

Registration number: 02877398

Centrica Energy Limited

Annual Report and Financial Statements

for the Year Ended 31 December 2016

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Centrica Energy Limited

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Centrica Energy Limited

Strategic Report for the Year Ended 31 December 2016

The Directors present their Strategic Report of Centrica Energy Limited ("the Company") for the year ended 31 December 2016.

Review of the business

The Company's Financial Statements have been prepared in accordance with Financial Reporting Standard 101: Reduced Disclosures Framework ('FRS 101').

The principal activity of the Company is the wholesale trading of physical energy products and the trading of energy related derivatives. The main products traded in the year were natural gas, electricity, emissions certificates, oil and coal in the UK and Europe.

The financial position of the Company is set out on page 10. The net assets for the financial year ended 31 December 2016 is £106.6m (2015: £432.8m). The financial performance of the Company is set out in the Directors' Report on page 3. Please refer to note 2 for detail of a prior year balance sheet restatement. This had no impact to net assets or profits for the financial year. Both the level of business during the year and the financial position of the Company at the year-end were in line with management's expectations.

These accounts are included in the consolidated accounts of Centrica plc, the ultimate parent and controlling company.

Principal risks and uncertainties

The principal risk and uncertainty affecting the business and execution of the Company strategy is continuing to operate efficiently and effectively within the regulatory requirements placed upon the business.

The Company's operations expose it to a number of financial risks. Given the size and nature of the Company these risks are managed by the risk and finance departments in accordance with the Group guidelines set by Centrica plc. The principal financial risk facing the Company is credit risk, which arises on intercompany and external balances and bank deposits. Bank deposits are only held with financial institutions, which have been approved by Centrica plc.

Exit from the European Union

The UK referendum vote in June to leave the European Union has added to the uncertainties faced by the business. However, we believe that the direct impact on the business of these events is limited in the short-term. Many details of the implementation process remain unclear. Extricating from the European Union treaties is a task of immense complexity but with that being said, the business is well-positioned to manage any market impacts. There are also potential tax consequences of the withdrawal agreement which we will continue to reassess (at each reporting date) to ensure our tax provisions reflect the most likely outcome following the withdrawal.

Key performance indicators (KPIs)

The Directors of the Group use a number of KPI's to monitor progress against the Group's strategy. The financial and non-financial performance indicators, which include the Company, are discussed on pages 18 and 19 of the Annual Report and Accounts 2016 of the Group which does not form part of this report.

In addition to the Group KPIs noted above, the Directors of the Company believe that the trader margin which drives the operating profit of the business is the critical KPI specific to the Company. The operating profit is noted within the income statement reported on page 8. The operating profit forms part of the monthly reporting pack reviewed by senior management to gain an understanding of the performance of the business. Additional KPIs include the Directors' review of counterparty credit risk, VaR and liquidity risk, which is analysed in detail within note 20. The extent of the risks relative to the approved limits are also reviewed monthly by senior management to gain an understanding of the performance of the business.

Centrica Energy Limited

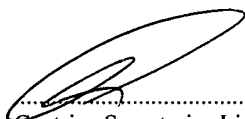
Strategic Report for the Year Ended 31 December 2016 (continued)

Future developments

The Directors expect the Company to continue to trade physical energy products and energy related derivatives for the foreseeable future.

The Centrica group is currently implementing the results of a 2015 strategic review. This implementation includes a review of how the Group's businesses are structured and may result in future changes to underlying subsidiary business operations including those of Centrica Energy Limited.

Approved by the Board on 5 May 2017 and signed on its behalf by:



Centrica Secretaries Limited
Company Secretary

Company registered in England and Wales, No. 02877398

Registered office:
Millstream
Maidenhead Road
Windsor
Berkshire
SL4 5GD

Centrica Energy Limited

Directors' Report for the Year Ended 31 December 2016

The Directors present their report and the Financial Statements for the year ended 31 December 2016.

Directors of the Company

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

Mr V M Hanafin

Mr A D Le Poidevin (resigned 1 October 2016)

Mr C Mangerah

Mr J Westby (appointed 1 October 2016)

Results and dividends

The results of the Company are set out on page 8. The profit for the financial year ended 31 December 2016 is £34.3m (2015: £53.1m). On 30 November 2016, the Company paid an interim dividend of £360m to its immediate parent undertaking GB Gas Holdings Limited (2015: £Nil). The Directors do not recommend the payment of a final dividend in respect of the financial year 31 December 2016 (2015: £Nil).

Directors' and officers' liabilities

In accordance with the Articles of Association, the Company has granted a deed of indemnity, to the extent permitted by law, to Directors and officers of the Company. Qualifying third party indemnity provisions (as defined by section 234 of the Companies Act 2006) were in force during the year ended 31 December 2016 and remain in force.

The Company also maintains Directors' and officers' liability insurance for its Directors and officers which has been purchased by the ultimate parent company, Centrica plc, and was in place throughout the year under review. The insurance does not provide cover in the event that the Director or officer is proved to have acted fraudulently.

Future developments

Future developments are discussed in the Strategic Report on pages 1-2.

Going concern

The Financial Statements have been prepared on a going concern basis.

Centrica Energy Limited

Directors' Report for the Year Ended 31 December 2016 (continued)

Statement of Directors' Responsibilities

The Directors are responsible for preparing the Strategic Report, Directors' Report and the Financial Statements in accordance with applicable UK law and regulations.

Company law requires the Directors to prepare financial statements for each financial year. Under that law the Directors have elected to prepare the financial statements in accordance with United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice), including FRS 101 'Reduced Disclosure Framework' ('FRS 101'). 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 Company and of the profit or loss of the Company for that period. In preparing these financial statements, the Directors are required to:

- select suitable accounting policies and apply them consistently;
- make judgements and accounting estimates that are reasonable and prudent;
- state whether FRS 101 has been followed, subject to any material departures disclosed and explained in the financial statements; 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 enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Disclosure of information to the 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 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.

Reappointment of auditors

Following a rigorous selection by the Audit Committee of Centrica plc, Deloitte LLP was selected as the Group's external auditor for the financial year commencing from 1 January 2017 (subject to ratification of their appointment at the Centrica plc 2017 AGM). Consequently, PricewaterhouseCoopers LLP will remain auditors of Centrica Energy Limited until the formal resignation process has been completed later in 2017, after which Deloitte LLP will be appointed as auditors of Centrica Energy Limited.

Pursuant to Section 487 of the Companies Act 2006, the auditors will be deemed to be reappointed and PricewaterhouseCoopers LLP will therefore continue in office, until the formal resignation process has been completed.

Centrica Energy Limited

Directors' Report for the Year Ended 31 December 2016 (continued)

Statement of Directors' Responsibilities (continued)

Approved by the Board on 5 May 2017 and signed on its behalf by:



Centrica Secretaries Limited
Company Secretary

Company registered in England and Wales, No. 02877398

Registered office:
Millstream
Maidenhead Road
Windsor
Berkshire
SL4 5GD

Centrica Energy Limited

Independent auditors' report to the members of Centrica Energy Limited

Report on the financial statements

Our opinion

In our opinion, Centrica Energy Limited's financial statements (the "financial statements"):

- give a true and fair view of the state of the Company's affairs as at 31 December 2016 and of its profit for the year then ended;
- 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.

What we have audited

The financial statements, included within the Annual Report and Financial Statements (the "Annual Report"), comprise:

- the Statement of Financial Position as at 31 December 2016;
- the Income Statement and Statement of Comprehensive Income for the year then ended;
- the Statement of Changes in Equity for the year then ended; and
- the notes to the financial statements, which include a summary of significant accounting policies and other explanatory information.

The financial reporting framework that has been applied in the preparation of the financial statements is United Kingdom Accounting Standards, comprising FRS 101 "Reduced Disclosure Framework", and applicable law (United Kingdom Generally Accepted Accounting Practice).

In applying the financial reporting framework, the Directors have made a number of subjective judgements, for example in respect of significant accounting estimates. In making such estimates, they have made assumptions and considered future events.

Opinions on other matters prescribed by the Companies Act 2006

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the Strategic Report and the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the Strategic Report and the Directors' Report have been prepared in accordance with applicable legal requirements.

In addition, in light of the knowledge and understanding of the Company and its environment obtained in the course of the audit, we are required to report if we have identified any material misstatements in the Strategic Report and the Directors' Report. We have nothing to report in this respect.

Other matters on which we are required to report by exception

Adequacy of accounting records and information and explanations received

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- we have not received all the information and explanations we require for our audit; or
- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements are not in agreement with the accounting records and returns.

We have no exceptions to report arising from this responsibility.

Centrica Energy Limited

Independent auditors' report to the members of Centrica Energy Limited (continued)

Directors' remuneration

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. We have no exceptions to report arising from this responsibility.

Responsibilities for the financial statements and the audit

Our responsibilities and those of the directors

As explained more fully in the Statement of Directors' Responsibilities set out on pages 4 and 5, the Directors are responsible for the preparation of the 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 financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland) ("ISAs (UK & 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.

What an audit of financial statements involves

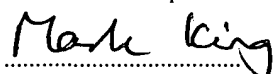
We conducted our audit in accordance with ISAs (UK & Ireland). An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of:

- whether the accounting policies are appropriate to the 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.

We primarily focus our work in these areas by assessing the Directors' judgements against available evidence, forming our own judgements, and evaluating the disclosures in the financial statements.

We test and examine information, using sampling and other auditing techniques, to the extent we consider necessary to provide a reasonable basis for us to draw conclusions. We obtain audit evidence through testing the effectiveness of controls, substantive procedures or a combination of both.

In addition, we read all the financial and non-financial information in the Annual Report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report. With respect to the Strategic Report and Directors' Report, we consider whether those reports include the disclosures required by applicable legal requirements.



Mark King (Senior Statutory Auditor)
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
London
5 May 2017

Centrica Energy Limited

Income Statement for the Year Ended 31 December 2016

	Note	2016 £ 000	2015 £ 000
Net trading income	4	64,025	103,174
Operating costs	5	<u>(33,862)</u>	<u>(37,095)</u>
Operating profit		30,163	66,079
Income from shares in group undertakings	7	-	4,000
Finance income	7	16,545	17,409
Finance cost	7	<u>(3,795)</u>	<u>(21,798)</u>
Profit before income tax		42,913	65,690
Income tax expense	10	<u>(8,575)</u>	<u>(12,620)</u>
Profit for the financial year		<u>34,338</u>	<u>53,070</u>

The notes on pages 12 to 40 form an integral part of these financial statements.

Centrica Energy Limited

Statement of Comprehensive Income for the Year Ended 31 December 2016

	Note	2016 £ 000	2015 £ 000
Profit for the financial year		34,338	53,070
Items that will not be reclassified subsequently to profit or loss	17		
Net actuarial gains/losses on defined benefit pension schemes		(555)	(189)
Items that may be reclassified subsequently to profit or loss	10		
Income tax on items that will not be reclassified to profit or loss		<u>124</u>	<u>2</u>
Total comprehensive income for the year		<u>33,907</u>	<u>52,883</u>

The notes on pages 12 to 40 form an integral part of these financial statements.

Centrica Energy Limited

Statement of Financial Position as at 31 December 2016

	Note	2016 £ 000	Restated 2015* £ 000
Non-current assets			
Investments	11	850	850
Defined benefit pension assets	17	-	269
Derivative financial instruments	15	5,914	8,652
Deferred tax assets	10	1,361	874
		<u>8,125</u>	<u>10,645</u>
Current assets			
Trade and other receivables	13	762,158	942,481
Inventories	14	5,608	-
Derivative financial instruments	15	1,291,322	1,696,565
Cash and cash equivalents	12	3,110	6,637
		<u>2,062,198</u>	<u>2,645,683</u>
Total assets		2,070,323	2,656,328
Current liabilities			
Trade and other payables	16	(597,074)	(610,354)
Derivative financial instruments	15	(1,350,499)	(1,595,846)
Current tax liabilities	10	(8,987)	(12,498)
		<u>(1,956,560)</u>	<u>(2,218,698)</u>
Non-current liabilities			
Deferred tax liabilities	10	-	(48)
Trade and other payables	16	(7,057)	(4,815)
Defined benefit pension liabilities	17	(66)	-
		<u>(7,123)</u>	<u>(4,863)</u>
Total liabilities		(1,963,683)	(2,223,561)
Net assets		106,640	432,767
Equity			
Called up share capital	18	50	50
Other reserves		892	926
Retained earnings		105,698	431,791
Total equity		106,640	432,767

*See note 2.

The financial statements on pages 8 to 40 were approved and authorised for issue by the Board of Directors on 5 May 2017 and signed on its behalf by:

Mr C Mangerah, Director Company number 02877398

The notes on pages 12 to 40 form an integral part of these financial statements.

Centrica Energy Limited

Statement of Changes in Equity for the Year Ended 31 December 2016

	Share capital £ 000	Other reserves £ 000	Retained earnings £ 000	Total £ 000
At 1 January 2016	50	926	431,791	432,767
Profit for the year	-	-	34,338	34,338
Other comprehensive expense	-	-	(431)	(431)
Total comprehensive income	50	926	465,698	466,674
Dividends	-	-	(360,000)	(360,000)
Share incentive plan	-	(34)	-	(34)
At 31 December 2016	50	892	105,698	106,640

	Share capital £ 000	Other reserves £ 000	Retained earnings £ 000	Total £ 000
At 1 January 2015	50	919	378,908	379,877
Profit for the year	-	-	53,070	53,070
Other comprehensive expense	-	-	(187)	(187)
Total comprehensive income	50	919	431,791	432,760
Share incentive plan	-	7	-	7
At 31 December 2015	50	926	431,791	432,767

The notes on pages 12 to 40 form an integral part of these financial statements.

Centrica Energy Limited

Notes to the Financial Statements for the Year Ended 31 December 2016

1 General information

Centrica Energy Limited (the 'Company') is a company limited by share capital incorporated and domiciled in the United Kingdom.

The address of its registered office and principle place of business is:

Millstream
Maidenhead Road
Windsor
Berkshire
SL4 5GD
England and Wales

These Financial Statements were authorised for issue by the Board on 5 May 2017.

2 Accounting policies

Basis of preparation

The Company meets the definition of a qualifying entity under FRS 100 (Financial Reporting Standard 100) issued by the Financial Reporting Council.

The Company is exempt by virtue of the Companies Act 2006 from the requirement to prepare group financial statements as it's a wholly-owned subsidiary of Centrica plc. These financial statements present information about the Company as an individual undertaking and not about its group, and have been prepared on a going concern basis, as described in the Directors' Report.

These financial statements have been prepared in accordance with Financial Reporting Standard 101 Reduced Disclosure Framework.

Prior year restatement

The 2015 comparatives have been restated to net down intercompany balances with British Gas Trading Limited as they meet the offsetting requirements under IAS 32. Trade and other receivables and Trade and other payables have both reduced by £84,349,000 as a result of this restatement. There is no impact to net assets or profit for the financial year. The impact to balances as at 1 January 2015 was to reduce Trade and other receivables and Trade and other payables by £34,560,000.

Going concern

The financial statements have been prepared on a going concern basis.

Summary of disclosure exemptions

The Company financial statements have been prepared in accordance with Financial Reporting Standard 101 Reduced Disclosure Framework ("FRS 101"). In preparing these financial statements the Company applies the recognition, measurement and disclosure requirements of International Financial Reporting Standards as adopted by the EU ("Adopted IFRSs"), but makes amendments where necessary in order to comply with the Companies Act 2006 and has set out below where advantages of the FRS 101 disclosure exemptions has been taken.

Centrica Energy Limited

Notes to the Financial Statements for the Year Ended 31 December 2016 (continued)

2 Accounting policies (continued)

In these financial statements, the Company has applied the exemptions available under FRS 101 in respect of the following disclosures:

- A Cash Flow statement and related notes;
- Comparative period reconciliations for share capital;
- Disclosures in respect of related party transactions with wholly-owned subsidiaries;
- Disclosures in respect of the compensation of Key Management Personnel;
- The effects of new but not yet effective IFRSs.

These financial statements are presented in pound sterling (with all values rounded to the nearest thousand except where otherwise indicated), which is also the functional currency of the Company. Operations and transactions conducted in currencies other than the functional currency are translated in accordance with the foreign currencies accounting policy set out below. The financial statements are prepared on the historical cost basis except for derivative financial instruments, financial instruments designated at fair value through profit and loss on initial recognition and the Company's share of assets of the Group's defined benefit schemes that have been recorded at fair value.

Changes in accounting policy

None of the standards, interpretations and amendments effective for the first time from 1 January 2016 have had a material effect on the financial statements.

Summary of significant accounting policies and key accounting estimates

The principal accounting policies applied in the preparation of these financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

Net trading income

Net trading income is the net of trading income and commodity costs. Trading income comprises the fair value of the consideration received or receivable from trading activities in the ordinary course of the business, and is recognised to the extent that it is probable that the economic benefits will flow to the Company and the trading income can be measured reliably. Trading income comprises both realised (settled) and unrealised (fair value changes) net gains and losses from trading in physical and financial energy contracts. Revenue is shown net of sales/value added tax, returns, rebates and discounts.

Commodity costs comprise the fair value of the consideration paid or payable from trading activities in the ordinary course of the business, and is recognised to the extent that it is probable that economic benefits will flow away from the Company and the cost can be measured reliably. Commodity costs comprise both realised (settled) and unrealised (fair value changes) net losses and gains from trading in physical and financial energy contracts.

Employee share schemes

The Centrica plc group, to which the Company belongs, has a number of employee share schemes, detailed in the Remuneration Report on pages 83-99 and in note S2 of the Group financial statements, 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 in the income statement together with a corresponding increase in equity over the vesting period, based on the Centrica plc 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 detailed in note S2 of the Group financial statements.

Centrica Energy Limited

Notes to the Financial Statements for the Year Ended 31 December 2016 (continued)

2 Accounting policies (continued)

Dividends

Dividend distribution to the Company's shareholders is recognised as a liability in the Company's financial statements in the period in which the dividends are approved by the Company's shareholders.

Income from shares in group undertakings

Income from shares in group undertakings comprises the consideration received or receivable from dividend distributions made by Centrica Energy (Trading) Limited to Centrica Energy Limited. It is recognised to the extent that it is probable that the economic benefits will flow to the Company and the share income can be measured reliably.

Foreign currencies

Transactions in foreign currencies are initially recorded at the functional currency rate prevailing at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated into pounds sterling at closing rates of exchange. Income and expenses in foreign currencies are translated into pounds sterling at rates of exchange prevailing at the time of the transactions. Exchange differences on monetary assets and liabilities are taken to the income statement. The pounds sterling translated equivalent of delivered energy financial derivative contracts and movements in the valuation of energy financial derivative contracts denominated in foreign currencies are included within net trading income.

Taxation

The tax expense for the period comprises current and deferred tax. Tax is recognised in profit or loss, except that a change attributable to an item of income or expense recognised as other comprehensive income is also recognised directly in other comprehensive income.

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. Tax is recognised in profit or loss, except that a change attributable to an item of income or expense recognised as other comprehensive income is also recognised directly in other comprehensive income.

Centrica Energy Limited

Notes to the Financial Statements for the Year Ended 31 December 2016 (continued)

2 Accounting policies (continued)

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 impairment 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 Company's assets and liabilities and their tax base.

Deferred tax liabilities are offset against deferred tax assets when the Company has a legally enforceable right to offset current tax assets and liabilities and the deferred tax assets and liabilities relate to taxes levied by the same tax authority. 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, joint ventures 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. The carrying amount of deferred tax assets are reviewed at each reporting date and a valuation allowance is set up against deferred tax assets so that the net carrying amount equals the highest amount that is more likely than not to be recovered based on current or future taxable profit.

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.

Investments in subsidiaries

The Company does not deem its investments in subsidiaries as well as related receivables to be impaired and supports this judgment through its impairment review process.

Inventories

Inventories of gas and oil are valued on a weighted average basis, at the lower of cost and estimated net realisable value.

Defined benefit pension obligation

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 Company's best estimate of the variables that will determine the ultimate cost of providing post-employment benefits.

Financial assets and liabilities

Financial assets and financial liabilities are recognised in the Company's statement of financial position when the Company becomes a party to the contractual provisions of the instrument. Financial assets are de-recognised when the Company 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.

Centrica Energy Limited

Notes to the Financial Statements for the Year Ended 31 December 2016 (continued)

2 Accounting policies (continued)

Trade and other receivables

Trade receivables are amounts due from customers for merchandise sold or services performed in the ordinary course of business. If collection is expected in one year or less (or in the normal operating cycle of the business if longer), they are classified as current assets. If not, they are presented as non-current assets.

Trade receivables are recognised initially at the transaction price. They are subsequently measured at amortised cost using the effective interest method, less provision for impairment. A provision for the impairment of trade receivables is established when there is objective evidence that the Company will not be able to collect all amounts due according to the original terms of the receivables.

Prepayments and accrued income comprise payments made in advance relating to the following year, and income relating to the current year, that will not be invoiced until after the balance sheet date.

Trade and other payables

Trade payables are obligations to pay amounts to suppliers in the ordinary course of business. Accounts payable are classified as current liabilities if payment is due within one year or less (or in the normal operating cycle of the business if longer). If not, they are presented as non-current liabilities. Trade payables are recognised at the original invoice amount.

Share capital

Ordinary shares are classified as equity. Equity instruments are measured at the fair value of the cash or other resources received or receivable. 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 re-acquired (treasury or own shares) are deducted from equity. No gain or loss is recognised in the Company's income statement on the purchase, sale, issue or cancellation of the Company's own equity instruments.

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.

Centrica Energy Limited

Notes to the Financial Statements for the Year Ended 31 December 2016 (continued)

2 Accounting policies (continued)

Derivative financial instruments

The Company routinely enters into sale and purchase transactions for physical delivery of gas, power and oil. 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 Company's statement of financial position at fair value. Gains and losses arising from changes in fair value on derivatives are taken directly to the income statement for the year.

The Company uses a range of derivatives for both trading and to hedge exposures to financial risks, such as 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. Further detail on the Group's risk management policies is included within the Annual Report and Accounts 2016 of the ultimate controlling party being Centrica plc, in the Strategic Report – Principal Risks and Uncertainties on pages 56 to 64 and in note S3.

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 Company 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 (not recognised) and amortised to the income statement based on volumes purchased or delivered over the contractual period until such time observable market data becomes available. When observable market data becomes available, any remaining deferred day-one gains or losses are recognised within the income statement. Gains and losses arising on derivatives entered into for speculative energy trading purposes are presented on a net basis within revenue.

Derivatives are classified as a current asset or liability. The full fair value of a hedging derivative is classified as a non-current asset or liability if the remaining maturity of the hedged item is more than 12 months and, as a current asset or liability, if the maturity of the hedged item is less than 12 months.

Embedded derivatives: derivatives embedded in other financial instruments or other host contracts are treated as separate derivatives when their risks and characteristics are not closely related to those of the host contracts and the host contracts are not carried at fair value, with gains or losses reported in the income statement. The closely-related nature of embedded derivatives is reassessed when there is a change in the terms of the contract which significantly modifies the future cash flows under the contract. Where a contract contains one or more embedded derivatives, and providing that the embedded derivative significantly modifies the cash flows under the contract, the option to fair value the entire contract may be taken and the contract will be recognised at fair value with changes in fair value recognised in the income statement.

Centrica Energy Limited

Notes to the Financial Statements for the Year Ended 31 December 2016 (continued)

3 Critical accounting judgements and key sources of estimation uncertainty

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. Quoted market prices considered for valuation purposes are the bid price for assets held and/or liabilities to be issued, or the offer price for assets to be acquired and/or liabilities held, although the mid-market price or another pricing convention may be used as a practical expedient (where typically used by other market participants). The judgements and the assumptions underpinning these judgements are considered to be appropriate.

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 Company's best estimate of the variables that will determine the ultimate cost of providing post-employment benefits.

4 Net trading income

The analysis of the Company's trading income for the year from continuing operations is as follows:

	2016	2015
	£ 000	£ 000
Trading income	44,740,917	52,875,146
Commodities costs	(44,626,447)	(52,738,329)
Transportation, Distribution & Metering costs	<u>(50,445)</u>	<u>(33,643)</u>
Net trading income	<u>64,025</u>	<u>103,174</u>

The Company carries out most of its trading within UK markets and generates the majority of its income in the UK. The other key markets in which revenue is generated are the Netherlands and Germany.

Centrica Energy Limited

Notes to the Financial Statements for the Year Ended 31 December 2016 (continued)

5 Analysis of operating costs by nature

The analysis of the Company's operating costs for the year is as follows:

	2016	2015
	£ 000	£ 000
Employee costs	16,323	13,854
Foreign exchange losses	2	24
Impairment of trade receivables	-	6
Other operating costs	17,537	23,211
Total costs	<u>33,862</u>	<u>37,095</u>

6 Employees' costs

The aggregate employee costs (including directors' remuneration) were as follows:

	2016	2015
	£ 000	£ 000
Wages and salaries	14,112	11,781
Social security costs	1,910	1,589
Pension and other post-employment benefit costs	207	262
Share-based payment expenses	4	7
Other employee expense	90	215
	<u>16,323</u>	<u>13,854</u>

In respect of the Directors' remuneration, refer to note 8.

The monthly average number of personnel directly employed by the Company, not including secondees from fellow Group companies, during the year was 21 (2015: 20). All personnel are based in the United Kingdom.

Centrica Energy Limited

Notes to the Financial Statements for the Year Ended 31 December 2016 (continued)

7 Net finance income/cost

Finance income

	2016 £ 000	2015 £ 000
Interest income from amounts owed by group undertakings	16,512	17,406
Interest income on bank and other short-term deposits	25	3
Income from shares in group undertakings	-	4,000
Other finance income	8	-
Total finance income	16,545	21,409

Income from shares in group undertakings comprises the consideration received or receivable from dividend distributions made by Centrica Energy (Trading) Limited to Centrica Energy Limited. It is recognised to the extent that it is probable that the economic benefits will flow to the Company and the share income can be measured reliably.

Finance interest

	2016 £ 000	2015 £ 000
Interest on amounts owed to group undertakings	(3,651)	(21,651)
Interest on bank overdrafts and borrowings	(144)	(162)
Other finance costs	-	15
Total finance cost	(3,795)	(21,798)
Net finance income/(costs)	12,750	(389)

Interest payable to/receivable from third parties relates mainly to interest on cash collateral received and paid by the Company under trading arrangements.

8 Directors' remuneration

The aggregate emoluments paid to Directors in respect of their qualifying services were £475,000 (2015: £592,000).

The aggregate value of company contributions paid to a pension scheme in respect of Directors' qualifying services were £25,000 (2015: £20,000). There were 2 Directors (2015: 2) to whom retirement benefits are accruing under defined benefit pension schemes. There were 2 Directors (2015: 1) to whom retirement benefits are accruing under money purchase pension scheme.

There were 4 Directors (2015: 4) who received shares in the ultimate parent company in respect of their qualifying services under a long-term incentive scheme. There was no Director (2015: 1) who exercised share options relating to the ultimate parent company.

Centrica Energy Limited

Notes to the Financial Statements for the Year Ended 31 December 2016 (continued)

8 Directors' remuneration (continued)

In respect of the highest paid Director:

	2016 £ 000	2015 £ 000
Remuneration	341	349
Company contributions to money purchase pension schemes	12	1
Total compensation	<u>353</u>	<u>350</u>

In the current year the highest paid Director received shares in respect of qualifying services under a long-term incentive scheme.

9 Auditors' remuneration

Auditors' remuneration totalling £213,000 (2015: £242,000) relates to fees for the audit of the FRS 101 statutory financial statements of the Company and includes fees in relation to the audit of the IFRS Group consolidation schedules, for the purpose of the Centrica plc group audit, which also contribute to the audit of the Company.

The Company has taken advantage of the exemption not to disclose amounts paid for non-audit services as these are disclosed in the Group financial accounts of its ultimate parent, Centrica plc.

10 Income tax

Tax charged/(credited) in the income statement

	2016 £ 000	2015 £ 000
Current taxation		
UK corporation tax at 20.00% (2015: 20.25%)	8,987	13,521
Deferred taxation		
Arising from origination and reversal of temporary differences - UK	<u>(412)</u>	<u>(901)</u>
Tax expense in the income statement	<u>8,575</u>	<u>12,620</u>

Centrica Energy Limited

Notes to the Financial Statements for the Year Ended 31 December 2016 (continued)

10 Income tax (continued)

The differences between the taxes shown above and the amounts calculated by applying the standard rate of UK corporation tax rate to the profit before tax are reconciled below:

	2016 £ 000	2015 £ 000
Profit before tax	42,913	65,690
Tax expense at standard UK rate 20.00% (2015: 20.25%)	8,583	13,302
<i>Effects of:</i>		
Adjustments in respect of prior years	-	71
Share options	-	3
Effects of group relief / other reliefs	-	(2)
Transfer pricing adjustments	-	2
Deferred tax expense (credit) from unrecognised tax loss or credit	-	(2)
Income not taxable	-	(810)
Tax rate changes	(8)	56
Total income tax expense	8,575	12,620

The main rate of corporation tax for the year to 31 December 2016 was 20%. The corporation tax rate will reduce to 19% with effect from 1 April 2017 and to 17% with effect from 1 April 2020 following the enactment of Finance (No 2) Act 2015 and Finance Act 2016 respectively. These enacted rates have been reflected in these financial statements when providing for deferred tax.

Deferred tax

The movements in respect of the deferred income tax assets and liabilities that occurred during the financial year are as follows:

	Fixed Assets £ 000	Temporary differences trading £ 000	Pension £ 000	Total £ 000
Current period opening balance	1	872	(48)	825
Charged / (credited) to Income Statement	-	475	(63)	412
Charged / (credited) to Other Comprehensive Income	-	-	124	124
31 December 2016	1	1,347	13	1,361
Prior period opening balance	1	4	(83)	(78)
Charged / (credited) to Income Statement	-	(83)	33	(50)
Charged / (credited) to Other Comprehensive Income	-	-	2	2
Prior year adjustment	-	951	-	951
31 December 2015	1	872	(48)	825

Centrica Energy Limited

Notes to the Financial Statements for the Year Ended 31 December 2016 (continued)

11 Investments in subsidiaries, associates and joint ventures

Investments classified as non-current

Equity investments	Shares in group undertakings (subsidiaries) £ 000	Total £ 000
Cost		
At 1 January 2016	850	850
At 31 December 2016	850	850
At 1 January 2015	850	850
At 31 December 2015	850	850

Details of the equity interests of the Company in its subsidiaries undertakings are as follows as at 31 December 2016:

Name of subsidiary	Principal activity	Class of shares held	Country of incorporation and principal place of business	Proportion of ownership interest and voting rights held	
				2016	2015
Centrica Energy (Trading) Limited	Agency and arranging services	Ordinary shares	United Kingdom	100%	100%

The Directors consider that the carrying value of the investments is supported by their underlying net assets.

12 Cash and cash equivalents

	2016 £ 000	2015 £ 000
Cash at bank	3,110	6,637

Cash at bank and in hand includes bank balances of £3,110,000 (2015: £6,637,000) that primarily represents cash that is required to be held to fulfil exchange requirements.

Centrica Energy Limited

Notes to the Financial Statements for the Year Ended 31 December 2016 (continued)

13 Trade and other receivables

	2016	Restated
	Current	2015
	£ 000	Current
		£ 000
Trade receivables	143	272
Amounts owed by group undertakings	97,797	349,213
Accrued energy income	577,440	503,753
Prepayments	-	1
Other receivables	86,778	89,242
	<u>762,158</u>	<u>942,481</u>

Trade receivables during the current year are all classed as current and none are overdue. Trade receivables in the prior year were all classed as current and none were overdue.

The 2015 comparatives have been restated to net down intercompany balances with British Gas Trading Limited as they meet the offsetting requirements under IAS 32. Amounts owed by group undertakings has reduced by £84,349,000 as a result of this restatement.

The amounts receivable from Group undertakings include £47,301,000 (2015: £345,912,000) that bears interest at a quarterly rate determined by Group Treasury and linked to the Group cost of funds. The quarterly rates ranged between 3.04 and 4.04% per annum during 2016 (2015: 2.36 and 2.88%). The other amounts receivable from Group undertakings are interest-free. All amounts receivable from Group undertakings are unsecured and repayable on demand.

The fair value of those trade and other receivables classified as financial instrument loans and receivables are disclosed in the financial instruments note 21.

The Company's exposure to credit and market risks, including impairments and allowances for credit losses, relating to trade and other receivables is disclosed in note 20 "Financial risk management and impairment of financial assets".

14 Inventories

	2016	2015
	£ 000	£ 000
Gas in storage	<u>5,608</u>	<u>-</u>

There is no significant difference between the replacement cost of inventories and their carrying amounts

Centrica Energy Limited

Notes to the Financial Statements for the Year Ended 31 December 2016 (continued)

15 Derivative financial instruments

	2016		2015	
	Current £ 000	Non-current £ 000	Current £ 000	Non-current £ 000
Derivative financial assets	1,291,322	5,914	1,696,565	8,652
Derivative financial liabilities	(1,350,499)	-	(1,595,846)	-
	<u>(59,177)</u>	<u>5,914</u>	<u>100,719</u>	<u>8,652</u>

16 Trade and other payables

	2016		Restated 2015	
	Current £ 000	Non-current £ 000	Current £ 000	Non-current £ 000
Trade payables	(137)	-	(11,651)	-
Accrued expenses	(570,319)	(7,057)	(431,699)	(4,815)
Amounts owed to group undertakings	(4,358)	-	(85,753)	-
Social security and other taxes	(106)	-	(57)	-
Other payables	(22,154)	-	(81,194)	-
	<u>(597,074)</u>	<u>(7,057)</u>	<u>(610,354)</u>	<u>(4,815)</u>

The fair value of the trade and other payables classified as financial instruments are disclosed in the financial instruments note 21.

The 2015 comparatives have been restated to net down intercompany balances with British Gas Trading Limited as they meet the offsetting requirements under IAS 32. Amounts owed to group undertakings has reduced by £84,349,000 as a result of this restatement.

The Company's exposure to market and liquidity risks, including maturity analysis, related to trade and other payables is disclosed in note 20 "Financial risk management and impairment of financial assets".

Amounts owed to group undertakings are interest-free, unsecured and repayable on demand.

Centrica Energy Limited

Notes to the Financial Statements for the Year Ended 31 December 2016 (continued)

17 Post-employment benefits

Summary of main schemes

The Company's employees participate in the following defined benefit pension schemes: Centrica Pension Plan (CPP) and Centrica Pension Scheme (CPS). Its employees also participate in the defined contribution section of the Centrica Pension Scheme. Information on these schemes is provided in note 22 of the Centrica plc 2016 Annual Report and Accounts.

Together with the Centrica Engineers Pension Scheme (CEPS), CPP and CPS form the majority of the Company's defined benefit obligation and are referred to below and in the Centrica plc 2016 Annual Report and Accounts as the 'Registered Pension Schemes'.

Accounting assumptions, risks and sensitivity analysis

The accounting assumptions, risks and sensitivity analysis for the Registered Pension Schemes are provided in note 22 to the Group Financial Statements.

Reconciliation of scheme assets and liabilities

The amounts recognised in the statement of financial position are as follows:

	2016			2015		
	Assets £ 000	Liabilities £ 000	Total £ 000	Assets £ 000	Liabilities £ 000	Total £ 000
1 January	3,897	(3,628)	269	4,336	(3,923)	413
Items included in the Income Statement:						
Current service cost	-	(53)	(53)	-	(65)	(65)
Interest (expense) / income	149	(141)	8	167	(152)	15
Past service credit	-	113	113	-	22	22
Other movements:						
Re-measurement (losses)/gains	954	(1,509)	(555)	(572)	383	(189)
Employer contributions	152	-	152	73	-	73
Benefits paid from schemes	(113)	113	-	(107)	107	-
31 December	<u>5,039</u>	<u>(5,105)</u>	<u>(66)</u>	<u>3,897</u>	<u>(3,628)</u>	<u>269</u>

Centrica Energy Limited

Notes to the Financial Statements for the Year Ended 31 December 2016 (continued)

17 Post-employment benefits (continued)

Presented in the statement of financial position as:

	2016 £ 000	2015 £ 000
Defined benefit pension assets	-	269
Defined benefit pension liabilities	(66)	-
	<u>(66)</u>	<u>269</u>

Analysis of the actuarial gains/(losses) recognised in reserves

	2016 £ 000	2015 £ 000
Actuarial gain/(loss) (actual return less expected return on pension scheme assets)	954	(572)
Experience gain/(loss) arising on the scheme liabilities	22	(110)
Changes in assumptions underlying the present value of the schemes' liabilities	(1,531)	493
Cumulative actuarial losses recognised in reserves at 1 January, before adjustment for taxation	(1,802)	(1,613)
Cumulative actuarial losses recognised in reserves at 31 December, before adjustment for taxation	<u>(2,357)</u>	<u>(1,802)</u>

Pension scheme contributions

Note 22 to the Group Financial Statements provides details of the triennial review based on the position at 31 March 2015 in respect of the UK Registered Pension Schemes and the asset-backed contribution arrangements. Under IAS 19: 'Retirement benefits (revised 2011)', the Company's contribution and trustee interest in the Scottish limited partnerships are recognised as scheme assets.

The Company estimates that it will pay £42,000 of employer contributions during 2017 at an average rate of 20% of pensionable pay, with contributions via the salary sacrifice arrangements of £18,000.

Although the Group has established a new funding arrangement in the year based on the position as at 31 March 2015, it should be noted that the market rates, from which the discount rate is derived, have continued to decline in the subsequent period. The Group continues to monitor its pension liabilities on an ongoing basis, including assessing various scenarios that may arise and their potential implications for the business.

Defined contribution pension scheme contributions

The total cost charged to income of £266,000 (2015: £219,000) represents contributions payable to these schemes by the Company at rates specified in the rules of the scheme.

Centrica Energy Limited

Notes to the Financial Statements for the Year Ended 31 December 2016 (continued)

17 Post-employment benefits (continued)

Pension scheme assets

Categories of scheme assets are as follows:

	2016			2015		
	Quoted £ 000	Unquoted £ 000	Total £ 000	Quoted £ 000	Unquoted £ 000	Total £ 000
Equities	1,970,000	307,000	2,277,000	1,867,000	219,000	2,086,000
Property	-	319,000	319,000	-	315,000	315,000
Diversified asset funds	50,000	-	50,000	47,000	-	47,000
Asset-backed contribution assets	-	406,000	406,000	-	243,000	243,000
Cash pending investment	276,000	-	276,000	60,000	-	60,000
Liability matching assets	1,241,000	844,000	2,085,000	874,000	556,000	1,430,000
High yield debt	309,000	1,296,000	1,605,000	167,000	780,000	947,000
Corporate bonds	<u>1,274,000</u>	<u>-</u>	<u>1,274,000</u>	<u>1,717,000</u>	<u>-</u>	<u>1,717,000</u>
Group pension scheme assets (i)	<u>5,120,000</u>	<u>3,172,000</u>	<u>8,292,000</u>	<u>4,732,000</u>	<u>2,113,000</u>	<u>6,845,000</u>
Company share of the above (£ 000)						
Company share of the above (£'000)	<u>5,039</u>	<u>-</u>	<u>5,039</u>	<u>3,897</u>	<u>-</u>	<u>3,897</u>

(i) Total pension scheme assets for the UK pension schemes.

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 corporate bonds and liability matching 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.

Centrica Energy Limited

Notes to the Financial Statements for the Year Ended 31 December 2016 (continued)

18 Capital and reserves

Allotted, called up and fully paid shares

	2016		2015	
	Number	Value £	Number	Value £
Ordinary shares of £1 each	50,196	50,196	50,000	50,000
Preference shares of £1 each	-	-	196	196
Total	50,196	50,196	50,196	50,196

Other share instruments issued

All Ordinary shares issued are classified as 'equity instruments' in accordance with IAS 32 'Financial instruments: presentation'. Similarly, the Preference shares are classified as an equity instruments as they meet the IAS 32 criteria for being classified as such as the redemption option is held by the issuer i.e. the Company.

The holders of Ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at meetings of the Company.

A special resolution was passed during the year to redesignate all the Preference shares of £1.00 each into Ordinary shares of £1.00 each, varying the class rights attached to the Preference shares by cancelling the Preference share class and adopting new Articles of Association.

Other reserves

Other reserves is mainly made up of the share-based payments reserve which reflects the obligation to deliver shares to employees under the existing share schemes in return for services provided to the Company.

Retained earnings

The balance classified as retained earnings includes the profits and losses realised by the Company in previous periods that were not distributed to the shareholders of the Company at the balance sheet date.

Centrica Energy Limited

Notes to the Financial Statements for the Year Ended 31 December 2016 (continued)

19 Dividends paid and proposed

	2016 £ 000	2015 £ 000
<i>Declared and paid during the year</i>		
Final dividend of £Nil (2015 - £Nil) per ordinary share	-	-
Interim dividend of £7,200.0 (2015 - £Nil) per ordinary share	360,000	-
	<u>360,000</u>	<u>-</u>

Proposed for approval by shareholders at the AGM

The Directors are proposing a final dividend for 2016 of £Nil (2015 - £Nil) per share totalling £Nil (2015 - £Nil).

20 Financial risk management

The Company's normal operating, investing and financing activities expose it to a variety of financial risks: market risk (including commodity price risk, currency risk and interest rate risk), credit risk and liquidity risk. The Company's overall financial risk management processes are designed to identify, manage and mitigate these risks.

Centrica Energy Limited

Notes to the Financial Statements for the Year Ended 31 December 2016 (continued)

20 Financial risk management (continued)

Market risk management

Market risk is the risk of loss that results from changes in market prices (commodity prices, foreign exchange rates and interest rates). The level of market risk to which the Company 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 Company's physical asset and contract portfolios.

Commodity price risk management

The most significant financial risk facing the Company relates to commodity prices, in particular for gas and electricity. Commodity price risk is the risk that changes to gas and electricity period prices would impact the net fair value of commodity contracts held for trading.

The Company'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 Company conducts its trading activities over the counter and through exchanges in the UK and parts of the rest of Europe. The Company 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 Company sets volumetric and VaR limits to manage the commodity price risk exposure associated with the Company'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 Company would expect it to take to close off a trading position.

The VaR, before taxation, associated with the Company's proprietary energy trading activities at 31 December 2016 was £1,113,000 (2015: £2,347,000).

Currency risk management

Currency risk is the risk that movements in foreign currency exchange rates will result in exchange gains and losses that are taken to the income statement. Currency risk arises when future commodity trading contracts or recognised assets or liabilities are denominated in a currency that is not the functional currency of the Company. The Company manages its foreign exchange risk by entering into forward contracts transacted with Group Treasury.

Sensitivity Analysis

An analysis of the sensitivity of the Company's financial position and performance to changes in foreign exchange rates has been performed. The Company deems 10% movements in the US Dollar and Euro currency rates relative to pounds sterling, to be reasonably possible. The impact of such movements on profit and equity, both before and after taxation is detailed below.

For the US Dollar, a 10% upward movement would decrease profit by £(347,000) (2015: £(169,000)) and a 10% downward movement would increase profit by £424,000 (2015: £206,000).

For the Euro, a 10% upward movement would decrease profit by £(1,537,000) (2015: £(309,000)) and a 10% downward movement would increase profit by £1,878,000 (2015: £377,000).

Interest rate risk management

Interest rate risk is managed centrally by Centrica plc.

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.

Centrica Energy Limited

Notes to the Financial Statements for the Year Ended 31 December 2016 (continued)

20 Financial risk management (continued)

The Company is exposed to credit risk in its trading, energy procurement and downstream activities. The maximum exposure to Counterparty credit risk from financial assets, as a result of trading and energy procurement activities is measured by counterparty credit rating as follows:

	2016			2015 Restated		
	Derivative financial instruments with positive fair values	Receivables from treasury, trading and energy with procurement counterparties	Cash and cash equivalents	Derivative financial instruments with positive fair values	Receivables from treasury, trading and energy with procurement counterparties	Cash and cash equivalents
	£ 000	£ 000	£ 000	£ 000	£ 000	£ 000
AAA to AA	6	-	-	-	242	6,227
AA- to A-	278,974	229,153	3,056	232,107	724,266	-
BBB+ to BBB-	864,315	366,917	54	1,159,162	110,607	410
BB+ to BB-	102,305	109,295	-	295,368	101,893	-
B or lower	22,428	43,981	-	9,412	381	-
Unrated	29,208	12,812	-	9,168	5,092	-
Total	1,297,236	762,158	3,110	1,705,217	942,481	6,637

(i) The unrated counterparty receivables primarily comprise amounts due from subsidiaries of rated entities, exchanges or clearing houses.

The 2015 comparatives have been restated to re-categorise £766,762,000 of derivative financial instruments with British Gas Trading Limited from Unrated to the BBB+ to BBB- category. The 2015 comparatives have also been restated to net down intercompany balances with British Gas Trading Limited as they meet the offsetting requirements under IAS 32. Receivables from treasury, trading and energy with procurement counterparties has reduced by £84,349,000 as a result of this restatement within the BBB+ to BBB- category.

The Company uses master netting agreements to reduce credit risk and net settles payments with counterparties where net settlement provisions exists (see table in note 21 under 'Financial assets and liabilities subject to offsetting, master netting arrangements and similar arrangements' for details of the amounts offset). In addition, the Company employs a variety of other methods to mitigate credit risk: margining, various forms of bank and parent company guarantees and letters of credit. See below for details of cash posted or received under margin or collateral arrangements.

Liquidity risk management

Liquidity risk is the risk that the Company is unable to meet its financial obligations as they fall due. Cash forecasts identifying the liquidity requirements of the Company are produced frequently. These are reviewed regularly to ensure sufficient financial headroom exists for at least a 12 month period. The Company finances its operations through a combination of cash flow from operations and financing received from other Centrica Group companies. Liquidity risk is managed centrally by Centrica plc.

Centrica Energy Limited

Notes to the Financial Statements for the Year Ended 31 December 2016 (continued)

20 Financial risk management (continued)

Maturity profiles

Maturities of derivative financial instruments, provisions, borrowings, and trade and other payables are provided in the following tables (all amounts are remaining contractual undiscounted cash flows):

Due for payment 2016	<1 year £ 000	1-2 years £ 000	2-3 years £ 000	3-4 years £ 000	4-5 years £ 000	>5 years £ 000
Energy and interest derivatives in a loss position that will be settled on a net basis	(14,363)	(29,472)	(2,208)	(1,607)	-	-
Gross energy procurement contracts and related derivatives carried at fair value (i)	(3,076,441)	(1,166,883)	(232,234)	(15,761)	-	-
Due for payment 2015 Restated	<1 year £ 000	1-2 years £ 000	2-3 years £ 000	3-4 years £ 000	4-5 years £ 000	>5 years £ 000
Energy and interest derivatives in a loss position that will be settled on a net basis	(155,447)	(27,742)	-	-	-	-
Gross energy procurement contracts and related derivatives carried at fair value (i)	(3,135,224)	(1,061,309)	(240,244)	(9,637)	(733)	-

(i) Proprietary energy trades are excluded from this maturity analysis as we do not take physical delivery of volumes traded under these contracts. The associated cash flows are expected to be equal to the contract fair value at the balance sheet date.

The 2015 comparatives have been restated to include intergroup positions within Energy and interest derivatives in a loss position that will be settled on a net basis of £154,447,000 (<1 year) and £27,742,000 (1-2 years).

The Company's liquidity is impacted by the cash pledged or received under margin and collateral agreements. The terms and conditions of these depend on the counterparty and the specific details of the transaction. Cash is generally returned to the Company or by the Company within two days of trade settlement. The table below summarises the movements in margin cash:

	2016 £ 000	2015 £ 000
Net cash received / (pledged) as collateral at 1 January	(13,430)	(85,716)
Net cash inflow	20,050	72,286
Net cash received / (pledged) as collateral at 31 December (i)	6,620	(13,430)

(i) Of the net cash collateral received / (pledged), £(19,100,000) (2015: £(75,322,000)) is included within Trade and other payables and £25,720,000 (2015: £61,892,000) within Trade and other receivables.

Centrica Energy Limited

Notes to the Financial Statements for the Year Ended 31 December 2016 (continued)

21 Fair value of financial instruments

Fair value

The fair value of the Company's financial instruments, together with the carrying amounts included in the balance sheet are analysed below:

	2016	2015 Restated
	Carrying value/ Fair value	Carrying value/ Fair value
	£ 000	£ 000
Loans and receivables:		
Trade receivables	143	272
Other receivables	86,778	89,243
Accrued energy income	577,440	503,753
Cash and cash equivalents	3,110	6,637
Amounts owed by group undertakings	97,797	349,213
Derivative financial instruments	1,297,236	1,705,217
Total financial assets	2,062,504	2,654,335
Financial liabilities measured at amortised cost:		
Trade payables	(137)	(11,651)
Accrued expense	(577,376)	(436,514)
Other payables	(22,154)	(81,194)
Amounts owed to group undertakings	(4,358)	(85,753)
Derivative financial instruments	(1,350,499)	(1,595,846)
Total financial liabilities	(1,954,524)	(2,210,958)

The carrying value of the Company's financial assets and liabilities are approximately equal to their fair value.

The 2015 comparatives have been restated to net down intercompany balances with British Gas Trading Limited as they meet the offsetting requirements under IAS 32. Amount owed by group undertakings and Amounts owed to group undertakings both reduced by £84,349,000 as a result of this restatement.

Loans and receivables and financial liabilities measured at amortised cost

Due to their nature and/or short term maturity, the fair values of trade and other receivables, cash and cash equivalents, amounts owed by group undertakings, trade and other payables, provisions and amounts owed to group undertakings are estimated to approximate their carrying values.

Centrica Energy Limited

Notes to the Financial Statements for the Year Ended 31 December 2016 (continued)

21 Fair value of financial instruments (continued)

Financial instruments carried at fair value

Determination of fair values and fair value hierarchy

Financial assets and financial liabilities measured and held at fair value are classified into one of three categories, known as hierarchy levels, which are defined according to the inputs used to measure fair value as follows:

- Level 1: Fair value is determined using observable inputs that reflect unadjusted quoted market prices for identical assets and liabilities.
- Level 2: Fair value is determined using significant inputs that may be directly observable inputs or unobservable inputs that are corroborated by market data.
- Level 3: Fair value is determined using significant unobservable inputs that are not corroborated by market data and may be used with internally developed methodologies that result in managements' best estimate of fair value.

Fair value hierarchy

	<i>Fair value hierarchy</i>		
	Fair value and carrying value £ 000	Level 2 £ 000	Level 3 £ 000
31 December 2016			
<i>Financial assets at fair value through profit or loss:</i>			
Derivative financial assets - held for trading			
Foreign exchange derivatives	1,935	1,935	-
Energy derivative contracts	<u>1,295,301</u>	<u>1,270,400</u>	<u>24,901</u>
Total financial assets at fair value through profit or loss	<u>1,297,236</u>	<u>1,272,335</u>	<u>24,901</u>
Derivative financial liabilities - held for trading			
Energy derivative contracts	<u>(1,350,499)</u>	<u>(1,340,426)</u>	<u>(10,073)</u>
Total financial liabilities at fair value through profit or loss	<u>(1,350,499)</u>	<u>(1,340,426)</u>	<u>(10,073)</u>
Total financial instruments at fair value	<u><u>(53,263)</u></u>	<u><u>(68,091)</u></u>	<u><u>14,828</u></u>

Centrica Energy Limited

Notes to the Financial Statements for the Year Ended 31 December 2016 (continued)

21 Fair value of financial instruments (continued)

31 December 2015 Restated	Fair value and carrying value £ 000	Level 2 £ 000	Level 3 £ 000
Financial assets at fair value through profit or loss:			
Derivative financial assets - held for trading			
Foreign exchange derivatives	5,637	5,637	-
Energy derivative contracts	<u>1,699,580</u>	<u>1,672,191</u>	<u>27,389</u>
Total financial assets at fair value through profit or loss	<u>1,705,217</u>	<u>1,677,828</u>	<u>27,389</u>
Derivative financial liabilities - held for trading			
Energy derivative contracts	<u>(1,595,846)</u>	<u>(1,552,210)</u>	<u>(43,636)</u>
Total financial liabilities at fair value through profit or loss	<u>(1,595,846)</u>	<u>(1,552,210)</u>	<u>(43,636)</u>
Total financial instruments at fair value	<u>109,371</u>	<u>125,618</u>	<u>(16,247)</u>

There were no material transfers during the financial year between level 1 and 2.

The 2015 comparatives have been restated to include £14,611,000 of derivative financial assets - held for trading as level 2 instead of level 3 and £1,636,000 of derivative financial liabilities - held for trading as level 3 instead of level 2 due to the re-classification of certain derivative contracts.

Level 3 fair value reconciliation

The reconciliation of the Level 3 fair value measurements during the year is as follows:

	Derivatives instruments (assets and liabilities) £ 000
2016	
Level 3 financial instruments	
1 January	(16,247)
Total realised and unrealised (losses)/gains:	
Recognised in the income statement	<u>31,075</u>
31 December	<u>14,828</u>

Centrica Energy Limited

Notes to the Financial Statements for the Year Ended 31 December 2016 (continued)

21 Fair value of financial instruments (continued)

	Derivatives instruments (assets and liabilities) £ 000
2015 Restated	
Level 3 financial instruments	
1 January	-
Total realised and unrealised (losses)/gains:	
Recognised in the income statement	(16,247)
31 December	<u>(16,247)</u>

The 2015 comparatives have been restated due to a re-classification amounting to £16,247,000 of certain contracts between level 2 and level 3.

Methods and assumptions

There were no material transfers during the financial year between level 1 and 2.

Transfers between fair value hierarchy levels are based on the values of the relevant assets and liabilities at the beginning of the reporting period.

The Company has classified fair value measurements using a fair value hierarchy that reflects the significance of the inputs used in marking the measurements. The fair value hierarchy has the following levels:

- quoted prices in active markets for the same instrument (ie without modification or repackaging) (Level 1);
- quoted prices in active markets for similar assets or liabilities or other valuation techniques for which all significant inputs are based on observable market data (Level 2); and
- valuation techniques for which any significant input is not based on observable market data (Level 3).

Assessing the significance of a particular input requires judgement. For the purposes of the fair value hierarchy, the Directors have determined Level 2 as the appropriate hierarchy level for all valuations generated from the Company's trading system given that all financial assets and financial liabilities measured and held at fair value mature within the active period. For trades currently assessed using valuation techniques outside the trading system, the Directors have determined Level 3 as the appropriate level.

Centrica Energy Limited

Notes to the Financial Statements for the Year Ended 31 December 2016 (continued)

21 Fair value of financial instruments (continued)

Valuation techniques used to derive Level 2 and 3 fair values and valuation process

Level 2 foreign exchange derivatives comprise forward foreign exchange contracts which are fair valued using forward exchange rates that are quoted in an active market.

Level 2 energy derivatives are fair valued by comparing and discounting the difference between the expected contractual cash flows for the relevant commodities and the quoted prices for those commodities in an active market. The average discount rate applied to value this type of contract during 2016 was 1% per annum (2015: 1% per annum).

For Level 3 energy derivatives, the main input used by the Company pertains to deriving expected future commodity prices in markets that are not active as far into the future as some of our contractual terms. The active period for the UK Gas, Power, Coal, Emissions and Oil markets is deemed to be 3 years. Fair values are then calculated by comparing and discounting the difference between the expected contractual cash flows and these derived future prices using an average discount rate of 1% per annum (2015: 2%).

Because the Level 3 energy derivative valuations involve the prediction of future commodity market prices, sometimes a long way into the future, reasonably possible alternative assumptions for gas, power, coal, emissions or oil prices may result in a higher or lower fair value for Level 3 financial instruments. Given the relative size of these fair values, it is unlikely that the impact of these reasonably possible changes would be significant when judged in relation to the Company's profit and loss or total asset value.

The Group's valuation process includes specific teams of individuals that perform valuations of the Group's derivatives for financial reporting purposes, including Level 3 valuations. The Group has an independent team that derives future commodity price curves based on available external data and these prices feed in to the energy derivative valuations. The price curves are subject to review and approval by the Centrica plc's Investment Sub-Committee and valuations of all derivatives, are also reviewed regularly as part of the overall risk management process.

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. The amount that has yet to be recognised in the Company 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:

	2016	2015 Restated
	£ 000	£ 000
Net deferred gains/(losses)		
1 January	(5,670)	-
Net losses deferred on new transactions	(6,480)	(6,667)
Recognised in the Income Statement during the year	3,918	997
31 December	(8,232)	(5,670)

The 2015 comparatives have been restated to include £6,667,000 of day one losses on new structured contracts and £873,000 of day one losses recognised in the income statement during the year.

Centrica Energy Limited

Notes to the Financial Statements for the Year Ended 31 December 2016 (continued)

21 Fair value of financial instruments (continued)

Financial assets and liabilities subject to offsetting, master netting arrangements and similar arrangements

				Related amounts not offset in the Company Balance Sheet (i)		
	Gross amounts of recognised financial instruments	Gross amounts of recognised financial instruments offset in the Company Balance Sheet	Net amounts presented in the Company Balance Sheet	Financial instruments	Collateral	Net amount
31 December 2016	£ 000	£ 000	£ 000	£ 000	£ 000	£ 000
Derivative financial assets	7,305,292	(6,008,056)	1,297,236	(454,451)	(19,100)	823,685
Derivative financial liabilities	(7,358,555)	6,008,056	(1,350,499)	454,451	25,720	(870,328)
Total derivatives	(53,263)	-	(53,263)	-	6,620	(46,643)
Accrued energy income	5,482,413	(4,813,608)	668,805	(81,201)	-	587,604
Accruals for commodity costs	(5,417,867)	4,813,608	(604,259)	81,201	-	(523,058)

Centrica Energy Limited

Notes to the Financial Statements for the Year Ended 31 December 2016 (continued)

21 Fair value of financial instruments (continued)

				Related amounts not offset in the Company Balance Sheet (i)		
	Gross amounts of recognised financial instruments	Gross amounts of recognised financial instruments offset in the Company Balance Sheet	Net amounts presented in the Company Balance Sheet	Financial instruments	Collateral	Net amount
31 December 2015	£ 000	£ 000	£ 000	£ 000	£ 000	£ 000
Derivative financial assets	8,150,189	(6,444,972)	1,705,217	(649,853)	(75,322)	980,042
Derivative financial liabilities	(8,040,818)	6,444,972	(1,595,846)	649,853	61,892	(884,101)
Total derivatives	109,371	-	109,371	-	(13,430)	95,941
Accrued energy income	4,647,499	(3,935,057)	712,442	(191,570)	-	520,872
Accruals for commodity costs	(4,660,400)	3,935,057	(725,343)	191,570	-	(533,773)

(i) The Company has arrangements in place with various counterparties in respect of commodity trades which provide for a single net settlement of all financial instruments covered by the arrangement in the event of default or termination, or other circumstances arising whereby either party is unable to meet its obligations. The above table shows the potential impact of these arrangements being enforced by offsetting the relevant amounts within each Company Balance Sheet class of asset or liability.

22 Parent and ultimate parent undertaking

The immediate parent undertaking is GB Gas Holdings Limited, a company registered in England and Wales.

The ultimate parent and controlling party is Centrica plc, a company registered in England and Wales, which is the only company to include these financial statements in its consolidated statements. Copies of the Centrica plc consolidated financial statements may be obtained from www.centrica.com.