Remuneration Policy

The Policy in the following pages sets out the Executive incentive arrangements applicable from 27 April 2015 onwards.

EXECUTIVE DIRECTORS' REMUNERATION

The Remuneration Committee (Committee) believes that the remuneration arrangements are completely aligned with the Executives' underlying commitment to act in the best interests of sustainable shareholder value creation, whilst ensuring behaviours remain consistent with the governance and values of the business.

Key objectives of reward framework

- The Policy aims to deliver a remuneration package:
- to attract and retain high calibre Executives in a challenging and competitive business environment;
- that delivers an appropriate balance between fixed and variable compensation for each Executive;
- that places a strong emphasis on performance, both short term and long term;
- strongly aligned to the 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.

Reward framework

The core design of the total remuneration framework for Executives ensures that a substantial portion of the maximum opportunity is dependent upon performance as indicated in the chart below. Total remuneration comprises fixed pay and variable performance related pay, which is further divided into short-term incentive (with a one-year performance period) and long-term incentive (with a three-year performance period).

Short-term incentives relate to awards under the Annual Incentive Plan (AIP) and long-term incentives relate to awards under the Long Term Incentive Plan (LTIP) both of which are described in the Remuneration Policy table.

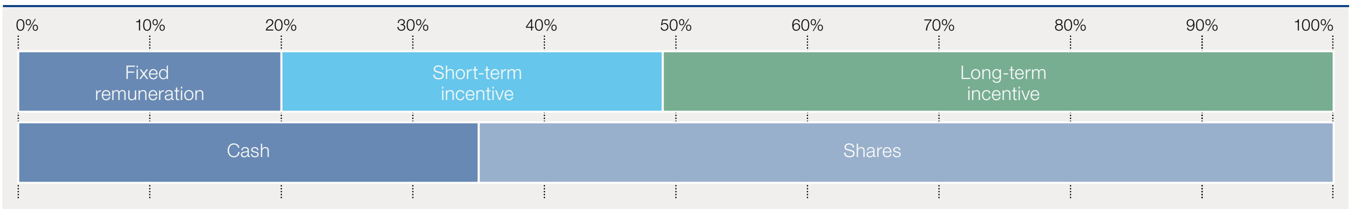
Key performance indicators (KPIs) have been selected that align with our purpose: to deliver energy and services to satisfy the changing needs of our customers and also support our long-term financial goals. In addition, our underlying principles of operating safely and with an engaged workforce are included.

The KPIs, set out in detail on pages 18 and 19 of the Annual Report and Accounts, influence the design and underpin the selection of performance criteria used within the incentive arrangements as demonstrated in the KPIs and incentives 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.

In addition, Executives are subject to a minimum shareholding guideline. Under the LTIP there are mandatory holding periods of three to five years from grant or award date, to provide further alignment with the returns to our shareholders.

Remuneration principles

- the potential maximum remuneration that Executives could receive is a key consideration 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, shareholder views, market changes, skills availability, competitive pressure and/or the economic climate when considering Executive remuneration. In so doing, the Committee follows similar principles that apply when remuneration is considered for all other employees within the Group; and
- benchmarking against UK cross-industry comparator organisations of similar size and complexity is used to assist the Committee in evaluating market movement and the relative competitive position of Executive remuneration to ensure that packages offered support the attraction and retention of high calibre individuals.



KPIs and incentives

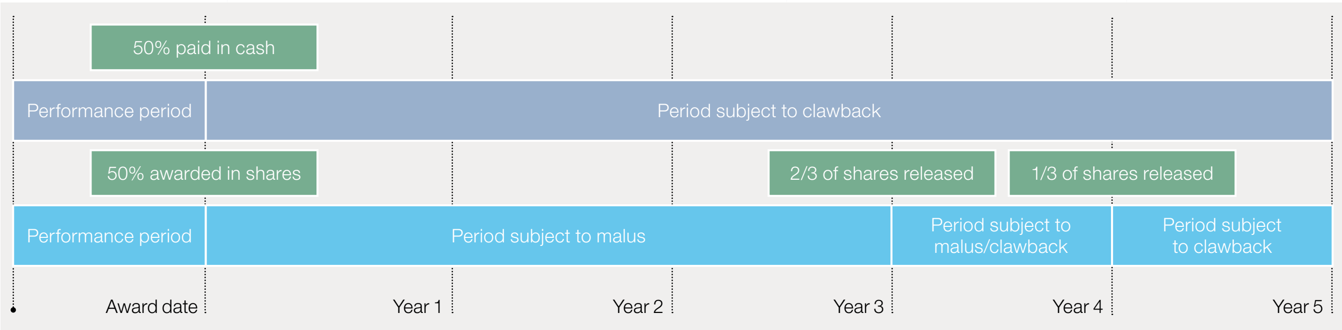
KPI	Incentive link
Adjusted operating cash flow (AOCF)	AIP primary financial measure
Adjusted operating profit	LTIP economic profit three-year measure
Adjusted basic earnings per share (EPS)	LTIP EPS growth measure
Total shareholder return (TSR)	AIP deferred share investment and minimum shareholding requirement
Lost time injury frequency rate (LTIFR)	LTIP non-financial KPI dashboard
Process safety	LTIP non-financial KPI dashboard
Customer satisfaction	LTIP non-financial KPI dashboard
Employee engagement	LTIP non-financial KPI dashboard

Remuneration Policy table

The table below sets out the Remuneration Policy that was approved at the AGM on 27 April 2015 and applies to Executives.

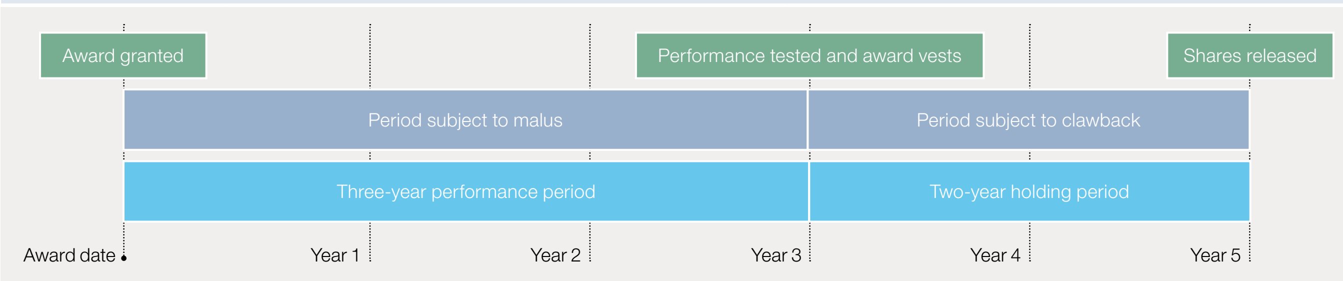
Purpose and link to strategy	Operation and clawback	Maximum opportunity	Performance measures
BASE PAY/SALARY			
Reflects the scope and responsibility of the role and the skills and experience of the individual. Salaries are set at a level sufficient to allow the Company to compete for international talent and to recruit, motivate and retain individuals of the correct calibre to execute our strategy.	Base salaries are reviewed annually, taking account of performance, market conditions and pay in the Group as a whole. Changes are usually effective from 1 April each year. This is consistent with the previously approved policy.	Ordinarily, base salary increases in percentage terms will be in line with increases awarded to other employees of the Group. Increases may be made above this level to take account of individual circumstances such as a change in responsibility, progression in the role or a significant increase in the scale or size of the role. The base salary for an Executive will not exceed £1 million per annum. This is consistent with the previously approved policy.	Not applicable.
SHORT-TERM INCENTIVE PLAN			
Designed to reward the delivery of key strategic priorities for the year. These priorities position the Group for strong short-term financial performance, in service of longer-term strategic goals.	The Annual Incentive Plan (AIP), together with the Long-Term Incentive Plan (LTIP), replaces the previous Annual Incentive Scheme (AIS), Deferred and Matching Share Scheme (DMSS) and Long-Term Incentive Scheme (LTIS). The AIP is designed to incentivise and reward the achievement of demanding financial and individual strategically aligned performance objectives. Following measurement of the performance outcome, half of the AIP award is paid in cash. The other half is required to be deferred into shares, two-thirds of which are released after three years and the remaining third after four years. Dividends are payable on the shares during the restricted period. If overall business performance is not deemed satisfactory, an individual's AIP payment for the year may be reduced or forfeited, at the discretion of the Committee. Malus and clawback apply to the cash and share awards (see policy table notes).	Maximum of 200% of base salary. Half the maximum is payable for on-target performance. The minimum award is 0%. The maximum was 180% of base salary under the previously approved policy. The 20% of base salary increase in maximum opportunity is offset by the 80% of base salary reduction in maximum long-term incentive opportunity and longer deferral periods.	Up to 75% of base salary based on individual strategic objectives aligned to the Group's strategic priorities, with the remainder based on adjusted operating cash flow (for 2016 onwards) and adjusted operating profit adjusted for movements in tax and capital employed (for 2015). Assessed over one financial year. Up to 72% of base salary was based on individual strategic objectives under the previously approved policy.

AIP timeline



Purpose and link to strategy	Operation and clawback	Maximum opportunity	Performance measures
LONG-TERM INCENTIVE PLAN			
Assists with Executive retention and incentivises an appropriate balance between short-term performance and long-term value creation for shareholders. Encourages sustainable high performance. Provides a direct link between remuneration and KPIs, reinforcing the desire for sustainable high performance over the long term.	The Long Term Incentive Plan (LTIP) simplifies the previous long-term incentive arrangements which were delivered under two separate schemes. LTIP awards are granted to Executives each year based on a percentage of base salary at the point of award. Shares vest at the end of a three-year performance period, depending on the achievement against the Company performance targets, but are not released until the fifth anniversary of the award date. LTIP awards are usually delivered as conditional shares which vest at the end of the three-year performance period. Awards may also be granted as nil-cost options with a seven-year exercise period. It is a requirement of the LTIP that the net shares are held for a further two years following the vesting date. Malus applies to the shares during the three-year performance period and clawback applies to the shares during the two-year retention period (see policy table notes). Dividend equivalents are calculated at the end of the performance period on any conditional LTIP share awards or nil-cost options. Dividend equivalents are paid as additional shares or as cash. If overall performance is not deemed satisfactory, the award for any year may be reduced or forfeited, at the discretion of the Committee.	Maximum of 300% of base salary plus dividend equivalents. The minimum vesting level is 0%. The maximum was 380% of base salary plus dividend equivalents under the previously approved policy.	One-third based on EPS over the three-year performance period. One-third based on absolute aggregate EP over the three-year performance period. One-third based on non-financial KPI dashboard. Where performance falls between stated points, vesting is calculated on a straight-line basis. The weighting to non-financial KPIs has marginally increased from 30% to 33.3% compared with the long-term incentive arrangements in the previously approved policy. This reflects the Committee's view of the appropriate balance between financial and non-financial measures at two-thirds/one-third respectively.

LTIP timeline



Purpose and link to strategy	Operation and clawback	Maximum opportunity	Performance measures
PENSION			
Positioned to provide a competitive post-retirement benefit, in a way that manages the overall cost to the Company.	Incoming Executives are entitled to participate in a Company money purchase pension arrangement or to take a fixed salary supplement (calculated as a percentage of base salary, which is excluded from any bonus calculation) in lieu of pension entitlement. The Group's policy is not to offer defined benefit arrangements to new employees at any level, unless this is specifically required by applicable legislation or an existing contractual agreement. This is consistent with the previously approved policy.	30% salary supplement for Chief Executive and 25% salary supplement for all other Executives. This is consistent with the previously approved policy.	Not applicable.
	Executives employed prior to 2013 are entitled to participate in a Centrica pension arrangement or to receive a fixed salary supplement in lieu of pension entitlement in accordance with the terms of their contracts. Mark Hanafin is entitled to receive a salary supplement equal to 40% of his base salary in lieu of pension or to participate in a Company money purchase pension arrangement. We would continue to honour defined benefit pension arrangements in the event of an individual being promoted to the Board who retains a contractual entitlement to such a pension benefit. This is consistent with the previously approved policy.	40% salary supplement for Executives employed prior to 2013. This is consistent with the previously approved policy.	
BENEFITS			
Positioned to ensure competitiveness with market practice.	The Group offers Executives a range of benefits including some or all of: • a company-provided car and fuel, or a cash allowance in lieu; • life assurance and personal accident insurance; • health and medical insurance for the Executive and their dependants; • health screening; and • a contribution towards financial planning advice. This is consistent with the previously approved policy.	Cash allowance in lieu of company car – £22,000 per annum. The benefit in kind value of other benefits will not exceed 5% of base salary. This is consistent with the previously approved policy.	Not applicable.
RELOCATION AND EXPATRIATE ASSISTANCE			
To enable the Group to recruit or promote the right individual into a role, to retain key skills and to provide career opportunities.	Assistance may include (but is not limited to) removal and other relocation costs, housing or temporary accommodation, education, home leave, repatriation and tax equalisation. This is consistent with the previously approved policy.	Maximum of 100% of base salary. This is consistent with the previously approved policy.	Not applicable.
ALL-EMPLOYEE SHARE PLANS			
Provide an opportunity for employees to voluntarily invest in the Company.	UK-based Executives are entitled to participate in the HMRC-approved Sharesave and Share Incentive Plan (SIP) on the same terms as all other eligible employees. The Sharesave plan offers a three or five-year savings period, with up to a 20% discount to the market value of the shares at the point of grant. The SIP currently offers partnership and matching shares. Dividends paid on SIP shares may be reinvested in the plan. This is consistent with the previously approved policy.	Maximum contribution limits are set by legislation. Levels of participation allowed by the Board are within these limits and apply to all participants. The SIP currently awards one free matching share for every two partnership shares purchased, up to a maximum of 22 matching shares per month, although the plan allows for higher levels of matching award. This is consistent with the previously approved policy.	Not applicable.

Policy table notes

The Committee reserves the right to make any remuneration payments and payments for loss of office, notwithstanding that they are not in line with the Remuneration Policy set out above, where the terms of the payment were agreed before the policy came into effect, at a time when the relevant individual was not an Executive of the Company or, in the opinion of the Committee, the payment was not in consideration for the individual becoming an Executive of the Company. For these purposes payments include the amounts paid in order to satisfy awards of variable remuneration and, in relation to an award over shares, the terms of the payment are agreed at the time the award is granted.

The Committee may make minor amendments to the policy set out above (for regulatory, exchange control, tax or administrative purposes or to take account of a change in legislation) without obtaining shareholder approval for that amendment.

PENSION ARRANGEMENTS APPLYING TO EXECUTIVES

Centrica Unfunded Pension Scheme (CUPS)

All registered scheme benefits are subject to HMRC guidelines and the Lifetime Allowance.

The CUPS defined contribution (DC) section provides benefits for individuals not eligible to join the CUPS defined benefit (DB) section and for whom registered scheme benefits are expected to exceed the Lifetime Allowance. The CUPS DC section is offered as a direct alternative to a cash salary supplement.

The CUPS DB section was closed to new members in October 2002.

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.

PERFORMANCE MEASURES

Adjusted earnings per share (EPS)

EPS is the Company's basic earnings per share adjusted for exceptional items and certain re-measurements net of taxation.

Adjusted operating cash flow (AOCF)

AOCF is the net cash flow from operating activities (which includes taxes paid) adjusted to include dividends received from joint ventures and associates and to exclude payments relating to exceptional items, UK defined benefit pension deficit contributions and movements in variation margin and cash collateral that are included in net debt.

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.

Further details of these performance measures are provided in notes 2, 4(f) and 10 of the financial statements, in the Annual Report and Accounts.

Non-financial KPI dashboard

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

- lost time injury frequency rate (LTIFR);
- significant process safety event;
- British Gas net promoter score (NPS);
- Direct Energy NPS; and
- employee engagement.

Employee engagement survey data is collected by an external provider and compared against an independent benchmark database.

Deloitte LLP reviewed the non-financial KPIs linked to executive remuneration and provided limited assurance using the International Standard on Assurance Engagements ISAE 3000 (Revised). The 2016 assurance statement and the Basis of Reporting, are available at centrica.com/assurance.

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

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

MALUS AND CLAWBACK

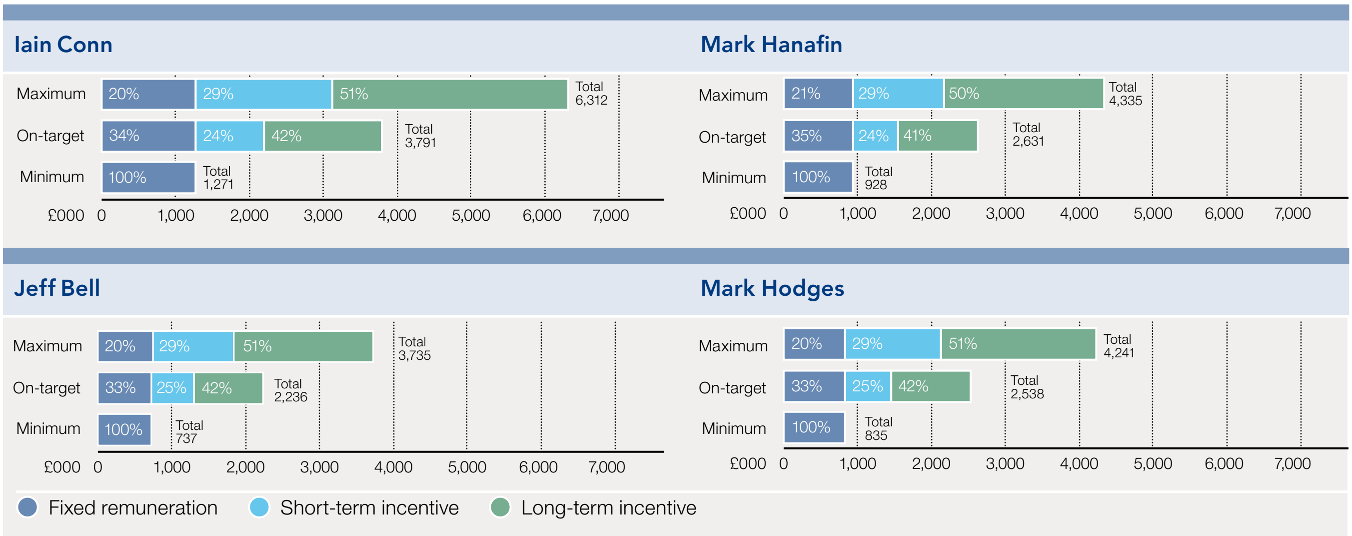
The Committee can apply malus (that is reduce the number of shares in respect of which an award vests) or delay the vesting of awards if it considers it appropriate where a participant has engaged in gross misconduct or displayed inappropriate management behaviour which fails to reflect the governance and values of the business or where the results for any period have been restated or appear inaccurate or misleading.

Where an award has vested, the resulting shares will generally be held for a period during which they may be subject to clawback in the event that the Committee determines that one or more of the circumstances above has occurred.

Total remuneration by performance scenario

The charts below indicate the minimum, on-target and maximum remuneration that could be received by each Executive, excluding share price movement, under the Remuneration Policy. Assumptions made for each scenario are:

- minimum – fixed remuneration only (base salary at current level, together with pension and benefits as set out in the Remuneration Policy table);
- on-target – fixed remuneration plus target AIP (as set out in the Remuneration Policy table) and expected value under the LTIP on vesting of 50%; and
- maximum – fixed remuneration plus maximum AIP opportunity (as set out in the Remuneration Policy table) and maximum levels of vesting under the LTIP.



Discretion and judgement

It is important that the Committee maintains the flexibility to apply discretion and judgement to achieve fair outcomes as no remuneration policy and framework, however carefully designed and implemented, can pre-empt every possible scenario. The Committee needs to be able to exercise appropriate discretion to determine whether mechanistic or formulaic outcomes are fair, in context and can be applied in an upward or downward manner when required. Judgement is applied appropriately by the Committee, for example when considering the political and social pressures on the business, the impact of significant movements in external factors such as commodity prices, in setting and evaluating delivery against individual performance targets to ensure they are considered sufficiently stretching and that the maximum and minimum levels are appropriate and fair.

The Committee has absolute discretion to decide who receives awards, the level of the awards under the incentive plans and the timing, within the parameters set in the rules.

In the case of a corporate action, the Committee can agree when a corporate action applies to a share award, whether awards pay out or are rolled over in this situation and how any special dividend might apply. The Committee also maintains the discretion to adjust any awards in the event of a variation of capital, for example to maintain the incentive value at the level originally intended.

The Committee retains discretion, consistent with market practice, regarding the operation and administration of the incentive plans including, but not limited to, the following:

- determination of the result of any disputes relating to the interpretation of the rules;
- alteration of the terms of the performance targets if it feels that they are no longer a fair measure of the Company's performance, as long as the new targets are not materially less challenging than the original ones; and
- determination that any award is forfeit in whole or in part.

The Committee also retains the discretion to forfeit or clawback deferred awards under the AIP if it determines that prior performance which resulted in the annual bonus being awarded was discovered to be a misrepresentation of results or inappropriate management behaviour which fails to reflect the governance or values of the business.

Recruitment policy

The Committee will apply the same remuneration policy during the policy period as that which applies to existing Executives when considering the recruitment of a new Executive in respect of all elements of remuneration as set out in the Remuneration Policy table.

Whilst the maximum level of remuneration which may be granted would be within plan rules and ordinarily subject to the maximum opportunity set out in the Remuneration Policy table, in certain circumstances, an arrangement may be established specifically to facilitate recruitment of a particular individual up to 25% above the maximum opportunity, albeit that any such arrangement would be made within the context of minimising the cost to the Company. The policy for the recruitment of Executives during the policy period includes the opportunity to provide a level of compensation for forfeiture of bonus entitlements and/or unvested long-term incentive awards from an existing employer, if any, and the additional provision of benefits in kind, pensions and other allowances, as may be required in order to achieve a successful recruitment.

The policy on the recruitment of new Non-Executive Directors (Non-Executives) during the policy period would be to apply the same remuneration elements as for the existing Non-Executives. It is not intended that variable pay, day rates or benefits in kind be offered, although in exceptional circumstances such remuneration may be required in currently unforeseen circumstances. The Committee will include in future Remuneration Reports details of the implementation of the policy as utilised during the policy period in respect of any such recruitment to the Board.

Termination policy

The Committee carefully considers compensation commitments in the event of an Executive's termination. The aim is to avoid rewarding poor performance and to reduce compensation to reflect the departing Executive's obligations and to mitigate losses.

Save for summary dismissal, the policy is to either continue to provide base pay, pension and other benefits for any unworked period of notice or, at the option of the Company, to make a payment in lieu of notice comprising base pay only. Typically any payment in lieu of notice will be made in monthly instalments and reduce, or cease completely, in the event that remuneration from new employment is received. An AIP award for the year in which the termination occurs may be made following the normal year end assessment process, subject to achievement of the agreed performance measures and time-apportioned for the period worked. Any award would be payable at the normal time with a 50% deferral and no new long-term incentive plan awards would be made.

Except in cases of death in service, the policy is not to vest any existing long-term incentive plan awards earlier than their normal vesting date. In all cases any vesting remains subject to satisfaction of the associated performance conditions and will be time-apportioned for the period worked.

Executives leaving following resignation will forfeit any potential AIP award for the performance year in which the resignation occurs and all unvested LTIP awards. In addition, Executives summarily dismissed will also forfeit any deferred shares. Deferred awards can also 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 or where the results for any period appear inaccurate or misleading.

On a change of control, existing LTIP awards will be exchanged on similar terms or vest to the extent that the performance conditions have been met at the vesting date and be time-apportioned to the vesting date, subject to the overriding discretion of the Committee.

Pay and employment conditions across the Group

The Group operates in a number of different environments and has many employees who carry out a range of 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. The ratio between fixed and variable pay for employees differs by level, geographic location and business unit.

A number of performance-related incentive schemes are operated across the Group which differ in terms of structure and metrics from those applying to Executives.

The Group also offers a number of all-employee share schemes in the UK and North America and Executives participate on the same basis as other eligible employees.

Performance measures applying to Executives are cascaded down through the organisation and Group employment conditions include high standards of health and safety and employee wellbeing initiatives.

No consultation in respect of Executive remuneration takes place with employees during the year.

Shareholding guidelines

Minimum shareholding guidelines are in place for Executive Directors to build and maintain a value of shares over a five-year period equal to two times base salary.

External appointments of Executives

It is the Company's policy to allow each Executive 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 Executive and are set out in the Directors' Annual Remuneration Report each year.

NON-EXECUTIVE DIRECTORS' REMUNERATION

Remuneration policy

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

Terms of appointment

Non-Executives, including the Chairman, do not have service contracts. Their appointments are subject to Letters of Appointment and the Articles of Association.

Remuneration Policy table

Purpose and link to strategy	Operation	Maximum opportunity	Performance measures
CHAIRMAN AND NON-EXECUTIVE DIRECTOR FEES			
Sufficient level to secure the services of individuals possessing the skills, knowledge and experience to support and oversee the Executive Directors in their execution of the Board's approved strategies and operational plans.	The fee levels for the Chairman are reviewed every two years by the Remuneration Committee. The fee levels of the Non-Executives are reviewed every two years by the Executive Committee. Non-Executives are paid a base fee for their services. Where individuals serve as Chairman of a Committee of the Board, additional fees are payable. The Senior Independent Director also receives an additional fee. **Fee levels from 1 January 2016:** Base fee £72,500 per annum. The following additional fees apply: • Chairman of Audit Committee – £25,000 per annum; • Chairman of Remuneration Committee – £20,000 per annum; • Chairman of Safety, Health, Environment, Security and Ethics Committee – £20,000 per annum; and • Senior Independent Director – £20,000 per annum. **Fee levels from May 2010 to 31 December 2015:** Base fee £65,000 per annum. The following additional fees applied: • Chairman of Audit Committee – £23,000 per annum; • Chairman of Remuneration Committee – £20,000 per annum; • Chairman of Corporate Responsibility Committee – £20,000 per annum; • Chairman of Safety, Health, Environment, Security and Ethics Committee (established July 2015) – £20,000 per annum; and • Senior Independent Director – £20,000 per annum. The Company reserves the right to pay a Committee membership fee in addition to the base fees. Non-Executives are able to use 50% of their fees, after appropriate payroll withholdings, to purchase Centrica shares. Dealing commission and stamp duty is paid by the Non-Executive. The Non-Executives, including the Chairman, do not participate in any of the Company's share schemes, incentive plans or pension schemes. Non-Executives will be reimbursed for business expenses relating to the performance of their duties including travel, accommodation and subsistence. In certain circumstances these, or other incidental items, may be considered a 'benefit in kind' and if so may be grossed up for any tax due.	The maximum level of fees payable to Non-Executives, in aggregate, is set out in the Articles of Association.	Not applicable.

SERVICE CONTRACTS

The Executive Directors' service contracts expire on their 65th birthday. Service contracts provide that either the Executive or the Company may terminate the employment by giving one year's written notice and that the Company may pay base salary only in lieu of notice.

All Executive and Non-Executive Directors are required to be re-elected at each AGM.

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.