Remuneration Report

Scott Wheway
Non-Executive Director

On behalf of the Board, I am pleased to present the Remuneration Committee's report for 2018.

In May 2018, following an extensive consultation exercise, we asked shareholders to approve our revised Remuneration Policy (Policy) which we sought to ensure was more closely aligned to our strategy and the delivery of long-term shareholder value through returns and growth (see box below). We were pleased to receive the support of over 95% of our shareholders for our revised Policy.

This report describes how we have implemented this Policy in its first year of operation.

Principal changes to Remuneration Policy approved by shareholders in 2018

- Introduced Total Shareholder Return (TSR) into the Long term Incentive Plan (LTIP).
- LTIP therefore has four measures: 33% weighting to relative TSR and 22% weighting to each of economic profit, cash flow growth and non-financial KPIs.
- Increased the weighting of financial performance within the Annual Incentive Plan (AIP) and moved to 75% financial and 25% personal objectives.
- Increased the shareholding requirement for Executive Directors from 200% to 300% of salary, and introduced a post-cessation shareholding requirement.
- Simplified our bonus deferral to three-year cliff vesting (rather than phased vesting).
- Reduced the maximum pension salary supplement level for newly recruited Executive Directors to 25% of salary.

Joiners and leavers during the year

In operating our Policy during the year, we determined the remuneration arrangements for three new Executive Directors (Executives), two external appointments and one internal promotion, as well as agreeing arrangements for two departing Executives. These arrangements were disclosed at the time and are set out in this report on page 99. In all cases the standard provisions of our Policy applied, taking into account the individual circumstances of each case. The Committee considered the fixed elements of remuneration carefully and in particular, offered pension contributions for all three Executives below the newly established Policy maximum level.

Responding to the Corporate Governance Code

The Committee carefully considered the requirements relating to remuneration committees in the revised Code, which applies from 1 January 2019, and the Committee's Terms of Reference were reviewed and updated. During the year we discussed how we would ensure the Committee better understands remuneration arrangements and related policies applying across the wider workforce and that these are taken into consideration when setting and agreeing executive remuneration. To enable employee views to be taken into account in Committee discussions and decision-making, we have invited Joan Gillman to participate in discussions in her capacity as employee champion for the Board.

In addition, and in response to investor guidance, we disclose our CEO pay ratio below, a year ahead of the statutory requirement.

CEO pay ratio

The Company has used its gender pay gap data (Option B in the Directors' Reporting Regulations) to determine the employees whose remuneration packages sit at the lower, median and upper quartile positions across the UK workforce. We have calculated the annual remuneration relating to 2018 for the three identified employees on the same basis as the CEO's total remuneration for 2018 in the single figure table, to produce the ratios below:

Quartile position	Employee job profile	Total remuneration	CEO pay ratio
Lower	Smart Energy Expert	£33,718	72:1
Median	Servicing Engineer	£41,239	59:1
Upper	Technical Engineer	£55,107	44:1

In future years the ratio will be disclosed in a table in the remuneration report, building incrementally to show the ratios over a 10-year period.

Remuneration outcomes for the year

Overall, this has been another challenging year, with volatile commodity prices, strong competitive pressures and significant political and regulatory intervention in our markets. The Committee has been impressed by the resilience of the leadership team which has pulled together strongly to deliver against a wide range of targets. In respect of financial performance, the AIP adjusted operating profit (AOP) target, which had a 40% weighting, was not achieved. However, with strong cost efficiency delivery above the maximum performance level (20% weighting) and capital discipline, the cash flow target (40% weighting) was marginally exceeded. On balance the Committee felt that the formulaic outcome against the financial performance targets set was a fair reflection of performance and was satisfied that the resulting 60.5% of salary was an appropriate outcome.

The Committee has considered the individual performance of the Executives and a summary of the assessment for each individual is set out on pages 95 to 96. Total AIP awards were therefore in the range of 80% to 82% of salary, compared to a target and maximum of 100% and 200% respectively.

The Committee also assessed the vesting outcome for long-term incentive awards that were made in early 2016. The LTIP awards were dependent on adjusted earnings per share (EPS), economic profit (EP), safety performance, employee engagement and customer service delivery as assessed by net promoter scores. Based on performance against these metrics over the three years the LTIP will vest at a level of 18% of the award. The value of the shares initially granted under the 2016 award has fallen and as such represents an outcome of approximately 41% of salary.

A summary of the short and long-term outcomes is presented in the charts over the following two pages.

Application of Policy for 2019

During October and November 2018, a pension benefit consultation took place across the membership of the Group's UK defined benefit plans. Once the outcome of the consultation became clear, which would see future benefit accrual reduce in response to rising costs and competitive pressure, the Committee discussed and agreed with a proposal from the leadership team that pension contributions for existing Executives and other members of senior management would reduce to a maximum of 15% with effect from 1 June 2019. This represents reductions of between one half and one quarter in the pension benefit for affected Executives and represents appropriate alignment with the wider workforce.

In 2019, only Iain Conn will receive a salary increase, of 1.9%, being below the average level of salary increases across the UK workforce. The other Executives are either new in position or are leaving during the year.

The Committee has reviewed the bonus measures and weightings to apply for 2019, in line with the Group Annual Plan, and no change is proposed.

LTIP measures will also remain unchanged for 2019 awards, with targets set to align with realistic but stretching outcomes for the business. Further detail on incentive measures and targets can be found on page 103.[1]

Conclusion

The Committee continues to take a disciplined approach to executive remuneration that seeks to ensure Executives are appropriately rewarded while ensuring alignment with the shareholder experience and execution of strategy. The Committee believes that the decisions made over the year achieve this aim and align pay and performance effectively. The Committee is dedicated to an open and transparent dialogue with our investors and therefore I welcome views on any part of our remuneration arrangements.

Scott Wheway
Non-Executive Director

Membership and attendance

The Committee is chaired by Scott Wheway, an independent Non-Executive Director. 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.

The Chairman of the Board, the Group Chief Executive, the Group General Counsel & Company Secretary, the Group HR Director and the Deputy Group HR Director & Group Head of Reward are normally invited to attend each Committee meeting to provide advice and guidance, other than in respect of their own remuneration.

Role of the Remuneration Committee

The role of the Committee continues to be ensuring that the Executives, the Executive Committee and the Chairman of the Board are appropriately rewarded, through making recommendations regarding remuneration policy and framework. The revised Terms of Reference further extend the Committee's remit to include greater responsibility for understanding how pay and conditions align across the Group.

The Committee monitors and reviews the effectiveness of the Directors' Remuneration Policy and considers its impact and compatibility with remuneration policies across the wider workforce. To facilitate this extended remit, the Committee is provided with information and context on pay, benefits and incentive structures in place across the Group to support its decision-making.

Areas of focus

Executive Director recruitment and terminations announced in 2018

Revised investor remuneration guidelines

The revised Corporate Governance Code and remuneration committees

Pay, benefits, incentives and policy across the wider workforce

Business performance and remuneration outcomes

(1) Confirmation of the 2019 LTIP grant level will be provided in our announcement, which will be available on the London Stock Exchange shortly after the grant on 1st April 2019.

Remuneration Summary for 2018

Total remuneration received in 2018 (£000)(1)

Iain Conn
£2,416
2017: £1,678

Jeff Bell
£1,241
2017: £994

Mark Hanafin
£1,501
2017: £1,726

Mark Hodges(2)
£822
2017: £1,119

Richard Hookway
£206

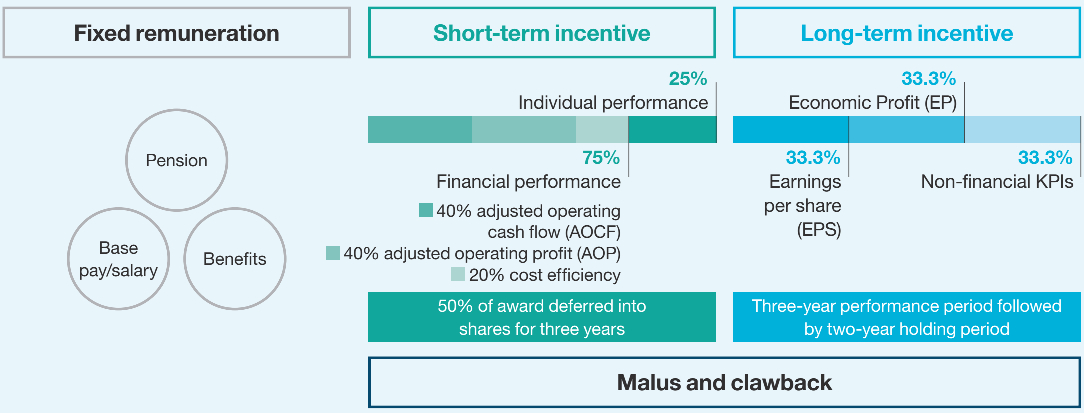
Chris O'Shea
£394

- Fixed remuneration
- Short-term incentive
- Long-term incentive

- Maximum total pay
- On-target total pay
- Minimum total pay

(1) Prepared on the same basis as the single figure for total remuneration table set out on page 94.
(2) As Mark Hodges is leaving the Company on 28 February 2019 his AIP and LTIP awards have been forfeited in full.

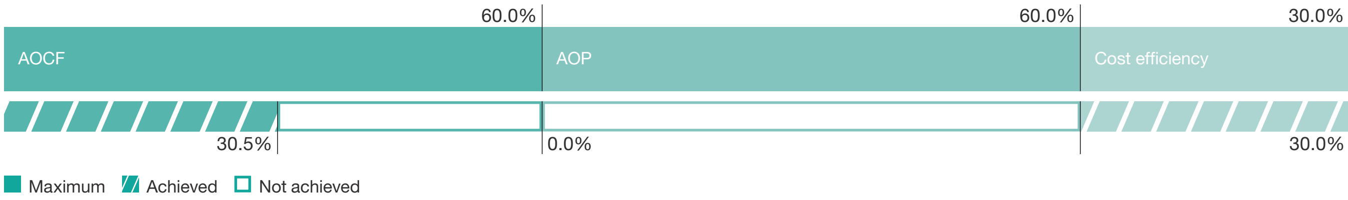
Components of remuneration package earned/ vested in 2018



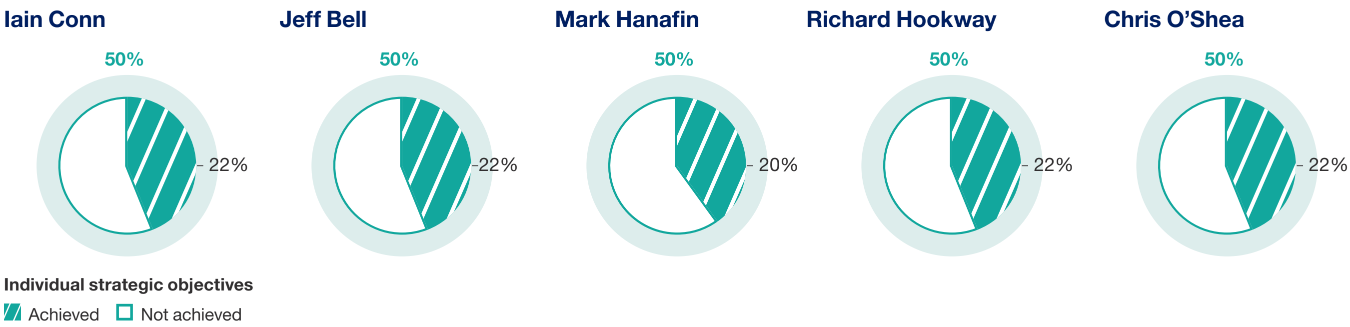
Read more about Our Remuneration Policy
Pages 104 to 109

Short-term incentive outcome (Annual Incentive Plan)

Financial performance



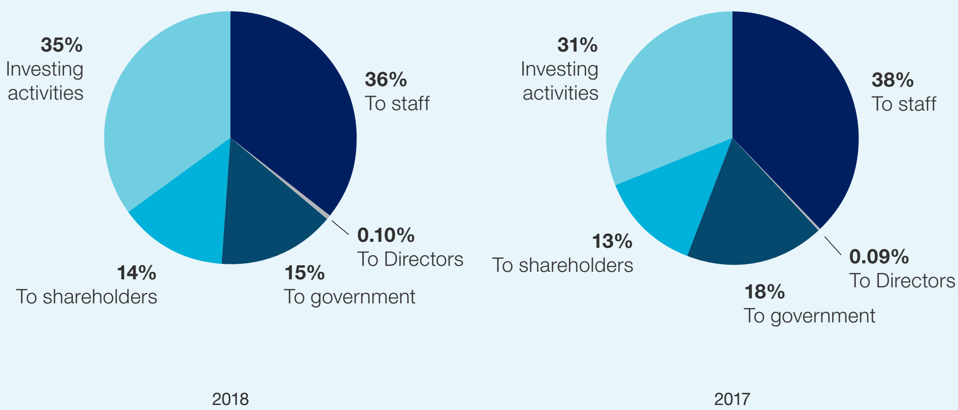
Individual performance



Long-term incentive outcome (Long Term Incentive Plan)

2018 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, the Directors' aggregate total remuneration for the year equates to 0.10% (2017: 0.09%) of the Group's operating cash flow.



Directors' Annual Remuneration Report

Directors' remuneration in 2018

This report sets out information on the remuneration of the Directors for the financial year ended 31 December 2018.

Single figure for total remuneration (audited)

	Salary/fees		Bonus (cash)		Bonus (deferred)		Benefits[1]		LTIPs		Pension[4][5]		Total	
£000	**2018**	2017	**2018**	2017	**2018**	2017	**2018**	2017	**2018[2]**	2017[3]	**2018**	2017	**2018**	2017[3]
Executives														
Iain Conn	**940**	936	**388**	–	**388**	–	**31**	30	**387**	431	**282**	281	**2,416**	1,678
Jeff Bell[6]	**479**	569	**198**	–	**198**	–	**35**	27	**230**	252	**101**	146	**1,241**	994
Mark Hanafin[6]	**584**	634	**235**	–	**235**	–	**23**	25	**261**	805	**163**	262	**1,501**	1,726
Mark Hodges[7]	**638**	634	**–**	–	**–**	–	**25**	34	**–**	292	**159**	159	**822**	1,119
Richard Hookway[8]	**100**	–	**41**	–	**41**	–	**4**	–	**–**	–	**20**	–	**206**	–
Chris O'Shea[9]	**191**	–	**79**	–	**79**	–	**7**	–	**–**	–	**38**	–	**394**	–
Total													**6,580**	5,517

(1) Taxable benefits include car allowance, health and medical benefits and financial planning advice. Non-taxable benefits include matching shares received under the Share Incentive Plan (SIP). Both taxable and non-taxable benefits are included in the table.
(2) LTIPs include the estimated value of the LTIP awards granted in 2016 and due to vest in April 2019, relating to the three-year performance period ending in 2018. Details of the performance outcomes are set out on pages 97 to 98. The estimated value of dividend equivalent shares has been included and the share price used to value the awards is 143.39 pence (the average share price from 1 October to 31 December 2018).
(3) The values of the LTIP awards vesting in April, May and August 2018 have been recalculated based on the share price on the dates of vest which were 139.57, 153.63 and 146.70 pence respectively. The previous disclosure in the 2017 single figure table used an estimated share price. Iain Conn, Jeff Bell, Mark Hanafin and Mark Hodges' total remuneration for 2017 has therefore been restated to include the amended value of these awards.
(4) Notional contributions to the Centrica Unapproved Pension Scheme defined contribution section (CUPS DC) for Jeff Bell, Mark Hanafin, Richard Hookway and Chris O'Shea have been included in this table as if CUPS DC was a cash balance scheme. This includes a deduction in respect of an allowance for CPI inflation on the opening balances of 3.0% in 2018 (0.9% in 2017). The 2017 pension benefit for Jeff Bell has been restated due to a minor reporting error in the 2017 disclosure.
(5) Iain Conn and Mark Hodges were entitled to receive a salary supplement of 30% and 25% of base salary respectively in 2018.
(6) Jeff Bell stepped down from the Board on 31 October 2018 and Mark Hanafin stepped down from the Board on 30 November 2018. The remuneration in this table includes their prorated salary, bonus, benefits and pension benefits earned up to the date they stepped down. The remuneration for the remainder of the year, whilst they were working their remaining notice periods, has been disclosed in the payments for loss of office disclosure below. The full estimated value of the LTIP awards granted in 2016 and due to vest in April 2019 has been included in the single figure table above.
(7) As Mark Hodges had tended his resignation and agreed a leaving date of 28 February 2019, his AIP award relating to the 2018 year, and all unvested LTIP awards as at his date of leaving, were forfeited.
(8) Richard Hookway joined Centrica on 1 November and was appointed to the Board on 1 December 2018. The remuneration in this table relates to the period from 1 November to 31 December 2018.
(9) Chris O'Shea joined Centrica on 10 September and was appointed to the Board on 1 November 2018. The remuneration in this table relates to the period from 10 September to 31 December 2018.

Single figure for total remuneration (audited)

	Salary/fees		Bonus (cash)		Bonus (defered)		Benefits		LTIPs		Pension		Total	
£000	**2018**	2017	**2018**	2017	**2018**	2017	**2018**	2017	**2018**	2017	**2018**	2017	**2018**	2017
Non-Executives														
Rick Haythornthwaite	**495**	495	**–**	–	**–**	–	**–**	–	**–**	–	**–**	–	**495**	495
Charles Berry[1]	**12**	–	**–**	–	**–**	–	**–**	–	**–**	–	**–**	–	**12**	–
Margherita Della Valle	**98**	98	**–**	–	**–**	–	**–**	–	**–**	–	**–**	–	**98**	98
Joan Gillman	**73**	73	**–**	–	**–**	–	**–**	–	**–**	–	**–**	–	**73**	73
Stephen Hester	**93**	93	**–**	–	**–**	–	**–**	–	**–**	–	**–**	–	**93**	93
Lesley Knox[2]	**–**	80	**–**	–	**–**	–	**–**	–	**–**	–	**–**	–	**–**	80
Carlos Pascual	**73**	73	**–**	–	**–**	–	**–**	–	**–**	–	**–**	–	**73**	73
Steve Pusey	**93**	93	**–**	–	**–**	–	**–**	–	**–**	–	**–**	–	**93**	93
Scott Wheway	**93**	85	**–**	–	**–**	–	**–**	–	**–**	–	**–**	–	**93**	85
Total													**1,030**	1,090

(1) Charles Berry was appointed as a Non-Executive Director on 31 October 2018.
(2) Lesley Knox resigned as a Non-Executive Director on 31 December 2017.

Payments for loss of office (audited)

Jeff Bell stepped down from the Board on 31 October 2018. He continued to work through his notice period and to receive his contractual salary, benefits and entitlement to incentives. For the period from 1 November to 31 December 2018, Jeff was paid £95,833 in base salary, £6,971 in benefits, £17,000 in pension benefits and £79,096 under the AIP.

Mark Hanafin stepped down from the Board on 30 November 2018. He continued to work through his notice period and to receive his contractual salary, benefits and entitlement to incentives. For the period from 1 December to 31 December 2018, Mark was paid £53,125 in base salary, £2,044 in benefits, £16,000 in pension benefits and £44,211 under the AIP.

The full leaving arrangements for Jeff Bell and Mark Hanafin are set out on page 99.

There were no other payments for loss of office in 2018.