Risk Steering Group (IRSG).

The CCSG monitors the risks and associated controls over financial reporting processes, including the process by which Centrica's Group Financial Statements are prepared for publication (the consolidation process). The financial reporting controls are monitored and maintained through the use of internal control frameworks which address key financial reporting risks, including risks arising from changes in the business or accounting standards. Effectiveness is assessed through quarterly self-certification and independent testing of the controls. The CCSG met three times during 2012 and is chaired by the Head of Group Financial Controls.

The IRSG monitors the Group's information systems control environment, providing robust challenge to the business units to ensure that information systems' risk management remains effective and appropriate for the Group. It is also responsible for monitoring the progress of key information security projects. The IRSG met four times during 2012 and is chaired by the Group Head of Information Risk.

Executive Committee and Audit Committee

The Group's material risks are also reported to the Executive Committee which regularly undertakes in depth reviews of specific risks as appropriate.

At each of its meetings in 2012 the Audit Committee received a Group risk report, which provided an assessment of the key risks facing the Company and the adequacy of the associated controls. In addition, the Audit Committee assessed the activity of the Group internal audit function including details of findings from reviews conducted against a plan which is approved annually by the Audit Committee. These reports, supplemented by management presentations and discussion with the Audit Committee, enable it to track issues, monitor performance and ensure that necessary actions are taken to remedy any significant failings or weaknesses identified.

The Company is also aware that the integrity and reputation of the Company's public financial reporting is of utmost importance. In addition to the controls described above, there are a number of further processes and steps to provide assurance over

CORPORATE GOVERNANCE REPORT CONTINUED

the completeness and accuracy of Centrica's public financial reporting, including:

- review by members of the Executive Committee;
- verification exercises;
- review and recommendation by the Audit Committee; and
- review and approval by the Board.

Centrica Storage and other Group companies

Centrica Storage Limited, which is subject to undertakings given to the Secretary of State for Business, Innovation and Skills, operates separately but to the same standards of internal control and risk management as the rest of the Group. The internal control and risk management processes of newly-acquired companies are also integrated with those of the Group.

The Board's review of the system of internal control

Each year, an extensive process of self-certification operates throughout the Group whereby the effectiveness of internal controls and compliance with Group business principles and policies are assessed. In 2012, the self-certification was completed both at the half year and full year. During the year, the self-certification process was enhanced so that it provided certification against a wider coverage of key controls affecting the operation of the business. The results of the annual process, together with the conclusions of the internal reviews by Internal Audit, inform the annual assessment performed by the Audit Committee.

The Board, with the advice of the Audit Committee, has reviewed the effectiveness of the system of internal control, for the period from 1 January 2012 to the date of this report and is satisfied that the Group complies with the Turnbull Guidance. The Board will continue routinely to challenge management in order to ensure that the system of internal control is constantly improving and remains fit for purpose.

Going concern

After making enquiries, the Board has a reasonable expectation that the parent company and the Group as a whole 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 Financial Statements. Further details of the Group's liquidity position and going concern review are provided in note 25 of the Financial Statements on pages 111 to 114.

Directors' responsibility statement

The Directors, who are named on pages 152 and 153, are responsible for preparing the Annual Report, the Directors' Remuneration Report and the Financial Statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare financial statements for each financial year. Accordingly, the Directors have prepared the Group Financial Statements in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union (EU) and the parent company Financial Statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law). Under company law the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Group and the Company and of the profit or loss of the Group for that period. In preparing these Financial Statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and accounting estimates that are reasonable and prudent;
- state whether IFRS as adopted by the EU and applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the Group and parent company Financial Statements respectively; and
- prepare the Financial Statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and the Group and enable them to ensure that the Financial Statements and the Directors' Remuneration Report comply with the Companies Act 2006 and, as regards the Group Financial Statements, Article 4 of the IAS Regulation. They are also responsible for safeguarding the assets of the Company and the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Furthermore, the Directors are responsible for the maintenance and integrity of the Company's website. Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Each of the Directors, whose names and functions are listed on pages 152 and 153 confirm that, to the best of their knowledge the Group Financial Statements, which have been prepared in accordance with IFRS as adopted by the EU, give a true and fair view of the assets, liabilities, financial position and profit of the Group. In addition, they confirm that the Directors' Report contained on pages 5 to 75, together with other disclosures given on pages 152 to 154, includes a fair review of the development and performance of the business and the position of the Group, together with a description of the principal risks and uncertainties that it faces.

Disclosure of information to auditors

Each of the Directors who held office at the date of approval of this Directors' Report confirm that, so far as they are aware, there is no relevant audit information of which the Company's auditors are unaware and that they have taken all steps that they ought to have taken as Directors to make themselves aware of any relevant audit information and to establish that the Company's auditors are aware of that information.

Independent auditors

PwC have expressed their willingness to be re-appointed as auditors of the Company. Upon the recommendation of the Audit Committee, separate resolutions to re-appoint them as the Company's auditors and to authorise the Directors to determine their remuneration will be proposed at the forthcoming AGM.

The Directors' Report for the year comprising pages 5 to 75 together with other disclosures given on pages 152 to 154 have been approved by the Board and signed on its behalf by:

Grant Dawson
General Counsel & Company Secretary
27 February 2013

REMUNERATION REPORT

"THE COMMITTEE AIMS TO PROVIDE CLEAR, TRANSPARENT REPORTING OF PERFORMANCE AND RESULTING REMUNERATION."

Lesley Knox
Chairman of the Remuneration Committee

On behalf of the Board I am pleased to present the Remuneration Committee's report for 2012.

The report has been designed to move towards the new requirements for remuneration reporting, as proposed by the Department for Business, Innovation and Skills (BIS) as part of their consultation process, and also to comply with existing requirements.

As we move towards separate votes on remuneration policy and the implementation of that policy, as required by the proposed new rules, we will look to segment the report so that it is clear which aspects shareholders will be asked to approve.

This year we have included a two page quick view summary of performance targets, outcomes, total remuneration opportunity and total remuneration received in 2012 for Executive Directors, together with the prior year for comparison purposes. The Committee aims to provide clear, transparent reporting of performance and resulting remuneration and believes that this report meets that objective.

As noted in the 2011 Remuneration Report, during the first quarter of 2012, the Committee adjusted the measurement and weighting of the key performance drivers within the existing incentive arrangements. We also introduced a formal mechanism for clawback of deferred rewards if it is subsequently discovered that results have been achieved by behaviour which fails to reflect the governance and values of the business. We have engaged with a number of shareholders during the year on our remuneration arrangements and remain committed to holding early discussions with shareholders in advance of any future changes.

Total variable earnings opportunity in 2012 remained unchanged from last year and the performance targets were both stretching and aligned with the Group's strategic objectives. The key performance drivers are based on simple measures and the arrangements require substantial deferral of short-term reward.

As we move forward the Committee intends to continue to strive for greater simplicity and transparency, to ensure alignment between the Group's strategic direction and the measures of performance, and to maintain a responsible approach to both fixed and variable remuneration, which respects both the social climate in which we operate and the demands of our business model.

MORE INFORMATION

For more information go online at centrica.com

REMUNERATION SUMMARY

Combined short-term and long-term incentive performance 2012

The charts below set out for each Executive Director the measures and their weighting (inner circle) and the performance achieved (outer circle) for both the short-term (Annual Incentive Scheme) and long-term (Long Term Incentive Scheme and Deferred and Matching Share Scheme) incentive arrangements operated during the year.

Short-term incentive targets

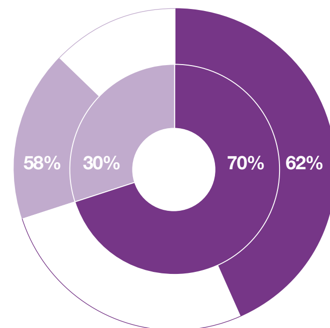
For Group economic profit (EP), adjusted operating profit of £2,892m less tax and a capital charge was required for 50% achievement and £3,197m for 100%.

For British Gas EP, adjusted operating profit of £1,063m less tax and a capital charge was required for 50% achievement and £1,179m for 100%.

For Centrica Energy EP, adjusted operating profit of £1,404m less tax and a capital charge was required for 50% achievement and £1,625m for 100%.

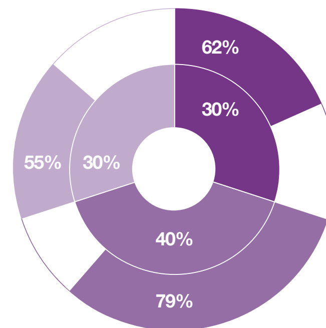
For Direct Energy EP, adjusted operating profit of C$513m less tax and a capital charge was required for 50% achievement and C$568m for 100%.

Sam Laidlaw



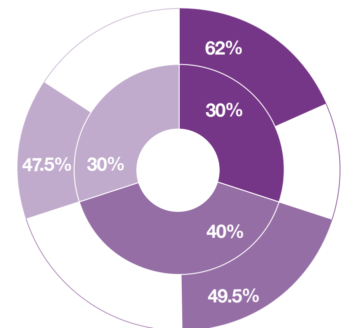
Group EP 62% achieved
Strategic priorities 58% achieved

Phil Bentley



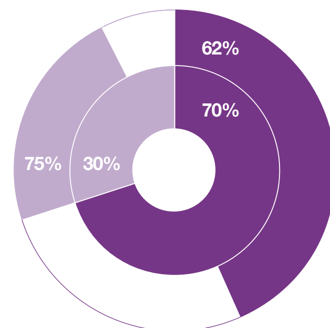
Group EP 62% achieved
British Gas EP 79% achieved
Strategic priorities 55% achieved

Mark Hanafin



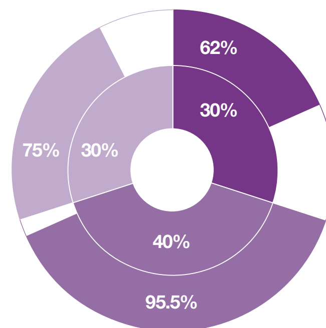
Group EP 62% achieved
Centrica Energy EP 49.5% achieved
Strategic priorities 47.5% achieved

Nick Luff



Group EP 62% achieved
Strategic priorities 75% achieved

Chris Weston



Group EP 62% achieved
Direct Energy EP 95.5% achieved
Strategic priorities 75% achieved

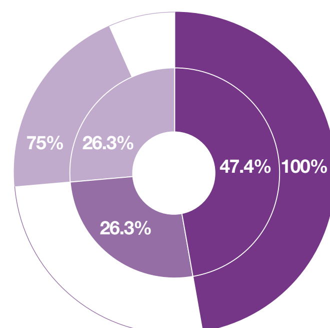
Long-term incentive targets

For Group EP 25% growth above 2009 actual was required for 100% achievement.

For Group earnings per share (EPS) a minimum growth of RPI +9% was required.

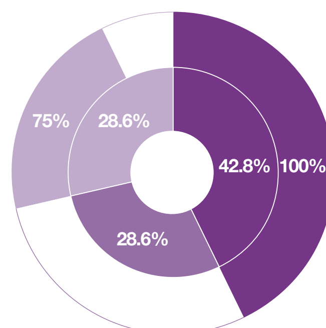
For total shareholder return (TSR) out-performance of the FTSE 100 Index by 0.1% per annum was required for 25% achievement and 7% per annum for 100%.

Sam Laidlaw



Group EP 100% achieved
EPS 0% achieved
TSR (relative) 75% achieved

Phil Bentley, Mark Hanafin, Nick Luff, Chris Weston

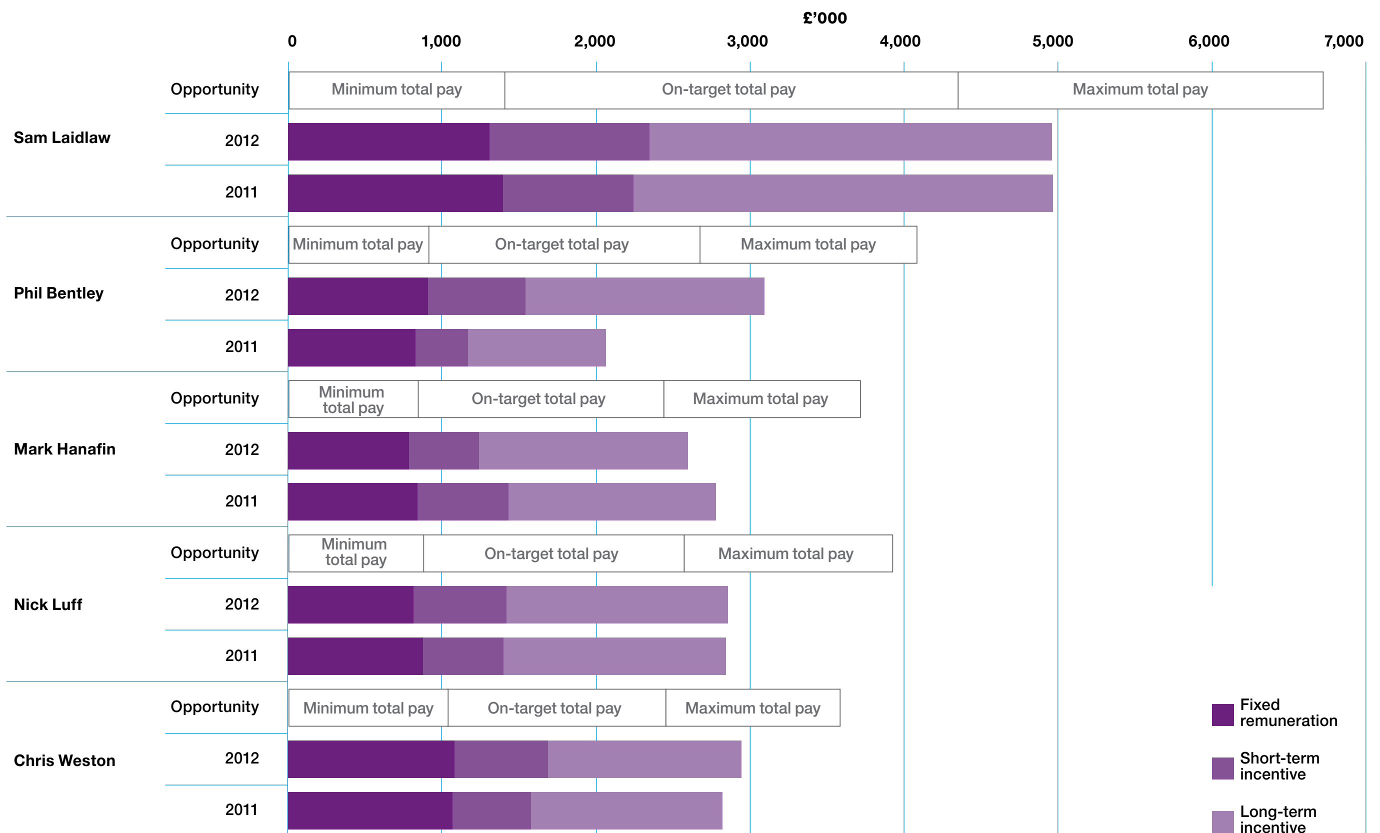


Group EP 100% achieved
EPS 0% achieved
TSR (relative) 75% achieved

Governance – Remuneration Report

Maximum total remuneration opportunity and total remuneration received in 2012

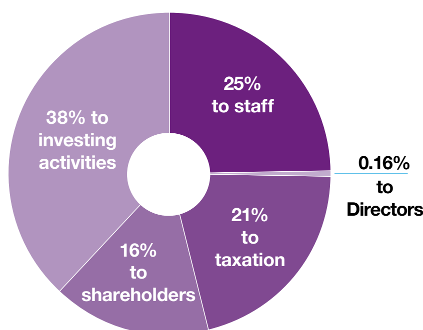
The chart below sets out the total remuneration received for the year for each Executive Director, prepared on the same basis as set out in the table on page 70. In addition, for comparison purposes, the chart provides an indication of minimum, on-target and maximum total remuneration, prepared on the same basis, other than to exclude share price movements, together with the total remuneration received for the prior year. Dividends accruing to share awards or received as a shareholder are not included.



2012 Cash flow distribution to stakeholders

The Committee monitors the relationship between the Directors' total remuneration and cash outflows to other stakeholders.

As demonstrated by the chart below, the Directors' aggregate total remuneration for the year equates to 0.16% (2011: 0.15%) of the Group's operating cashflow.



A further *c.*£700m of investment was funded from borrowing and other sources rather than from operating cashflows.

TSR vs CEO remuneration

Sam Laidlaw was appointed in July 2006. His total remuneration from 2009, the first year of full remuneration including vested long-term incentive plans, is shown in the chart below.

Comparison of overall Company performance and CEO pay

Total return indices – Centrica, FTSE 100 and CEO total pay

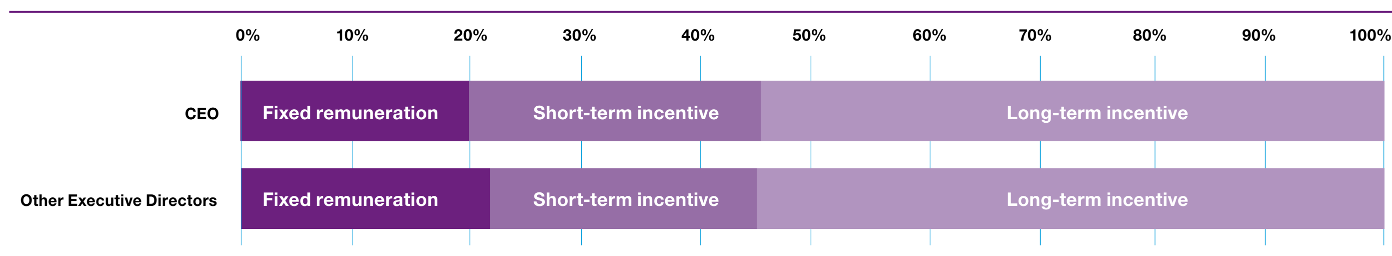
Source: Alithos Limited (with the exception of CEO total pay)
31 December 2007 = 100

Governance – Remuneration Report

REMUNERATION POLICY

The total remuneration package

The core design of the total remuneration package for Executive Directors ensures that a substantial portion of the maximum opportunity is dependent upon performance as indicated below.



Summary of remuneration elements for Executive Directors

Element	Opportunity	Objective and link to strategy	Current performance measures	Changes for 2013
Base pay	Salaries are reviewed annually, taking account of performance, market conditions and pay in the Group as a whole. Current salaries were originally set in 2010.	Reflects the role and sustained value of the individual in terms of skills, experience and contribution.	Not applicable.	Base salaries will be reviewed during the course of 2013.
Retirement benefits (i) (see pages 69 and 74)	Executive Directors are entitled to participate in a Centrica pension arrangement or to receive a salary supplement in lieu of pension of 40% of base pay.	Positioned to ensure broad competitiveness with market practice.	Not applicable.	No change.
Other benefits	Entitlements include car or car allowance, life assurance premiums, medical benefits and financial advice. Benefits are subject to financial limits as set out in appropriate policies. All taxable benefits are included in the table on page 70.	Positioned to ensure broad competitiveness with market practice.	Not applicable.	No change.
Annual Incentive Scheme (AIS) (see below and page 62)	Chief Executive 0 – 180% of base pay. Other Executive Directors 0 – 150% of base pay. Half the maximum is payable for on-target performance.	Designed to reward the delivery of key strategic priorities for the year. These priorities position the Group well for strong future performance, reinforcing the importance of balancing growth with economic profit returns in a business which is more vertically integrated and capital intensive. If overall business performance is not deemed satisfactory, the individual's bonus for the year may be reduced or forfeited, at the discretion of the Committee.	70% based on EP (ii). 30% based on strategic objectives aligned to business priorities.	No change.
Deferred and Matching Share Scheme (DMSS) (see pages 62 and 73)	Mandatory deferral of 40% of AIS award for Chief Executive and 30% for other Executive Directors. Additional deferral opportunity to take the total deferral up to 50% of maximum bonus opportunity. Up to two matching shares for each deferred share subject to performance over three years.	Assists with employee retention and incentivises an appropriate balance between short-term performance and long-term value creation for shareholders. Encourages sustainable high performance and discourages peaks and troughs. All deferred awards can be clawed back if it is subsequently discovered that the results have been achieved by behaviour which fails to reflect the governance and values of the business.	Absolute aggregate EP (ii) over the performance period: minimum £2.6bn and maximum £3.4bn provides one or two matching shares respectively. Where performance falls between stated points, vesting is calculated on a straight line basis.	No change.
Long Term Incentive Scheme (LTIS) (see pages 62, 71 and 72)	Up to 200% of base pay.	Provides a direct link between remuneration and Key Performance Indicators (KPIs) (iv), reinforcing the desire for sustainable high performance over the long-term. If overall performance is not deemed satisfactory, the award for any year may be reduced or forfeited, at the discretion of the Committee.	35% based on EPS (iii) with 25% vesting for achieving growth of RPI +9% and full vesting requiring RPI +30%. 35% based on absolute aggregate EP (ii) over performance period with 25% vesting for achieving £2.6bn and full vesting requiring £3.4bn. 30% based on non-financial KPI dashboard (iv). TSR (v) performance against the FTSE 100 Index acting as a positive or negative multiplier: 0.667x multiple for Index -7% per annum and 1.5x multiple for Index +7% per annum capped at the face value of the award. Where performance falls between stated points, vesting is calculated on a straight line basis.	No change.

Governance – Remuneration Report

(i) Retirement benefits

Centrica Pension Plan (CPP)

The CPP is a funded, HMRC-registered, final salary, contributory occupational pension scheme. Members' contributions are payable at the rate of 6% of pensionable earnings. Contributions made by the Executive Directors who are also members of the Centrica Unfunded Pension Scheme (CUPS) are payable at the rate of 6% of their total pensionable earnings above the scheme earnings cap.

No discretionary practices are taken into account in calculating transfer values.

Centrica Unfunded Pension Scheme (CUPS)

All registered scheme benefits are subject to HMRC guidelines and the Lifetime Allowance. The CUPS defined benefit section provides any additional benefits in excess of the maximum amount that could be provided through the CPP on the members' uncapped pensionable earnings. Pensionable pay increases are limited to pay reviews up to a maximum of 2% per annum with effect from 1 March 2012 for members of the CPP and CUPS defined benefit section.

The CUPS defined benefit section was closed to new members in October 2002. The CUPS defined contribution section provides benefits for individuals not eligible to join the CUPS defined benefit section and for whom registered scheme benefits are expected to exceed the Lifetime Allowance. The CUPS defined contribution section is offered as a direct alternative to a cash salary supplement.

CUPS is unfunded but the benefits are secured by a charge over certain Centrica assets. An appropriate provision in respect of the accrued value of these benefits has been made in the Company's balance sheet.

(ii) Economic profit (EP)

EP is adjusted operating profit (after share of joint venture interest) less a tax charge based on the tax rate relevant to the different business segments and after deduction of a capital charge. The capital charge is calculated as capital employed multiplied by the Group's weighted average cost of capital.

Where appropriate, expenditure on assets (and related costs) that are not yet in use (pre-productive capital) is excluded from capital employed. The absolute target range has been set in the context of increasing capital intensity and a significantly higher taxation environment for upstream profits driven by UK policy and geographic expansion.

(iii) Earnings per share (EPS)

EPS is the Company's fully diluted earnings per share adjusted for exceptional items and certain re-measurements.

(iv) Non-financial KPIs

The non-financial KPI dashboard is designed to reward sustained high performance over the entire three-year performance period. The measures are:

- lost time injury frequency rate;
- process safety;
- British Gas Net Promoter Score (NPS);
- Direct Energy NPS; and
- employee engagement.

For each measure three performance zones have been established, represented by the following indicators:

● High performance zone

● Median performance zone

● Low performance zone

The detail for 2012 is shown on page 72.

(v) Total shareholder return (TSR)

TSR is calculated as the annualised percentage increase in the Net Return Index of the Company above the Net Return Index of the FTSE 100 over the three-year performance period. The Net Return Index reflects movements in the share price and dividends re-invested over the performance period. In the opinion of the Directors, the FTSE 100 is the most appropriate index against which the TSR of Centrica plc should be measured as it is an index of similar sized companies.

REMUNERATION POLICY

Executive Directors' remuneration

The Remuneration Committee believes that our remuneration arrangements appropriately incentivise and reward shareholder value creation but do not encourage excessive risk taking.

The following sections outline the approach and framework relating to the remuneration of the executives with effect from 1 January 2012.

How reward aligns with our strategic priorities

The Committee believes alignment between Centrica's business strategy and executive remuneration is essential and therefore ensures that:

- remuneration comprises competitive fixed elements, to retain high quality talent without excessive cost to the business;
- a significant proportion of total remuneration depends on delivering business performance in line with the strategic priorities. Individuals are rewarded for good performance against stretching targets;
- short-term incentives focus on delivery against individual strategically-aligned performance measures. These include demanding financial and non-financial business-related objectives. A significant proportion of short-term incentives are required to be deferred, as outlined on page 64; and
- longer-term incentives are linked to, and reward, returns to shareholders over a three to four-year period.

How reward aligns with our KPIs

The KPIs, which are set out in detail on pages 18 and 19, underpin the selection of performance criteria used within the incentive arrangements as demonstrated in the table below. If overall performance is not deemed satisfactory, the award for any year may be reduced or forfeited, at the discretion of the Committee.

KPI	Performance measure	
Adjusted operating profit	EP – 1 year	EP – 3 year
EPS	EPS	
TSR	TSR	
Dividend per share	TSR	
Lost time injury frequency rate	Non-financial KPI dashboard	
Process safety	Non-financial KPI dashboard	
Customer trust	Non-financial KPI dashboard	
Employee engagement	Non-financial KPI dashboard	

Remuneration framework

The remuneration policy aims to deliver a remuneration package:

- to attract and retain high quality executives in a challenging and competitive business environment;
- that delivers an appropriate balance between fixed and variable compensation for each executive;
- which places a strong emphasis on performance, both short and long term;
- that strongly aligns achievement of strategic objectives and the delivery of sustainable value to shareholders; and
- that seeks to avoid creating excessive risks in the achievement of performance targets.

The remuneration framework reflects current best practice, including the provisions on the design of performance-related remuneration as set out in the UK Corporate Governance Code (the Code):

- the Committee reviews the packages and varies individual elements, when appropriate, from year-to-year;
- the potential maximum remuneration that executives could receive is of key interest when agreeing the level of base pay and the performance related elements of the remuneration package;
- the Committee takes account of, and is sensitive to, employment conditions throughout the Group and the current economic climate as a whole;
- benchmarking looks at a UK cross-industry comparator group of companies of similar size and complexity;
- the Annual Incentive Scheme (AIS) is designed to incentivise and reward the achievement of demanding financial and business-related objectives;
- long-term share-based incentives are designed to align the interests of the executives with the longer-term interests of our shareholders, by rewarding delivery of sustained, increased shareholder value;
- the Committee considers the aggregate impact of remuneration on the financial standing of the Group;
- the Committee carefully considers compensation commitments in the event of a director's termination. The aim is to avoid rewarding poor performance and to reduce compensation to reflect the departing directors' obligations to mitigate loss; and
- minimum shareholding guidelines for Executive Directors are in place and were last reviewed during 2012 to align with emerging investor preference.

All-employee share schemes
Executive Directors are also eligible to participate in the Company's HMRC-approved Sharesave Scheme and Share Incentive Plan, which are open to all eligible UK employees on the same basis, providing a long-term saving and investment opportunity.

Funding of share schemes
The Company may satisfy the requirements of its share schemes either by acquiring shares in the market or, subject to institutional guidelines, issuing new shares or using shares held in treasury.

Pay and conditions across the Group
Pay and employment conditions across the Group are taken into account when setting the remuneration of the executives.

The Group operates in a number of different environments and has many employees who carry out diverse roles across a number of countries. All employees, including executives, are paid by reference to the market rate and base pay is reviewed annually.

A number of performance-related bonus schemes and all-employee share plans are operated across the Group.

Business unit performance measures are cascaded down through the organisation and Group employment conditions include high standards of health and safety and equal opportunities.

Service contracts
The Executive Directors' service contracts expire on their 65th birthday, with the exception of Phil Bentley for whom three months' notice must be served by either party following his 65th birthday. Service contracts provide that either the Director or the Company may terminate the employment by giving one year's written notice and that the Company may pay compensation in lieu of notice.

On a change of control, conditional awards and nil-cost options under DMSS and LTIS will vest to the extent that the performance conditions will have been met at the vesting date and be pro-rated for the time elapsed since the start of each performance period, until the vesting date, subject to the overriding discretion of the Committee.

The Committee retains a level of flexibility, as permitted by the Code, in order to attract and retain suitable candidates. It reserves the right to offer contracts which contain an initial notice period in excess of one year, provided that at the end of the first such period the notice period reduces to one year.

External appointments of Executive Directors
It is the Company's policy to allow each Executive Director to accept one non-executive directorship of another company, although the Board retains the discretion to vary this policy.

Fees received in respect of external appointments are retained by the individual Director.

Shareholding guidelines
Minimum shareholding guidelines are in place for Executive Directors and senior executives to build and maintain a value of shares as follows:

- Chief Executive - 2 times base salary;
- other Executive Directors - 1.25 times base salary; and
- senior executives - 1 times base salary.

In addition to the guidelines above, for awards made after 1 January 2011, the guidelines now provide that all transferred shares under the Group's long-term incentive arrangements be retained for a minimum period of five years from the original award or grant date.

The executives have achieved, and in some cases materially exceeded, their minimum shareholding guidelines.

Non-Executive Directors' remuneration
Remuneration policy for Non-Executive Directors
Centrica's policy on Non-Executive Directors' fees takes into account the need to attract high-quality individuals, their responsibilities, time commitment and market practice.

Fees
The fee levels for the Chairman are reviewed every two years by the Remuneration Committee. The fee levels of the Non-Executive Directors are reviewed and approved every two years by the Executive Committee.

The Non-Executive Directors, including the Chairman, do not participate in any of the Company's share schemes, incentive plans or pension schemes.

Terms of appointment
Non-Executive Directors, including the Chairman, do not have service contracts. Their appointments are subject to the Articles of Association and the dates they joined the Board are shown on pages 152 and 153. Sir Roger Carr's letter of appointment contains a six-month notice period and his fees are reviewed and approved by the Committee.

REMUNERATION STATEMENT

This Statement sets out information on the remuneration of the Directors for the financial year ended 31 December 2012.

The Remuneration Committee

The Remuneration Committee (the Committee) firmly believes that Centrica's remuneration is and will remain in compliance with the principles of the Code and this Report outlines how the Company has applied the principles that relate to Directors' remuneration.

The role and membership of the Committee is set out in the Governance Report on page 56, together with the key issues reviewed by the Committee during 2012. In 2012, the Committee had access to the advice and views of:

- the Group Director, Human Resources;
- the Group Reward Director;
- the Chief Executive;
- the General Counsel & Company Secretary; and
- Deloitte LLP (Deloitte), independent external advisers to the Committee.

Deloitte also provide a number of consulting services throughout the Group. The Committee takes into account the Remuneration Consultants Group's Code of Conduct when dealing with its advisers. The Committee is satisfied with the performance of Deloitte, who were appointed in 2011, and has determined that it is not necessary to seek a tender for the services currently provided.

2012 Voting

At the Centrica Annual General Meeting held on 11 May 2012, shareholders approved the Remuneration Report for the year ended 31 December 2011. Below is the result in respect of the resolution, which required a simple majority (i.e. 50%) of the votes cast to be in favour in order for the resolution to be passed:

Votes for	%	Votes against	%
2,687,947,000	88.09	363,374,799	11.91

155,878,917 votes were withheld

A full schedule in respect of shareholder voting on the above and all resolutions at the 2012 Annual General Meeting is available on the Centrica website at centrica.com.

Executive Directors' remuneration

Base pay

There were no increases in Executive Directors' base pay in 2012, thus maintaining the levels originally set in 2010. Base salaries will be reviewed during the course of 2013.

Emoluments of the senior executives

The total emoluments of the two senior executives who served during 2012, calculated on the same basis as the emoluments of the Executive Directors detailed on page 70, fell into the following bands:

Bands £000	Number of executives
1,500 – 1,999	1
1,000 – 1,499	0
500 – 999	1

External appointments of Executive Directors

In 2012, Sam Laidlaw received £125,000 (2011: £125,000) as a non-executive director of HSBC Holdings plc and has waived his right to receive a fee for his role as the lead non-executive director of the Department of Transport.

In October 2012, Phil Bentley was appointed as a non-executive director of IMI plc and received £13,125.

Executive Share Option Scheme (ESOS)

- Outstanding ESOS options held by Chris Weston were granted on 18 March 2004, 1 April 2005 and 3 April 2006.
- No options have been granted under the ESOS since 2006.
- The performance criteria have now been met in respect of all of the outstanding grants under ESOS and Chris Weston has a 10 year period from each date of grant during which he can exercise his options.

Special Executive Share Option Scheme (SESOS)

- Outstanding SESOS options held by Mark Hanafin were granted on 26 September 2008.
- The grant is not subject to any performance conditions and Mark Hanafin has a 10 year period from the date of grant during which he can exercise his options.

LTIS and DMSS options

- Nil-cost options were granted to the Executive Directors in respect to LTIS and DMSS matching awards, excluding Chris Weston, on 6 April 2010, 4 April 2011 and 4 April 2012 and are disclosed on pages 71 and 73.
- Grants under LTIS are subject to EP, EPS, non-financial KPIs and TSR as outlined on pages 64 and 65.
- Grants under DMSS are subject to EP performance as outlined on pages 64 and 65.
- Recipients have a 10 year period from each date of grant during which to exercise any such options that may vest.
- Once vested, LTIS and DMSS matching nil-cost options will be disclosed in the table detailing Directors' interests in share options on page 73.

Sharesave Scheme

Outstanding Sharesave options held by the Executive Directors were granted on 3 April 2008, 6 April 2010 and 30 March 2012.

Funding of share schemes in 2012

During 2012, new issue shares were used to satisfy the release of shares or exercise of options under DMSS, LTIS, ESOS, Sharesave and SIP. Market purchased shares, held in trust, were used to satisfy outstanding allocations under DMSS (deferred and investment shares), the Restricted Share Scheme and the Deferred Bonus Plan. There are no shares currently held in treasury, in accordance with the Companies Act 2006.

Share Price

The closing price of a Centrica ordinary share on the last trading day of 2012, which was 31 December 2012, was 333.60 pence. The range during the year was 280.50 pence to 341.30 pence.

Pension and other benefits

Phil Bentley and Chris Weston participate in the CPP, a contributory final salary arrangement, and in the CUPS defined benefit (DB) section. Full disclosure of the pension arrangements for Phil Bentley and Chris Weston is given on page 74.

As previously reported, under the terms of his contract of employment, following completion of the appropriate qualifying period which ended on 14 January 2012, Phil Bentley is now entitled to draw his pension on an unreduced basis with effect from his 58th birthday.

Sam Laidlaw, Mark Hanafin and Nick Luff are entitled to receive a salary supplement of 40% of base pay, or participate in the CUPS defined contribution (DC) section. During the year, the three Executive Directors were invited to, and decided to participate in, the CUPS DC section and received an unfunded promise equal to 11.1% of base pay. Consequently, a salary supplement equal to 28.9% of base pay was paid in cash directly to each individual and is disclosed within the Directors' emoluments table on page 70.

Termination payments

No termination payments were made during 2012 (2011: £nil).

Non-Executive Directors' remuneration

Non-Executive fees

The annual fees payable to the Chairman and Non-Executive Directors are set out in the table below.

Base fees	**2012**
Chairman	£490,000
Non-Executive Directors	£65,000
Additional fees	
Chairman of Audit Committee	£23,000
Chairman of Remuneration Committee	£20,000
Chairman of Corporate Responsibility Committee	£20,000
Senior Independent Director	£20,000

The fee levels for the Chairman and the Non-Executive Directors were reviewed and increased in May 2010. There were no increases in fee levels for the Chairman and the Non-Executive Directors in 2012.

Statutory disclosures

Audit requirements

The Company's auditors, PricewaterhouseCoopers LLP, have audited from this point until the end of the Remuneration Statement on page 75, with the exception of the TSR charts on page 72.

Governance – Remuneration Report

REMUNERATION STATEMENT CONTINUED

Remuneration tables

Directors' remuneration

	Base pay/fees £000	Cash payments in lieu of pension and contributions to DB plans £000 (i)	Benefits and other cash £000 (ii)	Cash AIS £000	Deferred AIS £000 (iii)	Long-term incentives (LTIS and DMSS matching) £000 (iv)	**Total remuneration 2012 £000 (v)**	Total remuneration 2011 restated £000 (vi)
Chief Executive								
Sam Laidlaw	950	285	71	185	855	2,613	**4,959**	4,967
Executive Directors								
Phil Bentley	635	225	46	635	–	1,549	**3,090**	2,064
Mark Hanafin	575	173	35	23	431	1,358	**2,595**	2,778
Nick Luff	610	183	21	145	458	1,437	**2,854**	2,840
Chris Weston	510	167	403	224	383	1,254	**2,941**	2,798
	3,280	1,033	576	1,212	2,127	8,211	**16,439**	15,447
Chairman and Non-Executive Directors	963	–	–	–	–	–	**963**	963
Total remuneration	4,243	1,033	576	1,212	2,127	8,211	**17,402**	16,410

Directors' emoluments

	Base pay/fees £000	Cash payments in lieu of pension £000 (i)	Benefits and other cash £000 (ii)	Cash AIS £000	Deferred AIS £000 (iii)	**Total emoluments 2012 £000 (v)**	Total emoluments 2011 restated £000 (vii)
Chief Executive							
Sam Laidlaw	950	285	71	185	855	**2,346**	2,241
Executive Directors							
Phil Bentley	635	–	46	635	–	**1,316**	1,166
Mark Hanafin	575	173	35	23	431	**1,237**	1,430
Nick Luff	610	183	21	145	458	**1,417**	1,398
Chris Weston	510	–	403	224	383	**1,520**	1,574
	3,280	641	576	1,212	2,127	**7,836**	7,809
Chairman							
Sir Roger Carr	490	–	–	–	–	**490**	490
Non-Executive Directors							
Dame Helen Alexander	–	–	–	–	–	**–**	85
Margherita Della Valle	65	–	–	–	–	**65**	65
Mary Francis	105	–	–	–	–	**105**	105
Lesley Knox	85	–	–	–	–	**85**	–
Andrew Mackenzie	65	–	–	–	–	**65**	65
Ian Meakins	65	–	–	–	–	**65**	65
Paul Rayner	88	–	–	–	–	**88**	88
	963	–	–	–	–	**963**	963
Total emoluments	4,243	641	576	1,212	2,127	**8,799**	8,772

(i) Contributions into the defined benefit pension plan for Phil Bentley and Chris Weston, calculated using the BIS methodology of 20 times the increase in the accrued pension for the year are included in the Directors' remuneration table above. The table excludes CUPS defined contribution unfunded promises.

(ii) Benefits and other cash include:
- car, health and medical, financial planning and life assurance premiums; and
- benefits and expenses for Chris Weston under the terms of his international assignment agreement and for his relocation from Canada to the US.

(iii) Each Executive Director has deferred up to 50% of their maximum AIS potential on a gross basis and invested these funds into DMSS, see pages 62 and 73.

(iv) The long-term incentives include a forecast of the value of the LTIS awards due to vest in April 2013, relating to the three-year performance period ending in 2012, and a forecast of the value of DMSS matching awards due to vest in April 2013, relating to the three-year performance period ending in 2012. The share price used to calculate the forecasted value was the three month average to 31 December 2012 (328.6p per share). The LTIS awards were valued using the latest TSR projection as at 1 February 2013, which was 75.6% (see TSR chart on page 72), and the projected EPS performance outcome of 0%. The DMSS awards were valued using the projected EP performance outcome of 100%.

(v) The following are excluded from the table above: ESOS options, Sharesave (see table on page 73), the value of any shares awarded under the Share Incentive Plan and the value of dividend equivalent shares to be calculated at vesting in respect of LTIS and DMSS matching awards.

(vi) The 2011 total remuneration figures have been recalculated and restated based on the BIS methodology for calculating total emoluments. Consequently, the value of the long-term incentive awards vesting in 2012 has been included in the total remuneration for 2011.

(vii) The 2011 total emoluments figures have been recalculated and restated and now include: the AIS for the 2011 year that was deferred into the DMSS, and included in a separate table in the 2011 Remuneration Report, and £101,000 paid by the Company into a personal pension plan for Sam Laidlaw.

LTIS and SLTIS allocations for Executive Directors (number of shares)

	Vested during 2012		In performance period		
Date of allocation	3 Apr 09 (i) (iii)	9 Sep 09 (ii) (iii)	6 Apr 10 (iv) (v)	4 Apr 11 (iv) (v)	4 Apr 12 (iv) (v)
Sam Laidlaw	197,838	–	643,500	582,179	598,312
Phil Bentley	132,973	–	430,129	389,140	399,924
Mark Hanafin	114,594	–	389,487	352,371	362,136
Nick Luff	121,080	–	413,195	373,820	384,179
Chris Weston (v)	81,080	45,076	345,458	312,538	321,199
Market price at allocation	–	–	295p	326p	318p
Vesting date	–	–	8 Apr 13	4 Apr 14	4 Apr 15
Market price at vesting	312p	330p	–	–	–

(i) At the end of the performance period the Company's EPS growth in excess of RPI over the period, after the usual adjustment for tax equalisation, was 13.9%, resulting in vesting of 42.67% of the EPS shares. The TSR target for awards made in April 2009 had not been met and as a result none of the TSR shares allocated vested during the year. 21.3% of the original allocations were released on 4 April 2012 (2011: 27.5%).

(ii) At the end of the performance period the Company's EPS growth in excess of RPI over the period, after the usual adjustment for tax equalisation, was 13.9%, resulting in vesting of 42.67% of the EPS shares. Centrica had ranked 45th in the FTSE 100 comparator group for awards made in September 2009 and accordingly 37.5% of the TSR shares vested. 40.1% of the original allocations were released on 12 September 2012 (2011: 32.5%).

(iii) Additional shares were released to reflect the value of the dividends that would have been paid over the respective three-year period.

(iv) From 2010, LTIS awards have been structured as nil-cost options for all UK resident participants. Once vested, nil-cost options will be reported in the Directors' interests in share options disclosure within this report.

(v) In respect of Chris Weston, who was based in Canada and moved to the US during the year, conditional awards have been allocated and are included above.

LTIS

In 2012, LTIS allocations equal to 200% of base pay were awarded to Executive Directors and, at lower levels, to other senior executives. The performance measures attaching to the outstanding LTIS awards are shown in the table below.

Vesting criteria 2012	Performance condition over three-year period
35% on EPS (i) growth against RPI growth	Full vesting for EPS growth exceeding RPI growth by 30% Zero vesting if EPS growth does not exceed RPI growth by 9% Vesting will increase on a straight-line basis between 25% and 100% between these points.
35% on absolute aggregate EP	Full vesting for aggregate EP of £3.4bn Zero vesting if aggregate EP is below £2.6bn Vesting will increase on a straight-line basis between these points.
30% on non-financial KPI dashboard	As disclosed on page 65.
Positive/negative multiplier on TSR performance against the FTSE 100 index	0.667x multiple for Index -7% per annum and 1.5x multiple for Index +7% per annum subject to a cap at the face value of the award. Where performance falls between stated points, vesting is calculated on a straight-line basis.
Vesting criteria 2010 and 2011	
One half on EPS (i) growth against RPI growth	Full vesting for EPS growth exceeding RPI growth by 30% Zero vesting if EPS growth does not exceed RPI growth by 9% Vesting will increase on a straight-line basis between 25% and 100% between these points.
One half on TSR measured as a percentage out-performance of the FTSE 100 Index	Full vesting for TSR out-performance of the FTSE 100 Index by 7% per annum Zero vesting if TSR out-performance of the FTSE 100 Index does not exceed 0.1% per annum Vesting will increase on a straight-line basis between 25% and 100% for TSR out-performance of the FTSE 100 Index between these points.
Vesting criteria 2009	
One half on EPS (i) growth against RPI growth (i)	As above for 2010 and 2011.
One half on TSR measured against a comparator group of the FTSE 100 as constituted at the beginning of the performance period	Full vesting for upper-quintile ranking Zero vesting for sub-median ranking Vesting will increase on a straight-line basis between 25% and 100% for ranking between these points.

(i) EPS is the Group's diluted adjusted earnings per share.

Governance – Remuneration Report

REMUNERATION STATEMENT CONTINUED

LTIS Non-Financial KPI Dashboard

The non-financial KPI dashboard is designed to reward sustained high performance over the entire performance period, as indicated below.

For each measure three performance zones have been established, represented by the following indicators:

- ● High performance zone
- ● Median performance zone
- ● Low performance zone

Measure	Performance period Year 1 2012	 Year 2 2013	 Year 3 2014
Lost time injury frequency rate	● (high)	○	○
Process safety	● (high)	○	○
British Gas Net Promoter Score (NPS)	● (high)	○	○
Direct Energy NPS	● (high)	○	○
Employee engagement	● (median)	○	○

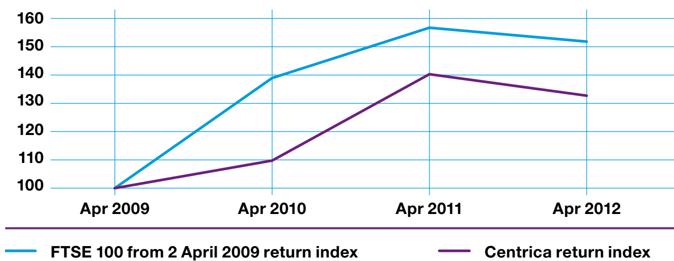
Total shareholder return (TSR)

In assessing the extent to which the performance conditions have been met, the Committee uses data provided by Alithos Limited (an independent third party) for comparative TSR performance. The Committee also considers whether the extent to which the performance conditions have been achieved is a genuine reflection of the Company's underlying financial performance.

The TSR graphs for the three-year performance of the LTIS awards that vested in April 2012 and September 2012 are shown below.

TSR – three year comparator group

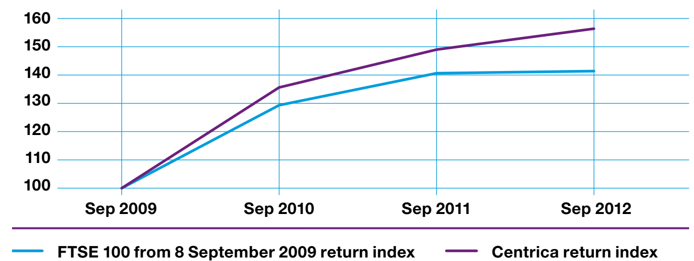
Centrica and FTSE 100 comparator companies



Source: Alithos Limited, 2 April 2009 = 100

TSR – three year comparator group

Centrica and FTSE 100 comparator companies

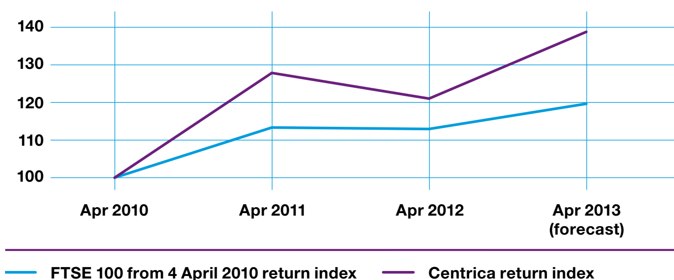


Source: Alithos Limited, 8 September 2009 = 100

The TSR graph for the three-year performance of the LTIS award due to vest in April 2013 is shown below, including forecast performance to April 2013.

TSR – three year comparator group

Centrica and FTSE 100 comparator companies



Source: Alithos Limited, 4 April 2010 = 100

Governance – Remuneration Report

DMSS for Executive Directors (number of shares)

	Deferred and investment shares acquired during 2012	Conditional matching shares awarded during 2012 (ii) (iii)	Deferred, investment and matching shares awarded during 2011 (ii) (iii) (iv)	Deferred, investment and matching shares awarded during 2010 (ii) (iii) (iv)	Deferred shares released and investment shares transferred during 2012 (iv)	Conditional matching shares released during 2012 (v)
Sam Laidlaw	272,848	548,114	733,103	800,728	282,574	701,639
Phil Bentley	129,720	305,306	397,889	436,973	86,099	172,198
Mark Hanafin	138,231	276,462	362,033	374,993	113,519	332,245
Nick Luff	146,645	293,290	381,808	396,565	140,352	356,787
Chris Weston (i)	122,605	245,210	318,556	349,128	109,241	280,040
Market price at Allocation date	312p	312p	332.14p	297.36p		
Vesting Date	4 Apr 15	4 Apr 15	4 Apr 14	8 Apr 13	4 Apr 12	4 Apr 12
Market price At Vesting Date					312p	312p

(i) In respect of Chris Weston, who was based in Canada and moved to the US during the year, conditional awards have been allocated and in this respect, 166,057 shares are included above.
(ii) From 2010, awards of matching shares to executives excluding Chris Weston have been structured as nil-cost options for all UK resident participants. Once vested, nil-cost options will be reported in the Directors' interests in share options disclosure within this report.
(iii) For the calculation of matching shares before 2012, investment shares were grossed up (to reflect the impact of income tax and employee's National Insurance Contributions (NICs)) so that the deferred and investment shares were matched on the same basis.
(iv) The number of matching shares released following the satisfaction of the performance condition is increased to reflect the dividends that would have been paid during the three-year performance period. Dividends are paid on the deferred and investment shares to the participants on the normal dividend payment date.
(v) As at 31 December 2011, the Company's cumulative EP growth over the three-year performance period was 62% and as a result the conditional matching shares vested in full.

Directors' interests in share options

Full details of the options over ordinary shares in the Company held by Executive Directors who served during the year, and any movements in those options in the year, are shown below.

	Options held as at 1 January 2012	Options granted during the year	Options exercised during the year	Options lapsed during the year	**Options held as at 31 December 2012**	Exercise price (pence) (i)	Date from which exercisable	Expiry date
Sam Laidlaw								
Sharesave	3,977	–	–	–	**3,977**	228.16	Jun 13	Nov 13
Phil Bentley								
Sharesave	3,977	–	–	–	**3,977**	228.16	Jun 13	Nov 13
Mark Hanafin								
SESOS	336,012	–	–	–	**336,012**	255.94	Sep 08	Sep 18
Sharesave	4,727	3,740	(4,727) (ii)	–	**3,740**	240.60 (iii)	Jun 15	Nov 15
	340,739	3,740	(4,727)	–	**339,752**			
Nick Luff								
Sharesave	7,392	–	–	–	**7,392**	227.24	Jun 13	Nov 13
Chris Weston								
ESOS	112,330	–	(112,330) (iv)	–	**-**	130.50	Mar 06	–
ESOS	120,379	–	–	–	**120,379**	199.36	Mar 07	Mar 14
ESOS	130,187	–	–	–	**130,187**	203.55	Apr 08	Mar 15
ESOS	267,920	–	–	–	**267,920**	253.80	Apr 09	Apr 16
Sharesave	4,727	3,740	(4,727) (v)	–	**3,740**	240.60 (iii)	Jun 15	Nov 15
	635,543	3,740	(117,057)	–	**522,226**			

(i) Where appropriate, exercise prices were adjusted to take account of the dilutive effect of the Rights Issue in 2008.
(ii) The share price on the date of exercise was 323.50p per share and consequently the gain on exercise was £6,143.
(iii) This relates to the exercise price of the options granted during the year. The exercise price of the options exercised during the year was 193.54 pence.
(iv) The share price on the date of exercise was 319.60p per share and consequently the gain on exercise was £212,416.
(v) The share price on the date of exercise was 308.60p per share and consequently the gain on exercise was £5,439.

REMUNERATION STATEMENT CONTINUED

Directors' interests in shares (number of shares)

The following table shows the interests of the Directors who held office at the end of the year in the ordinary shares of the Company and, for the Executive Directors, their interests in the Company's share schemes.

	Shareholdings as at 31 December 2012 (iii)	Shareholdings as at 1 January 2012	**DMSS total matching shares as at 31 December 2012**	DMSS total matching shares as at 1 January 2012	**LTIS total allocations of shares as at 31 December 2012**	LTIS total allocations of shares as at 1 January 2012
Chief Executive						
Sam Laidlaw (i) (ii)	**2,521,122**	2,249,985	**1,616,821**	1,770,346	**1,823,991**	2,032,379
Executive Directors						
Phil Bentley (i) (ii)	**2,219,238**	1,995,871	**902,306**	769,198	**1,219,193**	1,361,477
Mark Hanafin (i) (ii)	**519,093**	488,941	**803,486**	859,269	**1,103,994**	1,209,126
Nick Luff (i) (ii)	**646,997**	639,791	**851,255**	914,752	**1,171,194**	1,280,733
Chris Weston (i) (ii)	**631,754**	591,361	**727,750**	762,580	**979,195**	1,086,610
Chairman						
Sir Roger Carr	**58,361**	58,361	**–**	–	**–**	-
Non-Executive Directors						
Margherita Della Valle	**5,000**	5,000	**–**	–	**–**	–
Mary Francis	**3,500**	3,500	**–**	–	**–**	–
Lesley Knox	**3,500**	–	**–**	–	**–**	–
Andrew Mackenzie	**28,875**	28,875	**–**	–	**–**	–
Ian Meakins	**5,000**	5,000	**–**	–	**–**	–
Paul Rayner	**56,875**	56,875	**–**	–	**–**	–

(i) Executive Directors' shareholdings shown above include those held in the Share Incentive Plan and the deferred and investment shares held in DMSS. Shareholdings for Chris Weston include 166,057 notional deferred shares under DMSS which will remain notional until the end of the three-year deferral period due to local Canadian tax laws.
(ii) Matching shares held in DMSS and shares held under LTIS are conditional and the above numbers indicate the maximum potential opportunity. More detail can be found in their respective tables on pages 73 and 71.
(iii) From 1 January 2012 to 27 February 2013, none of the Directors had any interests in the securities of the Company's subsidiaries or associated undertakings.

Pension benefits earned by Directors in the CPP and CUPS defined benefit section

	Accrued pension as at 31 December 2012 £	Accrued pension as at 31 December 2011 £	Increase in accrued pension less inflation £	**Transfer value as at 31 December 2012 £**	Transfer value as at 31 December 2011 £	**Contribution paid in 2012 £**	Difference in transfer value less contributions £	Transfer value of increase in accrued pension excluding inflation £
Phil Bentley	**226,200**	209,500	11,253	**5,420,000**	3,641,900	**38,100**	1,740,000	228,500
Chris Weston	**125,600**	114,300	8,328	**1,879,800**	1,574,300	**30,600**	274,900	93,500

Notes on information shown in the table.

- The accrued pension is that which would be paid annually on retirement at age 62, based on eligible service to, and pensionable earnings at, 31 December 2012.The pension accrual rates for 2012 for Phil Bentley and Chris Weston were 2.65% and 2.22% of final pensionable earnings respectively.
- The increase in accrued pension has been adjusted to exclude inflation by revaluing the accrued pension as at 31 December 2011 by the rate of inflation (2.6%) and deducting this from the accrued pension as at 31 December 2012. The rate of inflation used for pension increases under both the CPP and CUPS was 2.6%, the annual rate to 30 September 2012 (the rate of inflation used for pensions in deferment from 1 January 2011 reference the Consumer prices index with a cap of 2.5% for pension accrued after 29 February 2012).
- As previously reported, under the terms of his contract of employment, the transfer value calculations in respect of Phil Bentley as at 31 December 2012 reflect his entitlement to retire on an unreduced pension at age 58 which vested on 14 January 2012 (the transfer value as at 31 December 2011 is based on an assumed retirement age of 62). If the pension at 31 December 2012 was provided on the basis of a Normal Retirement Age of 62 the transfer value would amount to £4,254,000, the difference in transfer value less contributions would amount to £574,000, and the transfer value of the increase in accrued pension excluding pension contributions would amount to £165,900.

Governance – Remuneration Report

Changes since 1 January 2013

Share Incentive Plan (SIP)

During the period from 1 January to 27 February 2013, the only changes to the Directors' interests in shares were in respect of shares acquired through the SIP: 108 shares in respect of Sam Laidlaw and 107 shares in respect of Mark Hanafin, Nick Luff, Chris Weston and Phil Bentley.

Termination arrangements for Phil Bentley

As announced on 27 February 2013, Phil Bentley will be stepping down from his role as Managing Director of British Gas, and therefore as an Executive Director, on 30 June 2013 and he will leave the Company by 31 December 2013.

Phil Bentley will continue as Managing Director of British Gas until 30 June 2013 and therefore will stand for re-election as a Director at the Company's Annual General meeting in May for the interim period. From 1 July to 31 December 2013 he will cease to be a Director but will remain as an employee.

Phil Bentley will be paid according to his current contractual arrangements including pro rata performance bonus awards through to the expiry of his accrued vacation on 31 July 2013. Thereafter he will be paid a basic salary and all bonus earning opportunities will cease. He will not participate in any new long-term awards to be made in 2013. In the event that he takes up new full time employment after the handover he may be released from his employment, in which case all remuneration will cease at that time.

On completion of his employment he will have been deemed to have worked his contractual notice period and no lump sum will be paid in lieu of notice.

Phil Bentley is classified as a 'good leaver' and is therefore entitled to all accrued allocations that have been earned during his employment under the long term incentive plans in the normal way. The value of the long term incentive plans will be time apportioned and will remain subject to the performance conditions and therefore the actual number of shares which will vest will be lower than the maximum potential. The actual value of the awards will be determined at the end of the performance measurement period.

Phil Bentley will leave with a pension entitlement consistent with his contractual rights which reflects his length of service and includes accrued rights transferred in from his prior employment commencing in September 1980. Under the pension arrangements he is entitled to retire at age 55 on a reduced pension, or at age 58 on an unreduced pension. Based on the contributions at 31 December 2012 and assuming he retires at age 58, he will become entitled to an annual pension from the Company of approximately £226,200.

This Report on remuneration has been approved by the Board of Directors and signed on its behalf by:

Grant Dawson
General Counsel & Company Secretary
27 February 2013

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
Senior Statutory Auditor
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
London
27 February 2013

Financial Statements

Contents

78 Group Financial Statements

82 Notes to the Financial Statements

82 Summary of significant new accounting policies and reporting changes

82 Centrica specific accounting measures

83 Critical accounting judgements and key sources of estimation uncertainty

86 Segmental analysis

91 Costs of continuing operations

91 Directors and employees

92 Exceptional items and certain re-measurements

93 Net interest

93 Taxation

94 Dividends

95 Earnings per ordinary share

96 Sources of finance

97 Notes to the Group Cash Flow Statement

99 Goodwill and other intangible assets

102 Property, plant and equipment

103 Interests in joint ventures and associates

104 Inventories

104 Trade and other receivables

105 Derivative financial instruments

106 Hedge accounting

107 Trade and other payables

108 Deferred tax liabilities and assets

108 Provisions for other liabilities and charges

109 Fair value of financial instruments

111 Financial risk management

115 Share capital

115 Accumulated other comprehensive (loss)/income

116 Other equity

116 Pensions

119 Business combinations and asset purchases

120 Disposals, discontinued operations and disposal groups held for sale

120 Auditors' remuneration

121 Commitments and contingencies

122 Related party transactions

123 Fixed-fee service and insurance contracts

123 Events after the balance sheet date

124 Supplementary information

124 General information

124 Summary of significant accounting policies

130 Financial risk management

132 Segmental analysis

132 Other equity

133 Pensions

133 Share schemes

133 Fixed-fee service and insurance contracts

134 Principal undertakings

135 Independent Auditors' Report – Company

136 Company Balance Sheet

137 Notes to the Company Financial Statements

143 Gas and Liquids Reserves

144 Five Year Record

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.

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			2011 (restated) (ii)	
	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)	**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

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.

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

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	2012 Interest expense £m	2012 Interest income £m	2012 Total £m	2011 Interest expense £m	2011 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	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
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.

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.

Directors' Report – Business Review
Directors' Report – Governance
Financial Statements
Directors' Report – Appendix
Shareholder Information

Financial Statements

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.

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						2011					
	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	2,526	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		2012			2011		
CGU(s)	Principal acquisitions to which goodwill and intangibles with indefinite useful lives relate	**Carrying amount of goodwill £m**	**Carrying amount of indefinite-lived intangible asset (i) £m**	**Total £m**	Carrying amount of goodwill (restated) (iii) £m	Carrying amount of indefinite-lived intangible asset (i) £m	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.

Financial Statements

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.

Financial Statements

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).

Financial Statements

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

Directors' Report – Business Review
Directors' Report – Governance
Financial Statements
Directors' Report – Appendix
Shareholder Information

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.

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	2012 Level 1 £m	2012 Level 2 £m	2012 Level 3 £m	2012 Total £m	2011 Level 1 £m	2011 Level 2 £m	2011 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).

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 6¹⁴⁄₈₁p 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.

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:

	2012		2011	
Life expectancy at age 65 for a member	**Male Years**	**Female Years**	Male Years	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.

	2012		2011	
Impact of changing material assumptions	**Increase/ decrease in assumption**	**Indicative effect on scheme liabilities %**	Increase/ decrease in assumption	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

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.

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

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

SUPPLEMENTARY INFORMATION CONTINUED

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.

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
Senior Statutory Auditor
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
London
27 February 2013

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
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

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 Pension liabilities £m	2012 Pension assets £m	2011 Pension liabilities (restated) £m	2011 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

NOTES TO THE COMPANY FINANCIAL STATEMENTS CONTINUED

XI. Shareholders' funds and reserves

	Profit and loss account									
	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	**2012 Total £m**	2011 (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.

Financial Statements

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.

Appendix to the Directors' Report

Contents

146 Performance Measures

146 British Gas

148 Centrica Energy

148 Centrica Storage

149 Direct Energy

150 Corporate Responsibility

152 Biographies of the Board of Directors and Senior Executives

154 Other Statutory Information

Appendix to the Directors' Report

PERFORMANCE MEASURES

British Gas

	FY 2012	FY 2011	Δ%	H2 2012	H2 2011	Δ%
Total customer accounts (period end) ('000)	**24,982**	25,364	(1.5)	24,982	25,364	(1.5)
Total customer households (period end) ('000)	**11,745**	11,997	(2.1)	11,745	11,997	(2.1)
Joint product households (period end) ('000)	**2,149**	2,207	(2.6)	2,149	2,207	(2.6)
Gross revenue (£m)	**13,857**	12,403	12	6,650	6,049	10
Operating cost (excluding bad debt) (£m)	**1,418**	1,425	(0.5)	707	678	4.3
Operating profit (£m)	**1,093**	1,005	9	530	487	9

2011 gross revenue has been restated to reflect the reclassification of the British Gas New Energy business from Residential energy supply to Residential services and the reclassification of the British Gas Community Energy business from Residential Energy supply to Business energy supply and services.
Total customer accounts has been restated to exclude the Water Supply Pipe product, which has been incorporated into the Plumbing and Drains product.

Residential energy supply

	FY 2012	FY 2011	Δ%	H2 2012	H2 2011	Δ%
Customer accounts (period end)						
Gas ('000)	**8,905**	9,139	(2.6)	8,905	9,139	(2.6)
Electricity ('000)	**6,751**	6,742	0.1	6,751	6,742	0.1
Total ('000)	**15,656**	15,881	(1.4)	15,656	15,881	(1.4)
Estimated market share (%)						
Gas	**39.9**	41.2	(1.3) ppts	39.9	41.2	(1.3) ppts
Electricity	**25.1**	25.2	(0.1) ppts	25.1	25.2	(0.1) ppts
Average consumption						
Gas (therms)	**494**	443	12	218	181	20
Electricity (kWh)	**3,794**	3,805	(0.3)	1,875	1,858	0.9
Total consumption						
Gas (mmth)	**4,460**	4,099	9	1,945	1,669	17
Electricity (GWh)	**25,683**	25,602	0.3	12,696	12,600	0.8
Gross revenue (£m)						
Gas	**5,884**	4,903	20	2,668	2,248	19
Electricity	**3,237**	3,027	7	1,646	1,580	4.2
Total	**9,121**	7,930	15	4,314	3,828	13
Transmission and metering costs (£m)						
Gas	**1,327**	1,212	9	676	611	11
Electricity	**915**	782	17	477	401	19
Total	**2,242**	1,994	12	1,153	1,012	14
Total environmental costs (£m)	**732**	599	22	347	347	0.0
Total social costs (£m)	**89**	78	14	29	40	(28)
Operating profit (£m)	**606**	544	11	261	263	(0.8)
Operating margin (%)	**6.6**	6.9	(0.3) ppts	6.1	6.9	(0.8) ppts

2011 gross revenue and operating profit have been restated to reflect the reclassification of the British Gas New Energy business from Residential energy supply to Residential services and the reclassification of the British Gas Community Energy business from Residential energy supply to Business energy supply and services.
The definition of total environmental costs has been restated and includes CERT, CESP, ROCs, carbon and FIT costs.

Appendix to the Directors' Report

Residential services

	FY 2012	FY 2011	Δ%	H2 2012	H2 2011	Δ%
Customer product holdings (period end)						
Central heating service contracts ('000)	**4,663**	4,696	(0.7)	4,663	4,696	(0.7)
Kitchen appliances care (no. of customers) ('000)	**465**	476	(2.3)	465	476	(2.3)
Plumbing and drains care ('000)	**1,714**	1,728	(0.8)	1,714	1,728	(0.8)
Home electrical care ('000)	**1,444**	1,462	(1.2)	1,444	1,462	(1.2)
Other contracts ('000)	**116**	122	(4.9)	116	122	(4.9)
Total holdings ('000)	**8,402**	8,484	(1.0)	8,402	8,484	(1.0)
Domestic central heating installations ('000)	**94**	105	(10)	50	51	(2.0)
Gross revenue (£m)						
Central heating service contracts	**839**	807	4.0	435	411	6
Central heating installations	**258**	295	(13)	137	144	(4.9)
Other	**577**	542	6	291	278	5
Total	**1,674**	1,644	1.8	863	833	3.6
Operating profit (£m)	**312**	269	16	187	159	18
Operating margin (%)	**18.6**	16.4	2.2 ppts	21.7	19.1	2.6 ppts

2011 gross revenue has been restated to reflect the reclassification of the British Gas New Energy business from Residential energy supply to Residential services.
UK residential product holdings have been restated to exclude the Water Supply Pipe product, which has been incorporated into the Plumbing and Drains product.

Business energy supply and services

	FY 2012	FY 2011	Δ%	H2 2012	H2 2011	Δ%
Customer supply points (period end)						
Gas ('000)	**322**	363	(11)	322	363	(11)
Electricity ('000)	**602**	636	(5)	602	636	(5)
Total ('000)	**924**	999	(8)	924	999	(8)
Average consumption						
Gas (therms)	**2,737**	2,629	4.1	1,156	1,130	2.3
Electricity (kWh)	**27,521**	25,732	7	14,014	12,895	9
Total consumption						
Gas (mmth)	**940**	986	(4.7)	399	413	(3.4)
Electricity (GWh)	**17,110**	16,731	2.3	8,581	8,320	3.1
Gross revenue (£m)						
Gas	**1,014**	931	9	443	416	6
Electricity	**1,841**	1,713	7	929	866	7
Business services	**207**	185	12	101	106	(5)
Total	**3,062**	2,829	8	1,473	1,388	6
Transmission and metering costs (£m)						
Gas	**178**	188	(5)	85	94	(10)
Electricity	**409**	372	10	212	188	13
Total	**587**	560	5	297	282	5
Operating profit (£m)	**175**	192	(9)	82	65	26
Operating margin (%)	**5.7**	6.8	(1.1) ppts	5.6	4.7	0.9 ppts

2011 gross revenue and operating profit have been restated to reflect the reclassification of the British Gas Community Energy business from Residential energy supply to Business energy supply and services.

Appendix to the Directors' Report

PERFORMANCE MEASURES CONTINUED

Centrica Energy

	FY 2012	FY 2011	Δ%	H2 2012	H2 2011	Δ%
Operating profit (£m)	**1,230**	1,023	20	548	492	11
Gas						
Gas production volumes (mmth)						
Morecambe	**740**	817	(9)	378	418	(10)
Other UK and Netherlands	**883**	933	(5)	403	419	(3.8)
Norway	**557**	164	240	381	82	365
Trinidad and Tobago	**261**	246	6	131	162	(19)
Total	**2,441**	2,160	13	1,293	1,081	20
Oil and condensate production volumes (mmboe)						
UK and Netherlands	**7.4**	7.8	(5)	3.5	3.5	0.0
Norway	**8.9**	4.7	89	5.9	2.1	181
Total	**16.3**	12.5	30	9.4	5.6	68
Total production volumes (mmboe)	**56.7**	48.2	18	31.0	23.2	34
Average gas sales price (p/therm)	**54.7**	51.6	6	56.7	52.5	8
Average oil and condensate sales price (£/boe)	**62.8**	57.2	10	63.4	56.9	11
DDA costs (£/boe)	**9.8**	10.1	(3.0)	10.1	9.5	6
Lifting costs (£/boe)	**9.7**	9.9	(2.0)	10.1	10.1	0.0
Total production and overhead costs (£m)	**1,374**	1,127	22	803	544	48
Exploration and appraisal costs (£m)	**139**	97	43	108	51	112
Operating profit (£m)	**919**	769	20	411	355	16
Estimated net proven and probable reserves of gas (BCF)	**2,376**	2,019	18	nm	nm	nm
Estimated net proven and probable reserves of liquids (mmboe)	**129**	73	77	nm	nm	nm
Total net proven and probable reserves (mmboe)	**525**	410	28	nm	nm	nm
Power						
Power generated (GWh)						
Gas-fired	**8,952**	14,973	(40)	4,046	7,542	(46)
Renewables	**533**	596	(11)	287	321	(11)
Nuclear	**12,004**	11,157	8	6,050	4,966	22
Total	**21,489**	26,726	(20)	10,383	12,829	(19)
Achieved Clean Spark Spread (£/MWh)	**10.7**	10.1	6	11.2	9.3	20
Achieved power price (including ROCs) (£/MWh) – renewables	**105.7**	111.2	(4.9)	111.3	124.7	(11)
Achieved power price (£/MWh) – nuclear	**49.6**	48.5	2.3	49.8	50.4	(1.2)
Operating profit (£m)	**311**	254	22	137	137	0.0

Centrica Storage

	FY 2012	FY 2011	Δ%	H2 2012	H2 2011	Δ%
Average SBU price (in period) (pence)	**31.0**	30.0	3.3	33.9	25.2	35
Gross revenue (£m)						
Standard SBUs	**141**	136	3.7	77	58	33
Other	**61**	48	27	34	29	17
Total	**202**	184	10	111	87	28
Operating profit (£m)	**89**	75	19	53	36	47

Appendix to the Directors' Report

Direct Energy	FY 2012	FY 2011	Δ%	H2 2012	H2 2011	Δ%
Total residential energy and services accounts (period end) ('000)	**5,856**	5,647	3.7	5,856	5,647	3.7
Gross revenue (£m)	**6,015**	6,117	(1.7)	3,096	3,021	2.5
Operating profit (£m)	**331**	312	6	165	138	20
Residential energy supply						
Customer accounts (period end) ('000)	**3,455**	3,364	2.7	3,455	3,364	2.7
Gross revenue (£m)	**2,357**	2,416	(2.4)	1,147	1,126	1.9
Operating profit (£m)	**156**	161	(3.1)	55	56	(1.8)
Operating margin (%)	**6.6**	6.7	(0.1) ppts	4.8	5.0	(0.2) ppts
Business energy supply						
Gas sales (mmth)	**793**	714	11	372	297	25
Electricity sales (GWh)	**51,378**	46,350	11	27,443	24,159	14
Gross revenue (£m)	**2,690**	2,748	(2.1)	1,394	1,372	1.6
Operating profit (£m)	**129**	110	17	69	52	33
Operating margin (%)	**4.8**	4.0	0.8 ppts	4.9	3.8	1.1 ppts
Residential and business services						
Contract relationships (period end) ('000)	**2,401**	2,283	5	2,401	2,283	5
On demand and installation jobs ('000)	**670**	703	(5)	316	372	(15)
Gross revenue (£m)	**532**	520	2.3	279	271	3.0
Operating profit (£m)	**33**	28	18	22	19	16
Operating margin (%)	**6.2**	5.4	0.8 ppts	7.9	7.0	0.9 ppts

On demand and installation jobs has been restated to reflect management reporting.

Upstream and wholesale energy	FY 2012	FY 2011	Δ%	H2 2012	H2 2011	Δ%
Gas production volumes (mmth)	**549**	567	(3.2)	270	287	(6)
Oil and liquids production volumes (mmboe)	**1.1**	0.7	57	0.5	0.4	25
Total production volumes (mmboe)	**10.1**	10.0	1.0	4.9	5.1	(3.9)
Power generated (GWh)	**6,336**	5,247	21	3,016	2,924	3.1
Gross revenue (£m)	**436**	433	0.7	276	252	10
Operating profit (£m)	**13**	13	0.0	19	11	73
Estimated net proven and probable reserves of gas (BCF)	**581**	603	(3.6)	nm	nm	nm
Estimated net proven and probable reserves of liquids (mmboe)	**11**	8	38	nm	nm	nm
Total net proven and probable reserves (mmboe)	**108**	109	(0.9)	nm	nm	nm

Direct Energy with comparator year of 2011 restated to remove effect of foreign exchange movements

	FY 2012	FY 2011	Δ%	H2 2012	H2 2011	Δ%
Revenue (£m)						
Residential energy supply	**2,357**	2,425	(2.8)	1,147	1,128	1.7
Business energy supply	**2,690**	2,782	(3.3)	1,394	1,378	1.2
Residential and business services	**532**	523	1.7	279	272	2.6
Upstream and wholesale energy	**436**	437	(0.2)	276	252	10
Direct Energy revenue	**6,015**	6,167	(2.5)	3,096	3,030	2.2
Operating profit (£m)						
Residential energy supply	**156**	163	(4.3)	55	56	(1.8)
Business energy supply	**129**	111	16	69	52	33
Residential and business services	**33**	28	18	22	19	16
Upstream and wholesale energy	**13**	13	0.0	19	11	73
Direct Energy operating profit	**331**	315	5.0	165	138	20

2011 figures restated at 2012 weighted average exchange rate

Appendix to the Directors' Report

PERFORMANCE MEASURES CONTINUED

Corporate Responsibility

Treating customers fairly

Metric	Unit	2012 target	2012 performance	2011 performance	What's next
British Gas Net Promoter Score (NPS)	See note[(i)] for a definition of NPS	Achieve a score of +27 by end of 2012	+30[(ii)] (high performance range)	+26[(iii)] (high performance range)	To remain within the high performance range within each business
Direct Energy Net Promoter Score (NPS)		Achieve a score of +27 by end of 2012	+39[(ii)] (high performance range)	+28[(iii)] (high performance range)	
Vulnerable households impacted by British Gas initiatives	Number	Measure only	2.1 million[(ii)]	1.7 million[(iii)]	Continue to support our most vulnerable customers through the British Gas Energy Trust and obligations such as the Warm Home Discount

(i) NPS measures customers' responses to the question 'How likely would you be to recommend us (0–10 scale)?' The score is calculated by the percentage of customers defined as promoters (scoring 9–10) minus the percentage defined as detractors (0–6).

(ii) Assured by Deloitte LLP for the 2012 Annual Report. See centrica.com/report2012/assurance to view Deloitte's full assurance statement and the Basis of Reporting.

(iii) Assured by Deloitte LLP for the 2011 Annual Report. See centrica.com/report2011/assurance to view Deloitte's full assurance statement and the Basis of Reporting.

Achieving reductions in carbon emissions

Metric	Unit	2012 target	2012 performance	2011 performance	What's next
Lifetime carbon savings driven by the Carbon Emissions Reduction Target (CERT)	Tonnes of CO_2 saved	16.3 million[(i)] by end of 2012	15.0 million	14.6 million	Whilst the CERT programme ended on 31 December 2012 we will continue to work towards our obligations in this area
Smart meter installations	Number of meters installed (cumulative since 2009)	1.1 million cumulative by end of 2012	881,794[(ii)]	459,422[(iii)]	British Gas will continue to be the UK leader in smart meter installations
Carbon intensity of power generation	g CO_2/kWh	Reduce our UK power generation carbon intensity to 270 by end of 2012	UK: 159[(iv)] Group wide: 197	UK: 199[(v)(vi)] Group wide: 220[(v)]	Reduce our Group power generation carbon intensity to 260 by end of 2020
Absolute carbon emissions (Scope 1 and Scope 2 emissions as defined by the Greenhouse Gas Protocol)	Tonnes CO_2 equivalent	Measure only	7.2 million	8.1 million	
Internal carbon footprint (property, fleet and travel)	Tonnes CO_2 equivalent	Reduce the carbon footprint of our core offices, company vehicles and travel by 20% by 2015	91,988 a 2% reduction on 2011	94,092[(iii)] a 5% reduction on 2010	Continue to work to our 2015 target By the end of 2012 we had achieved a 21% reduction from 2007 base year

(i) All yearly CERT targets have been amended retrospectively to a consistent figure of 16.3 million tonnes of CO_2 saved per year to enable a simple comparison between British Gas' overall five year performance against the five year CERT obligation volume of 96.3 million tonnes of CO_2.

(ii) Assured by Deloitte LLP for the 2012 Annual Report. See centrica.com/report2012/assurance to view Deloitte's full assurance statement and the Basis of Reporting. This figure represents cumulative smart meter installations for residential and business customers. Only data representing 514,482 smart meter installations was assured by Deloitte due to the historical nature of the data.

(iii) This is an updated figure to that reported previously, following subsequent validation carried out on data.

(iv) 2012 data subject to final EU Emissions Trading System (ETS) verification.

(v) Restated due to verification by EU ETS.

(vi) Assured by Deloitte LLP for 2011. See centrica.com/responsibility to view Deloitte's full assurance statement and the Basis of Reporting for 2011.

Appendix to the Directors' Report

Safety

Metric	Unit	2012 target	2012 performance	2011 performance	What's next
Lost time injury frequency rate (LTIFR)[(i)]	Per 100,000 hours worked	Reduce LTIFR to 0.225 by end of 2012	0.20[(ii)]	0.25[(iii)]	We aim to reduce accident rates across all businesses, with increasing focus on the TRIR as a representative measure. At a Group level we aim to maintain, and if possible further improve, our LTIFR of 0.20
Total recordable injury rate (TRIR)[(iv)]	Per 100,000 hours worked	Reduce TRIR to 1.59 by end of 2012	1.42	1.66[(iii)]	
Road safety incidents rate – low severity	Per 1 million km driven	Measure only	5.0	7.5[(iii)]	We aim to continue the reduction in road safety incidents through proactive driver safety programmes
Road safety – number of high severity incidents	Number	Measure only	6	10[(iii)]	
Fatalities	Number	Measure only	0	0[(iii)]	
Significant process safety event	Number	0	0[(ii)]	2	We aim to continue to focus on the management of our major accident hazards. We track detailed leading metrics at an executive level, with the ultimate aim of zero significant process safety events

(i) A lost time injury is defined as an incident arising out of Centrica's operations which leads to an injury where the employee or contractor is not available to work for one day or more, excluding the day that the injury occurred.

(ii) Assured by Deloitte LLP for the 2012 Annual Report. See centrica.com/report2012/assurance to view Deloitte's full assurance statement and the Basis of Reporting.

(iii) Assured by Deloitte LLP for the 2011 Annual Report. See centrica.com/report2011/assurance to view Deloitte's full assurance statement and the Basis of Reporting.

(iv) A recordable injury is an injury that requires more than first aid. This includes fatalities, lost time, restricted duty and medical aid.

Our people

Metric	Unit	2012 target	2012 performance	2011 performance	What's next
Diversity – female and male	Percentage	Promote diversity in leadership roles and recruitment	28.3 female 71.7 male	29.1 female 70.9 male	Continue to promote diversity in leadership roles and recruitment
Retention	Percentage	Maintain the good levels of retention	89.7	89.5[(i)]	Encourage and maintain healthy retention levels
Absence	Days per full time employee	Maintain and improve levels of absenteeism	8.2	7.3[(ii)]	Focus on driving down absence in British Gas
Employee engagement	Mean score out of 6	4.91	4.72[(iii)]	n/a	Implement action plans driven out of the 2012 engagement survey

(i) Assured by Deloitte LLP for the 2011 Annual Report. See centrica.com/report2011/assurance to view Deloitte's full assurance statement and the Basis of Reporting.

(ii) Restated due to change in methodology for recording absence.

(iii) Assured by Deloitte LLP for the 2012 Annual Report. See centrica.com/report2012/assurance to view Deloitte's full assurance statement and the Basis of Reporting.

Responsible business practices

Metric	Unit	2012 target	2012 performance	2011 performance	What's next
Total community contributions[(i)]	£ million	Invest in local communities and relevant charitable organisations	233.6[(ii)]	67.7	Make a positive contribution through the way we operate and by investing in, and engaging with, communities where we work in the UK, North America and other parts of the world
Total employee volunteering hours[(iii)]	Number of hours	Support our employees in their volunteering efforts	43,623	81,969	

(i) Includes charitable donations calculated through the London Benchmarking Group methodology, combined with the cost of voluntary and mandatory programmes to support vulnerable customers in the UK.

(ii) Comprising £224 million in mandatory and £343,000 in voluntary contributions for vulnerable customers in the UK, and £9.3 million in charitable contributions. This includes £5.5 million Group cash donations (2011: £1.8 million). The London Benchmarking Group methodology was applied for calculating our charitable contributions, with major investments in education and young people (£3.4 million), environment (£2.8 million), health (£1.1 million) and social welfare (£1.2 million).

(iii) Includes volunteering hours during and outside of working hours.

BOARD OF DIRECTORS AND SENIOR EXECUTIVES

Board of Directors

1. Sir Roger Carr
Chairman (66)

Sir Roger 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. During 2011, he was appointed president of the CBI and a member of the UK Prime Minister's Business Advisory Group. 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.

2. Sam Laidlaw
Chief Executive (57)

Sam joined Centrica as Chief Executive 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 UK Prime Minister's Business Advisory Group. Previously he was executive vice president of the Chevron Corporation, chief executive officer at Enterprise Oil and president and chief operating officer at Amerada Hess. He is a trustee of the medical charity RAFT.

3. Phil Bentley
Managing Director, British Gas (54)

Phil joined Centrica as Group Finance Director on 13 September 2000, a position he held until the end of February 2007 when he was appointed Managing Director, British Gas. Phil was also Managing Director, Europe between July 2004 and September 2006. He will stand down from his role as Managing Director of British Gas and as a Director of Centrica plc on 30 June 2013. He was appointed as a non-executive director of IMI plc in October 2012 and will take up the position of chairman of their audit committee from May 2013.

4. Margherita Della Valle
Non-Executive Director (47)

Margherita joined the Board on 1 January 2011 and is Deputy Chairman of the Audit Committee. She will become Chairman of the Audit Committee in July 2013. In October 2010 she was appointed group financial controller of Vodafone Group Plc, prior to which she was chief financial officer for the group'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.

5. Mary Francis CBE
Senior Independent Director (64)

Mary joined the Board on 22 June 2004 and is Senior Independent Director, Chairman of the Corporate Responsibility Committee and Deputy Chairman of the Nominations Committee. In October 2012 she was appointed to the Board of Swiss Reinsurance Company Ltd and she has been proposed for appointment to the board of the Swiss Re Group, subject to election at their AGM in April 2013. 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.

6. Mark Hanafin
Managing Director, Centrica Energy (53)

Mark joined Centrica as Managing Director, Centrica Energy on 14 July 2008. He 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 (GEC) having qualified as a chartered engineer.

Appendix to the Directors' Report

7. Lesley Knox
Non-Executive Director (59)

Lesley 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.

8. Nick Luff
Group Finance Director (45)

Nick joined Centrica as Group Finance Director on 1 March 2007. 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.

9. Andrew Mackenzie
Non-Executive Director (56)

Andrew joined the Board on 1 September 2005. Andrew has been appointed as CEO of BHP Billiton with effect from 10 May 2013 and he will resign as a Non-Executive Director of Centrica at that date. He will not, therefore, seek re-election as a Director at the Annual General Meeting to be held on 13 May 2013.

10. Ian Meakins
Non-Executive Director (56)

Ian joined the Board on 1 October 2010. In July 2009 he joined the Wolseley Group as chief executive. He was previously chief executive 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.

11. Paul Rayner
Non-Executive Director (58)

Paul joined the Board on 22 September 2004 and is Chairman of the Audit Committee. He will step down from the Board on 31 December 2013 and 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.

12. Chris Weston
Managing Director, North America (49)

Chris was appointed to the Board on 1 July 2009 upon his appointment as Managing Director, North America. He was previously Managing Director, British Gas Services from June 2005. Prior to this, he was Managing Director, British Gas Business from January 2002. He joined Centrica 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.

Senior Executives

13. Grant Dawson
General Counsel & Company Secretary (53)

Grant has been General Counsel & Company Secretary of Centrica since the demerger from British Gas plc in February 1997, having joined British Gas in October 1996.

14. Jill Shedden
Group Director, Human Resources (47)

Jill was appointed Group Director, Human Resources on 1 July 2011. Previously she was HR Director for Centrica Energy. She joined British Gas plc as a graduate in 1988 and has since held a wide range of roles across the Group including HR Director for British Gas Business and British Gas Residential.

BOARD OF DIRECTORS AND SENIOR EXECUTIVES PHOTOGRAPHS ON PAGES 6 AND 7

OTHER STATUTORY INFORMATION

Management report
The Directors' Report for the year can be found on pages 5 to 75 and pages 146 to 154. The management report for the year, as required by the Disclosure and Transparency Rules, is incorporated by reference within the Directors' Report.

Major acquisitions and disposals
Full details of acquisitions and disposals are disclosed in the Business Review on pages 5 to 50 and notes 30 and 31 to the Financial Statements on pages 119 and 120.

Events after the balance sheet date
Events after the balance sheet date are disclosed in note 36 to the Financial Statements on page 123.

Related party transactions
Related party transactions are set out in note 34 to the Financial Statements on page 122.

Creditor payment policy
It is the Group's policy to:

- agree the terms of payment in advance with the supplier;
- ensure that suppliers are aware of the terms of payment; and
- pay in accordance with contractual and other legal obligations.

The number of days' purchases outstanding as at 31 December 2012 was 33 (2011: 33) for the Group (excluding Centrica Energy Limited) and 32 (2011: 30) for the Company.

Essential contractual arrangements
The Group has contractual and other arrangements with various third parties. Whilst the loss of, or disruption to, certain of these arrangements could affect the operations of the Group temporarily, this Annual Report does not contain information about these third parties as none of the arrangements are considered to be essential to the Group's business.

Significant agreements – change of control
The following are significant agreements to which the Company is party which take effect, alter or terminate in the event of a change of control in the Company following a takeover bid:

- as part of the demerger in 1997, BG Group plc (which is a separately listed company and not a part of the Centrica Group) assigned ownership of the British Gas trade marks and related logos to Centrica for use in Great Britain. BG Group plc has the right to call for a re-assignment of this intellectual property if control of Centrica is acquired by a third party; and
- in 2009, Centrica entered into certain transactions with EDF Group in relation to an investment in British Energy, an owner and operator of nuclear power stations in the UK. The transactions include rights for EDF Group and Centrica to offtake power from existing and new build British Energy nuclear power stations and to invest in new build nuclear power stations. As part of these arrangements, on a change of control of Centrica, the Group loses its rights to participate on the Boards of the companies in which it has invested and on Technical Committees for new nuclear development. Furthermore, where the acquirer is not located in certain specified countries, EDF Group is able to require Centrica to sell out its investments.

Charitable and political donations
During the year, the Group made cash charitable donations to support the community of £5.5 million (2011: £1.8 million). Total community contributions and related activities on community support are described in the Appendix to the Directors' Report on page 151. Centrica's political donations policy states that Centrica operates on a politically neutral basis. No donations were made by the Group for political purposes during the year. However, in accordance with the Federal Election Campaign Act, Direct Energy has authorised the establishment of a Political Action Committee (PAC), to facilitate voluntary political contributions by its US employees. The PAC is not controlled by Centrica and contributions from the fund are determined by a governing board of PAC members. Participation in the PAC is voluntary for eligible employees. In 2012, contributions to the PAC by employees amounted to US$10,900. The PAC made 19 political donations totalling US$7,500.

Share capital
The Company was authorised at the 2012 AGM to allot shares within certain limits and as permitted by the Companies Act. A renewal of this authority will be proposed at the 2013 AGM. The Company's issued share capital as at 31 December 2012, together with details of shares issued during the year, is set out in note 26 to the Financial Statements on page 115.

Each ordinary share of the Company carries one vote. Further information on the voting and other rights of shareholders are set out in the Articles and in the explanatory notes which accompany notices of general meetings, all of which are available on the Company's website.

Authority to purchase shares
The Company was authorised at the 2012 AGM to purchase its own shares, within certain limits and as permitted by the Articles. A renewal of this authority will be proposed at the 2013 AGM. Shares repurchased may be cancelled or retained as treasury shares to accommodate requirements for shares under the Group's share incentive schemes. No shares were purchased under this authority during 2012, however, on 4 February 2013 the Company announced a £500 million share repurchase programme.

Material shareholdings
At 31 December 2012 Centrica had received notification of the following material shareholdings pursuant to the Disclosure and Transparency Rules:

	31 December 2012		
	Ordinary shares	**% of share capital**	Nature of holding
Invesco Limited	**258,200,185**	**4.97%**	Indirect
Legal & General Group	**201,705,927**	**3.88%**	Direct

No changes have been disclosed in accordance with these rules in the period 31 December 2012 to 27 February 2013.

Shareholder Information

Contents

156 Financial Calendar

157 Shareholder Information

161 Glossary

163 Index

FINANCIAL CALENDAR 2013-2014

* Provisional dates

SHAREHOLDER INFORMATION

Managing your shares

Please contact our Registrar, Equiniti, to manage your shareholding. Information is also available through the Shareholder Centre on our website, including frequently asked questions and forms available to download to help you to:

- transfer your shares;
- change your registered name or address;
- register a lost share certificate and obtain a replacement;
- consolidate your share certificates;
- manage your dividend payments;
- buy, sell or transfer shares through Centrica FlexiShare;
- notify the death of a shareholder; and
- register for electronic communications.

You can also manage your shareholding online by registering for Shareview via the electronic communications section of the Shareholder Centre.

When contacting Equiniti or registering online, you should have your shareholder reference number at hand. This can be found on your share certificate or dividend tax voucher.

If you hold less than 2,500 shares, you will be able to change your registered address or set up a dividend mandate instruction over the phone. For security, if you hold more than 2,500 shares, you will need to put this in writing.

Please note, if you receive more than one copy of documents that we send you, it is likely that you have more than one account on the share register, perhaps with a slightly different name or address. If you write to Equiniti and give them the shareholder reference numbers, they will be able to combine your accounts into one.

We work with a specialist tracing agency, ProSearch, to identify shareholders whose details are not up to date and who have outstanding cash entitlements. Please notify Equiniti when you move house to ensure you continue to receive all our communications.

Centrica FlexiShare

FlexiShare is an easy way to hold Centrica shares without a share certificate. Your shares would be held in a nominee company, Equiniti Corporate Nominees Limited, however you are able to attend and vote at general meetings as if the shares were held in your own name. Holding your shares in this way is free and comes with a number of benefits:

- low cost share-dealing rates, full details of which are available on the Shareholder Centre together with dealing charges;
- quicker settlement periods for buying and selling shares; and
- the opportunity to join the Dividend Reinvestment Plan.

Dividends

Dividends on Centrica shares are usually paid in June and November. Details of the dividends for the year ended 31 December 2012 can be found in note 10 to the Financial Statements on page 94.

You are encouraged to have your dividends paid directly to your bank or building society account. This means that you will receive the money on the day it is paid which avoids any risk of missing cheques. If you do choose to receive your dividends in this way, a consolidated tax voucher will be sent to you in March each year.

If you do not have a UK bank or building society account, Equiniti are able to pay dividends in local currencies in over 30 countries. For a small fee, you could have your dividends converted from sterling and paid into your designated bank account, usually within five days of the dividend being paid.

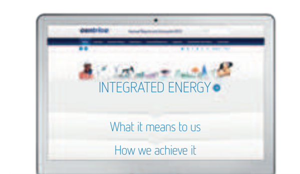
Buying and selling shares with a share certificate

If you wish to buy or sell Centrica shares and hold a share certificate, you can do this:

- by using the services of a stockbroker or high street bank; or
- through telephone or online services.

In order to sell your shares in this way, you will need to present your share certificate at the time of sale.

MANAGE MORE ONLINE



You can view and manage your shareholding online. Go to the electronic communications section of the Shareholder Centre on our website at centrica.com/shareholdercentre.

SHAREHOLDER INFORMATION CONTINUED

Shareholder communication

Changes in legislation have meant it is now possible for us to communicate to a greater extent with shareholders using our website. We strongly encourage our shareholders to receive communications electronically as it allows us to make considerable savings, both environmentally and financially, and allows you to:

- view the Annual Report and Annual Review on the day they are published;
- receive an email alert when shareholder communications are available;
- cast your AGM vote; and
- manage your shareholding quickly and securely.

In April 2012, together with Equiniti, we introduced an electronic queries service to enable our shareholders to manage their investment 24/7. Since then Equiniti have:

- addressed 2,000 queries using the electronic queries service;
- handled over 19,500 calls; and
- completed 150,000 transactions.

Details of this service can be found at shareview.co.uk.

A wealth of other information is available on our website, including:

- regular updates about our business;
- comprehensive share price information;
- financial results; and
- dividend payment dates and amounts.

Share repurchase programme

On 4 February 2013, the Company announced it would launch a £500 million share repurchase programme over the next 12 months. Further information is available from the Shareholder Centre on our website.

American Depository Receipts (ADR)

We have an ADR programme, trading under the symbol CPYYY. Centrica's ratio is one ADR being equivalent to four ordinary shares. Further information is available from the Shareholder Centre or please contact:

ADR Depositary
The Bank of New York Mellon – Shareowner Services
PO Box 358516, Pittsburgh, PA
Email: shrrelations@bnymellon.com or via bnymellon.com/shareowner
Telephone: 1-888-269-2377 toll-free in the US or +1 201-680-6825 from outside the US
Website: adrbnymellon.com

ShareGift

It may be that you have a small number of shares which would cost you more to sell these than they are worth. It is possible to donate these to ShareGift, a registered charity, who provide a free service to enable you to dispose charitably of such shares. More information on this service can be obtained from sharegift.org or call +44 (0) 207 930 3737.

Centrica share history

Centrica's shares were first traded on the London Stock Exchange on 17 February 1997 following the demerger from British Gas plc. Since then there have been three events affecting the share capital, as shown below, with full details available from Equiniti and on our website:

- 1999 share consolidation;
- 2004 share consolidation; and
- 2008 rights issue.

CONTACT EQUINITI

Contact details for our registrar

Equiniti, Aspect House, Spencer Road, Lancing, West Sussex BN99 6DA, United Kingdom

Telephone: 0871 384 2985* and outside the UK +44 121 415 7061
Textphone: 0871 384 2255* and outside the UK +44 121 415 7028

Online: https://help.shareview.co.uk

* Calls to this number cost 8 pence per minute plus network extras. Lines are open from 8.30 am to 5.30 pm, Monday to Friday, UK time.

Beware of share fraudsters

Shareholders are cautioned to be very wary of any unsolicited advice, offers to buy shares at a discount, sell your shares at a premium or offers of free company reports.

£200 million

The Financial Services Authority (FSA) report that such scams cost investors in excess of £200 million each year.

Centrica is aware that some of its shareholders have recently received unsolicited phone calls or letters from individuals or companies offering to buy or sell Centrica shares on very favourable terms. These communications imply a connection with Centrica and are often from overseas based 'brokers' who are very persuasive and extremely persistent, with professional websites to support their activities.

If you do receive such an approach, you are encouraged to take the following steps:

- obtain the full name of the person and organisation and make a record of any other information they give you, for example telephone number, address, web address;
- if the caller persists, simply hang up; and
- report the matter to the FSA so that they can investigate. You are able to do this online at fsa.gov.uk/consumerinformation/scamsandswindles or by calling them on 0845 606 1234*.

You are advised to deal only with financial services firms that are authorised by the FSA. Check the firm is properly authorised by the FSA before getting involved by visiting fsa.gov.uk/fsaregister. If you do deal with an unauthorised firm, you will not be eligible to receive payment under the Financial Services Compensation Scheme if anything goes wrong.

Details of any share-dealing services that Centrica endorses are available on our website and are included in Company mailings.

* Call rates may vary.

FINANCIAL SERVICES AUTHORITY

Check if financial services firms are authorised by the FSA by visiting fsa.gov.uk/fsaregister

Accessibility

If you would like this Annual Report in an alternative format, such as large print, Braille or CD, you can request these in the following ways:

Telephone: 0800 111 4371 Textphone: 18001 0800 111 4371

Please note that these numbers should be used to request copies of alternative formats only. For general shareholder enquiries, please use the Centrica shareholder helpline 0871 384 2985*.

* Calls to this number cost 8 pence per minute plus network extras. Lines are open from 8.30 am to 5.30 pm, Monday to Friday, UK time.

SHAREHOLDER INFORMATION CONTINUED

Analysis of shareholders as at 31 December 2012

Distribution of shares by type of holder	Number of holdings	Number of shares
Nominees and institutional investors	15,873	4,864,978,409
Individuals	664,959	334,041,265
Total	680,832	5,199,019,674

Size of holding	Number of holdings	Shares
1–500	498,376	113,974,972
501–1,000	104,122	72,172,111
1,001–5,000	70,199	130,079,922
5,001–10,000	4,891	34,028,164
10,001– 50,000	2,028	37,480,234
50,001–100,000	227	16,740,141
100,001– 1,000,000	592	226,893,474
1,000,001 and above	397	4,567,650,656
Total	680,832	5,199,019,674

As at 31 December 2012 there were 72,048 participants in FlexiShare, with an aggregate shareholding of 128,975,197 shares registered in the name of Equiniti Corporate Nominees Limited.

ONLINE

This Annual Report can be viewed online. To see more go to centrica.com/report2012

GLOSSARY

$	Refers to US dollars unless specified otherwise
<1 year	Less than 1 year
>1 year	Greater than 1 year
2P	Proven and probable
AFS	Available-for-sale
AGR	Advanced gas-cooled reactor
Associate	An entity in which the Group has an equity interest and over which it has the ability to exercise significant influence
bbl	Barrels of oil
BCF	Billion cubic feet
CER	Certified emissions reduction (carbon emissions certificate)
CERT	Carbon emissions reduction target
CGU	Cash generating unit
CPI	Consumer Price Index
DECC	Department of Energy and Climate Change
DPS	Total dividend per share (excluding special dividends) paid in respect of each financial year
EBITDA	Earnings before interest, tax, depreciation and amortisation
EMIR	European Market Infrastructure Regulation
Employee engagement	Individuals' perception of different components within an organisation, which in turn has a measurable impact on business performance
EMR	Energy Market Reform
EPS	Earnings per share. This measure of performance is calculated as profit before other costs and depreciation of fair value uplifts to property, plant and equipment from strategic investments and exceptional items and certain re-measurements for the year, attributable to equity shareholders of the parent company, divided by the weighted average number of shares in issue during the year
EUA	European Union allowance (carbon emissions certificate)
FSA	Financial Services Authority
FTSE 100	Financial Times Stock Exchange 100 share index, an average of share prices in the 100 largest, most actively traded companies on the London Stock Exchange
FVLCS	Fair value less costs to sell
g CO_2/kWh	Grammes of carbon dioxide per kilowatt hour
GFRMC	Group Financial Risk Management Committee
GWh	Gigawatt hour
IAS 19	The International Accounting Standard related to Employee Benefits. These financial reporting rules include requirements related to pension accounting
IAS 39	The International Accounting Standard related to financial instruments (recognition & measurement)
IFRIC	International Financial Reporting Interpretations Committee
IFRS	International Financial Reporting Standard
Jointly controlled entity	A joint venture which involves the establishment of an entity to engage in economic activity, which the Group controls jointly with its fellow venturers
kWh	Kilowatt hour
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 market-based 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
LNG	Liquefied natural gas
LTIFR	Long term injury frequency rate (previously referred to as LTIR). A lost time injury is defined as an incident arising out of Centrica's operations which leads to an injury where the employee or contractor is not available to work for one day or more, excluding the day that the injury occurs

GLOSSARY CONTINUED

MiFID	Markets in Financial Instruments Directive
mmboe	Million barrels of oil equivalent
mmth	Million therms
MWh	Megawatt hour
NBV	Net book value
NGO	Non-governmental organisation
NPS	Net Promoter Score. NPS measures customer advocacy by responses to the question 'How likely would you be to recommend us (0–10 scale)?' The score is calculated by the percentage of customers defined as promoters (scoring 9–10) minus the percentage defined as detractors (0–6)
PP&E	Property, plant and equipment
Process safety	A significant process safety event is 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
PRT	Petroleum revenue tax
RMR	Retail Market Review
ROC	Renewable obligation certificate
RPI	Retail Price Index
SCT	Supplementary charge associated with UK Corporation Tax
Securities	Comprised of 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
Spark spread	The difference between the price of a unit of electricity and the cost of the gas used to generate it
TSR	Total shareholder return measures the return to shareholders in terms of the growth of a £100 investment in the Company's shares, assuming that dividends and returns of capital are reinvested. We compare our TSR with those of the other 99 members of the FTSE 100
TWh	Terrawatt hour
VAT	Value added tax
VIU	Value in use
Vulnerable customer	A customer is vulnerable if for reasons of age, health, disability or severe financial insecurity, they are unable to safeguard their personal welfare or the personal welfare of other members of the household

INDEX

Accounting policies, measures and judgements 38, 76, 82-83, 106, 124-130, 136, 138-139

Accumulated amortisation/depreciation and impairment 99, 102, 126, 127, 138-139

Accumulated other comprehensive income/loss 79, 115, 116, 118

Acquisitions, business combinations 38, 44, 47, 49, 57, 82, 84, 98, 99, 102, 105, 108

Alternative Formats 159

Assets and liabilities 79, 82, 84, 88-89, 93-94, 103, 106, 108, 115, 125-126, 128, 131-132, 137, 144, 161

Auditors – re-appointment 55, 60

Auditors – remuneration 55, 60, 120-121

Auditors – report to the members of Centrica plc 55, 69, 76, 135

Awards 20

Balance Sheet 38, 76, 123, 124-129, 154

Balance Sheet – Company 136

Balance Sheet – Group 80

Biomass 16, 29, 41, 47

Board of Directors 6-7, 129, 152-153

Borrowings, bank overdrafts, loans and others 37, 80-81, 89, 93, 96-98, 103, 109, 111, 113, 115, 119, 125, 127-128, 131, 137-139, 144

British Gas 5-6, 10, 12-13, 14-15, 19-20, 22-25, 40-44, 86-92, 144, 146-147, 150-151

Business combinations 38, 84, 99, 119-120, 125

Business principles 8, 40, 46

Capital management 38

Carbon intensity, emissions 24, 39-42, 122, 150, 161

Cash and cash equivalents 81, 96, 98, 109, 112, 114, 128

Cash Flow Statement 76, 81, 97-98, 118, 128

CCGT (combined cycle gas turbine) 12, 17, 28-29

Centrica Energy 12-13, 14-15, 20, 26-29, 41, 43, 82, 86-91, 132, 143-144, 148, 150-151

Centrica Storage 13-14, 21, 30-31, 86-91, 132, 143-144, 148

CERT (Carbon Emissions Reduction Target scheme) 24, 122, 146, 150, 161

CESP (Community Energy Saving Programme) 24, 146

Chairman’s Statement 5-8

Change of control 67, 154

Charitable and political donations 154

Chief Executive’s Review 9-17

Climate change 30, 41, 44, 47, 84, 161

Commitments, contingencies and indemnities 66, 84, 111, 121-122, 131, 142

Committees 7, 54, 58-59, 130, 154

Communities 8, 20, 40-41, 46, 151

Competition – North America 15, 32, 44, 46-47

Competition – UK 44, 46-47, 50

Continuing operations 4, 22, 26, 30, 32, 36-37, 78, 81-83, 86-88, 90-95, 97, 128, 144

Corporate governance 55-56, 66, 76, 152

Corporate responsibility 3, 7-8, 39-40, 42-43, 46, 57, 69, 152

Cost of sales 78, 84, 91, 124-125, 127, 133, 144

Costs of continuing operations 91

Creditor payment policy 154

Customers – health and safety 7, 23, 33

Customers – numbers 15, 24-25, 33, 47, 104, 147

Customers – service 3, 10-11, 13-17, 20, 22-25, 32, 34, 39-43, 46, 50, 57, 150

Deferred corporation tax liabilities and assets 108, 140

Direct Energy 12-13, 14-15, 17, 19, 21, 32-35, 40-42, 86-92, 132, 143-145, 149, 150-151

Directors – Annual Incentive Scheme 56, 66

Directors – biographies 152-153

Directors – directors’ indemnities 53

Directors – disclosure of information to auditors 60

Directors – emoluments 68-70

Directors – pensions 74, 85, 116-119

Directors – re-election 8, 56, 75, 153

Directors – remuneration policy 61, 66-67

Directors – responsibility statement 76, 135

Directors – service contracts 67

Directors – share interests 53

Directors – training 7, 54-55

Disposals 47, 83, 99, 102, 108, 120, 138, 143, 154

Dividends 3, 5, 14, 18, 37, 65-66, 71, 73, 79, 81, 94, 103, 123, 128, 142, 157, 161-162

Dyno 99

Earnings per ordinary share 4, 78, 95-96, 144

Electricity Market Reform 16-17, 44

Electronic communications 157

Employees – costs 91

Employees – engagement 3, 19, 23, 43, 57, 65-66, 151

Employees – numbers 5, 7, 20-21, 42, 91

Employees – pensions 128, 133, 137, 141-142

Employees – policies 43

Employees – training 19, 40, 42-43, 45

Energy chain 12

Energy efficiency 13-14, 21-25, 32, 41, 46-47, 84

EPS (adjusted basic earnings per share) 4, 18, 37, 64-66, 69-71, 125, 133, 137, 161

Europe 2, 46, 59, 96, 106, 110, 114, 131, 143, 152-153

Events after the Balance Sheet date 38, 123, 154

Exceptional items and certain re-measurements 65, 78, 82-83, 87, 91-95, 105, 132, 144

INDEX CONTINUED

Executive team 54
Fair value 36-38, 82-85, 93, 95, 100-101, 109-111, 113, 161
Financial calendar 156
Financial instruments – derivative 105
Financial instruments – fair value 82
Financial instruments – hedge accounting 37, 96, 98
Financial Review 36-38
Financial risk management 111-114, 130-132, 138, 161
Five-year record 144
Fixed fee service and insurance contracts 123, 125, 133
FSA (Financial Services Authority) 54, 96, 133, 159, 161
Gas and liquids reserves 84, 143
Gas exploration 26
Gas production 9, 21, 26-27, 32, 35, 38, 41, 94, 101-102, 109, 120, 127, 132, 134, 148-149
Glossary 161-162
Goodwill and other intangible assets 99, 100-101, 144
Group Financial Statements 124, 134-135, 137-142
Health and safety 3, 7, 14, 17, 19, 23, 26-27, 31, 33, 35, 42, 57, 65-67, 151, 162
Hedge accounting 105-107, 129, 137
Income Statement 78-79, 91-92
Indemnities 53, 84, 122
Interest 93
International Financial Reporting Standards 38, 76, 82
Inventories 97, 104, 127
Joint ventures and associates 36-37, 78-79, 81-82, 88, 93-94, 97, 103-104, 115, 122, 126-127, 132, 134, 144
Key performance indicators (KPIs) 3, 15, 18-19, 39, 64-66, 71-72, 125, 137
Liquefied natural gas (LNG) 13, 16-17, 29, 31, 41, 48, 121, 134, 161
Low carbon 2, 9-10, 13, 16, 39, 41
LTIFR (lost time injury frequency rate) 3, 14, 19, 23, 33, 42, 44, 65-66, 151, 161
Net interest 36-37, 78, 93, 107
NPS (Net Promoter Score) 15, 19, 23, 34, 40-41, 65, 72, 150, 162
Nuclear 2, 4-5, 10, 12, 14, 16, 20, 26-29, 37-38, 41-42, 45, 47, 55, 83-85, 92, 95, 103-104, 122-123, 130, 132, 134, 148, 152, 154
Ofgem 14, 23-24, 40-41, 44, 122
Other equity 79, 116, 132-133
Outsourcing and offshoring 121
Power generation 16-17, 20-21, 26, 32, 35-37, 41, 45, 47, 85, 102, 124-125, 130, 132, 134, 150
Prices, wholesale and retail 5, 14, 16-17, 23-24, 28, 30, 34-38, 40, 44, 46-48, 50, 85, 100-101, 130-131
Principal undertakings 134, 138
Property, plant and equipment 81-82, 87, 88, 90, 95, 97, 102, 121, 127, 130, 144, 162
Provisions 4, 38, 85, 97, 108-109, 113, 138-140
Related party transactions 122, 154
Renewables – wind farm 5, 12, 14, 16, 26, 29, 38-39, 41, 83, 85, 102-103, 109, 120, 122, 134, 138, 142, 148
Renewables Obligation Certificate (ROC) 126, 162
Reserves 1-2, 10, 12, 16, 20, 26-28, 32, 35, 132, 143
Retail Market Review 40, 44
Rights Issue 73, 144, 158
Risk Management 32, 35, 38, 55, 111-114, 129-132, 138
Segmental analysis 86-90, 132
Shale gas 5, 16, 29, 41, 48, 57
Share-based payments 91, 122, 125, 133, 137, 138
Share capital 79, 81, 83, 95, 115, 128, 132, 142, 154, 158,
Shareholder information 156-160, 161-162
Share repurchase 4-5, 14, 17, 38, 123, 154, 158
Share schemes – employee 43, 56, 67, 69, 79, 115-116, 125, 133, 136-138, 142
Share schemes – Executive 64, 67, 69-70, 73-75, 133
Shares – analysis of shareholders 160
Shares – funds 136, 142
Shares – material shareholdings 154
Shares – price 49, 58, 63, 65, 69, 70, 73, 140, 158
Shares – share capital 79, 81, 83, 95, 115, 128, 132, 142, 154, 158
Smart meters 13, 15, 17, 20, 22, 25, 47, 84
Sources of finance 38, 96-97
Statement of Changes in Equity 76, 79, 142
Statutory Information 154
Strategic Priorities 2, 6, 9-11, 16, 32, 40, 47, 66
Supplementary information 124-134
Supply chain 17, 39, 44
Tangible fixed assets 137
Tax and taxation 4-5, 16, 18-19, 23, 36-38, 65, 80-81, 85, 87-89, 92-95, 98, 100-101, 103-104, 108, 112, 115-118, 120, 126, 128, 132-133, 137-144, 157, 161-162
Trade marks 154
Trade payables 107, 113, 128
Trade receivables 91, 104-105, 113, 122, 128
Trade Unions 50, 116
TRIR (total recordable injury rate) 42, 151
TSR (total shareholder return) 3, 10, 18, 63-66, 69-72, 125, 133, 137, 162
Vulnerable customers 15, 24, 40-41, 43, 46, 150-151
Warm Home Discount (WHD) 15, 24, 43-44, 150

Disclaimer

This Annual Report and Accounts does not constitute an invitation to underwrite, subscribe for, or otherwise acquire or dispose of any Centrica shares or other securities.

This Annual Report and Accounts contains certain forward-looking statements with respect to the financial condition, results, operations and businesses of Centrica plc. These statements and forecasts involve risk and uncertainty because they relate to events and depend on circumstances that will occur in the future. There are a number of factors that could cause actual results or developments to differ materially from those expressed or implied by these forward-looking statements and forecasts.

Past performance is no guide to future performance and persons needing advice should consult an independent financial adviser.

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Designed and produced by
CONRAN DESIGN GROUP

Photography by David Hares, Mike Abrahams, Igor Emmerich, Charlie Fawell and David Partner.

Printed by CPI Colour Limited
ISO14001, FSC certified and CarbonNeutral®.

CENTRICA PLC
Registered office: Millstream,
Maidenhead Road, Windsor,
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Company registered in England
and Wales No. 3033654
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