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中國石化鎮海煉油化工有限公司
Sinopec Zhenhai Refining & Chemical Company Limited

(a joint stock limited company incorporated in the People's Republic of China with limited liability)

(Stock Code: 1128)

Announcement

The Company was granted waivers from strict compliance with the relevant provisions of the Listing Rules by the Hong Kong Stock Exchange with respect to certain Continuing Connected Transactions with Sinopec Group Company and its associates referred to in the prospectus published at the time of the Company's initial public offer on 15 November 1994. These connected transactions included purchases of domestic crude oil and other raw materials, import of crude oil, sales of refined products or by-products, research and development arrangements, insurance arrangements and carrying out of construction and overhaul of production and other facilities.

The Hong Kong Stock Exchange subsequently confirmed in February 2000 when Sinopec Group Company, formerly a substantial shareholder having a direct interest in the Company, underwent a major reorganisation to establish Sinopec Corp, that these waivers would remain valid following such reorganisation.

As a result of recent changes to the Listing Rules, these waivers are no longer valid and the Company must comply with the relevant Listing Rules requirements for it to continue conducting the Continuing Connected Transactions previously subject to waivers.

In addition, the Company proposes to enter other Continuing Connected Transactions in respect of the agency sales of products, financial services and land management and leasing with Sinopec Corp and Sinopec Group Company.

On 19 August 2005, the Company entered into the Mutual Supply Framework Agreement and Comprehensive Services Framework Agreement with Sinopec Corp and Sinopec Group Company, respectively, in respect of the Continuing Connected Transactions.

Under the Listing Rules, the purchase of raw materials, sales of products and services, construction and overhaul services, financial services and agency sales of products are Non-Exempt Continuing Connected Transactions and subject to reporting, announcement and the approval of the Company's Independent Shareholders. Insurance arrangement, research and development and land management and leasing are Continuing Connected Transactions subject to reporting and announcement.

The Company has appointed Partners Capital as the independent financial adviser to advise the independent board committee in respect of the Non-Exempt Continuing Connected Transactions. A circular containing details of the Continuing Connected Transactions together with a notice of, and forms of proxy for, a shareholders' meeting to approve the non-exempt Continuing Connected Transactions, and including the advice of Partners Capital in respect of the terms of the Non-Exempt Continuing Connected Transactions, will be despatched to the shareholders of the Company as soon as is reasonably practicable. Shareholders of the Company who are deemed to have an interest in any of the Continuing Connected Transaction shall abstain from voting at the relevant shareholders' meeting.

1. INTRODUCTION

The Company was granted waivers from strict compliance with the relevant provisions of the Listing Rules by the Hong Kong Stock Exchange with respect to certain Continuing Connected Transactions with Sinopec Group Company and its associates at the time of the Company's initial public offer on 15 November 1994. These transactions included purchases of domestic crude oil and other raw materials, import of crude oil, sales of refined products or by-products, research and development arrangements, insurance arrangements and carrying out of construction and overhaul of production and other facilities.

The Hong Kong Stock Exchange subsequently confirmed in February 2000 when Sinopec Group Company, formerly a substantial shareholder having a direct interest in the Company, underwent a major reorganisation to establish Sinopec Corp, that these waivers would remain valid following such reorganisation.

As a result of recent changes to the Listing Rules, these waivers are no longer valid and the Company must now comply with the relevant Listing Rules requirements for it to continue conducting the Continuing Connected Transactions previously subject to waivers.

In addition, the Company proposes to enter other Continuing Connected Transactions in respect of the agency sales of products, financial services and land management and leasing with Sinopec Corp and Sinopec Group Company.

2. CONTINUING CONNECTED TRANSACTIONS

2.1 Overview

On 19 August 2005, the Company and Sinopec Corp entered into the Mutual Supply Framework Agreement. On the same day, the Company and Sinopec Group Company entered into the Comprehensive Service Framework Agreement. The Framework Agreements, which govern the Continuing Connected Transactions, will expire on 31 December 2007.

Sinopec Corp and its associates will be the counter-parties of the Continuing Connected Transactions under the Mutual Supply Agreement. Sinopec Group Company and its associates will be the counter-parties of the Continuing Connected Transactions under the Comprehensive Services Agreement.

The table below sets forth a summary of the Mutual Supply Framework Agreement and the Comprehensive Services Framework Agreement:

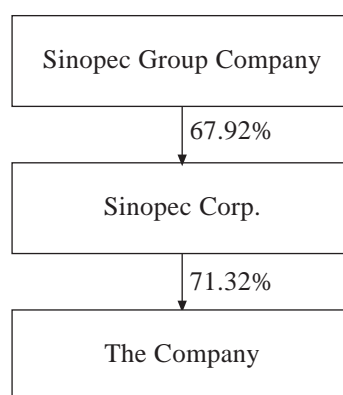
Category of connected transaction	Segment by product or activity	Historical figures (in RMB million) for the years ending 31 December			Estimated amount (in RMB million) for the years ending 31 December		
		2002	2003	2004	2005	2006	2007
Mutual Supply Framework Agreement							
(1) Purchases of raw materials	Crude oil and other raw materials, auxiliary materials, power and fuel, and services	5,765	8,311	14,928	37,619	55,192	78,965
(2) Sales of products and services	Sale of refined products, intermediate petrochemical products and other petroleum refined by-products	14,575	21,365	32,124	53,973	74,622	102,155
(3) Agency sales of products	Commission	0	0	0	74	153	192
Comprehensive Services Framework Agreement							
(4) Construction and overhaul services	Construction and overhaul of production and other facilities	383	1,178	788	3,100	12,170	13,434
(5) Financial services	Deposits and related interest income	0	0	0	1,752	1,902	1,952
(6) Insurance services	Insurance premium expenses	41	45	54	56	66	83
	Safety funds received	19	18	17	20	25	33

Category of connected transaction	Segment by product or activity	Historical figures (in RMB million) for the years ending 31 December			Estimated amount (in RMB million) for the years ending 31 December		
		2002	2003	2004	2005	2006	2007
		(7) Research and development services	Research and development expenses	35	35	0	35
	Research and development subventions received	5	8	0	10	12	18
(8) Land management and leasing services	Operating lease expenses	0	0	13	15	29	36

2.2 Connected persons and their Relationships

Sinopec Corp holds approximately 71.32% equity interest of the Company's issued share capital and is the controlling shareholder of the Company. Sinopec Group Company is the ultimate parent of the Company. Principal operations of Sinopec Corp and Sinopec Group Company, together with their associates, are exploration, extracting and sale of crude oil and natural gas; pipe transportation of crude oil and natural gas; oil refining; production, sale and transportation of petrochemical, fibre and other chemical products, wholesaling, retailing, storage and transportation of oil products and other petroleum products; operation of convenient stores; production of electricity; production and installation of machineries; design and construction; purchase and sale of raw materials, coal, equipment and apparatus; production and management of equipment; research, development and application of technologies and information; import and export business; transfer of technology and labour.

The ownership and controlling relationship between the Company and ultimate parent are set out below:



The Company and each of the connected persons involved in the Continuing Connected Transactions (except where the connected party is Sinopec Group Company) are owned by the same ultimate parent, Sinopec Group Company, either directly or indirectly.

2.3 Background, Reasons for Transactions, Pricing Policies and Caps

2.3.1 Purchases of crude oil and other raw materials, auxiliary materials, power and fuel and corresponding services

Background: The Company produces products including petroleum products, intermediate petrochemical products and other petroleum refined by-products. All of these products are produced from processing of crude oil, other raw materials, and auxiliary materials. Since the Company's initial public offer on 15 November 1994, the Company has been purchasing crude oil, other raw materials and auxiliary materials from Sinopec Corp and its associates, including

Sinopec Pipeline Transport & Storage Company (a branch of Sinopec Corp), China International United Petroleum & Chemicals Co., Ltd (a subsidiary of Sinopec Corp) and Sinopec Shengli Oilfield Co., Ltd. (a subsidiary of Sinopec Corp). Other raw materials include methanol, naphtha, methyl tertiary-butyl ether and residue; auxiliary materials include catalysts.

The table below sets forth the historical figures of the Company's aggregate purchases of raw materials from Sinopec Corp and its associates for each of the three years ended 31 December 2004:

	Historical Figures for the year ended 31 December		
	2002 <i>(RMB million)</i>	2003 <i>(RMB million)</i>	2004 <i>(RMB million)</i>
Import of crude oil	3,861	6,162	14,853
Purchase of domestically-produced crude oil	1,874	2,102	—
Import and export of crude oil service charges	<u>30</u>	<u>46</u>	<u>75</u>
	<u><u>5,765</u></u>	<u><u>8,311</u></u>	<u><u>14,928</u></u>

Source: Annual reports of the Company for 2003 and 2004.

The Company proposes to enter into the Mutual Supply Framework Agreement to continue to purchase crude oil and other raw materials, auxiliary materials, power and fuel and corresponding services from Sinopec Corp and its associates for the three years ending 31 December 2007.

Reasons for such transactions: China's oil and petrochemical industry has always been the subject of extensive regulation by the PRC government. Transactions involving crude oil are subject to State allocation. In accordance with the State plan, the Company's imported crude oil is allocated by Sinopec Corp, and the Company imports crude oil through the associates of Sinopec Corp. The Company also purchases domestically-produced crude oil from the associates of Sinopec Corp. Accordingly, the Company's allocation of raw material requirements are governed by State regulations and administrative measures of Sinopec Corp.

Pricing: Pursuant to the Mutual Supply Framework Agreement, the price of the crude oil related raw materials purchased from Sinopec Corp and its associates are determined as follows:

- (a) if there are applicable State (central and local governments) tariffs, the pricing of the Company's purchases shall be bound by the State tariffs; or
- (b) if there are no State tariffs, but there are applicable State guided prices, the pricing of the Company's purchases shall be bound by the State guided prices; or
- (c) if there are no applicable State tariffs or State guided prices, the pricing of the Company's purchases shall be determined in accordance with the prevailing market price (including any bidding price).

The Company will settle the purchases of crude oil and other raw materials, auxiliary materials, power and fuel and corresponding services by way of cash payments.

Caps: For the three years ending 31 December 2007, the annual transaction values in relation to the purchases of crude oil and other raw materials, auxiliary materials, power and fuel and corresponding services from Sinopec Corp and its associates shall not, in aggregate, exceed the caps of RMB37.6 billion (equivalent to HK\$36.1 billion), RMB55.2 billion (equivalent to HK\$53.0 billion) and RMB79 billion (equivalent to HK\$75.6 billion), respectively.

The caps referred to above are determined with reference to:

- (a) the previous transactions conducted and transaction amounts in respect of purchases of raw materials from Sinopec Corp and its associates. For the three years ended 31 December 2004, purchase of raw materials by the Company from Sinopec Corp and its associates increased by a compound annual growth rate of 61%;
- (b) the Company's estimate of its business growth;
- (c) the Company's estimate of the increase in its production capacity;
- (d) the Company's estimate of the increase in the costs of raw materials.

The Company's principal raw material is crude oil. In recent years, prices of crude oil have been fluctuating widely. The average dated price (freight-on-board) of Brent crude oil increased 15.5% in 2003, 32.7% in 2004 and 47% in the first half of 2005. The Company has taken into account the increasing crude oil price in determining the caps for the years ending 2005, 2006 and 2007.

Additionally, in 2004 the Company's comprehensive processing capacity was 16 million tpa. Since 2004, the Company has commenced the 20 million tpa refining capacity expansion project. In April 2005, the Company completed the construction and commenced operation of a 1 million tpa delayed coking unit, which led to an increase in comprehensive processing capacity to 18.5 million tpa. It is expected that by the end of 2006, the Company will complete construction and commence operation of a 1.5 million tpa hydrocracking unit and related auxiliary facilities, and will increase its comprehensive processing capacity to 20 million tpa. The completion of the new projects will significantly increase the production capacity of the Company, which also gives rise to an increase in the need for crude oil and other raw materials. Taking into account these factors, the Company arrives at the caps above.

2.3.2 Revenue from Petroleum Products Sales and Service Provision

Background: The products sold by the Company include refined products (such as gasoline, diesel, kerosene, naphtha, heavy fuel, solvent oil, clean oil and raw materials for clean oil), intermediate petrochemical products (such as benzene, PX, propylene and polypropylene) and other petroleum refined by-products (such as asphalt, petroleum coke and sulphur). Transactions involving sales and purchases of petroleum products (including gasoline, diesel and kerosene) are subject to regulation by the PRC government. Since the Company's initial public offer on 15 November 1994, the Company has been selling products and providing corresponding services in accordance with the State's requirement to Sinopec Corp and its associates. The Company convened extraordinary general meetings in December 2003 and February 2005 respectively which approved the connected transaction in relation to sales of PX entered into between the Company and Yizheng (a subsidiary of Sinopec Corp) and the connected transactions in relation to the sale of naphtha entered into between the Company and SECCO (an associate of Sinopec Corp). Further details of the connected transactions in relation to sales of PX and naphtha are contained in the Company's circulars dated 2 December 2003 and 24 December 2004, respectively. The Company's connected transaction with regards to PX with Yizheng will expire on 31 December 2005, and the connected transactions with regards to naphtha with SECCO will expire on 31 December 2007. Upon approval by the Independent Shareholders of the Mutual Supply Framework Agreement, the agreement entered into between the Company and Yizheng on 10 November 2003 in respect of PX will lapse and will be replaced by the Mutual Supply Framework Agreement. The agreement entered into between the Company and SECCO in respect of naphtha on 7 December 2004 will continue to be effective.

Sinopec Corp was one of the Company's five largest customers for the three years ended 31 December 2004. The table below sets forth the historical figures of the Company's aggregate sales of products and revenue from service provision to Sinopec Corp and its associates for each of the three years ended 31 December 2004:

	Historical Figures for the year ended 31 December		
	2002	2003	2004
	<i>(RMB million)</i>	<i>(RMB million)</i>	<i>(RMB million)</i>
Sales of PX to Yizheng	0	293	1,771
Sales of other products and provision of services to Sinopec Corp and its associates	<u>14,575</u>	<u>21,072</u>	<u>30,353</u>
	<u><u>14,575</u></u>	<u><u>21,365</u></u>	<u><u>32,124</u></u>

Source: Annual reports of the Company for 2003 and 2004.

The Company proposes to enter into the Mutual Supply Framework Agreement to continue to sell products and provide corresponding services to Sinopec Corp and its associates for the three years ending 31 December 2007.

Reasons for such transactions: China's oil and petrochemical industry has always been the subject of extensive regulation by the PRC government. Transactions involving the sale and purchase of petroleum products are controlled by the PRC government. Accordingly, the Company's sales of petroleum products are governed by the relevant PRC regulations and measures. These regulations and measures dictate the transaction value, the volume and all other terms and conditions at which the Company conducts its sales of petroleum products. Most of the end users of intermediate petrochemical products are Sinopec Corp and its associates, and selling to large customers can ensure stable sales.

Pricing: The selling prices of products and services to Sinopec Corp and its associates under the Mutual Supply Framework Agreement are determined as follows:

- (a) if there are applicable State (central and local governments) tariffs, the pricing of the Company's sales shall be bound by the State tariffs; or
- (b) if there are no State tariffs, but there are applicable State guided prices, the pricing of the Company's sales shall be bound by the State guided prices; or
- (c) if there are no applicable State tariffs or State guided prices, the pricing of the Company's sales shall be determined in accordance with the prevailing market price (including any bidding price).

Sinopec Corp and its associates will settle their purchases of the Company's petroleum products and related services by way of cash payments.

Caps: For the three years ending 31 December 2007, the annual transaction values in relation to the revenue of products sales and services provision to Sinopec Corp and its associates shall not, in aggregate, exceed the caps of RMB54.0 billion (equivalent to HK\$51.9 billion), RMB74.6 billion (equivalent to HK\$71.7 billion) and RMB102.2 billion (equivalent to HK\$98.2 billion), respectively.

The caps referred to above are determined with reference to:

- (a) the previous transactions conducted and transaction amounts in respect of sales of products and provision of services to Sinopec Corp and its associates (including Yizheng). For the three years ended 31 December 2004, sales of products and provision of services to Sinopec Corp and its associates increased by a compound annual growth rate of 48%;
- (b) the Company's estimate of the increase in the costs of raw materials;
- (c) the Company's estimate of the increase in the overall demand for petroleum products in the PRC; and
- (d) the Company's estimate of the increase in the market price of petroleum products and the market price of services. In general, market price of petroleum products increases as raw material price, in particular crude oil price, increases.

Additionally, in 2004 the Company's comprehensive processing capacity was 16 million tpa. Since 2004, the Company has commenced the 20 million tpa refining capacity expansion project. In April 2005, the Company completed the construction and commenced operation of a 1 million tpa delayed coking unit, which led to an increase in comprehensive processing capacity to 18.5 million tpa. It is expected that by the end of 2006, the Company will complete construction and commence operation of a 1.5 million tpa hydrocracking unit and related auxiliary facilities, and will increase its comprehensive processing capacity to 20 million tpa. The completion of the new projects will significantly increase the production capacity of the Company. Accordingly, the Company expects that its sales would increase as a result of an enlarged production capacity. Taking into account these factors, the Company arrives at the caps above.

2.3.3 Agency Sales of Petrochemical Products

Background: Currently, the Company sells its petrochemical products primarily by its sales personnel. The Company proposes to enter into the Mutual Supply Framework Agreement to appoint Sinopec Corp and its associates as agents of the Company in respect of the agency sales of the Company's petrochemical products for the three years ending 31 December 2007.

Reasons for such transactions: Trading, distribution and marketing of the Company's products are important elements in the success of the business of the Company. The Company considers the broadening of its trading, distribution and marketing network to be beneficial.

Sinopec Corp is one of the largest petrochemical companies in Asia and has a strong trading, distribution and marketing network. The Company believes that it will benefit from Sinopec Corp's experience, expertise and strong global network and will increase the sales of its petrochemical products and improve the Company's bargaining position with customers.

Pricing: Pursuant to the Mutual Supply Framework Agreement, the commissions payable to Sinopec Corp and its associates in connection with the agency sales of the Company's petrochemical products are determined on the prevailing market percentage commission of the agency sales of the Company's petrochemical products.

The Company will settle the agency commissions by way of cash payments.

Caps: For the three years ending 31 December 2007, the annual commission payable to Sinopec Corp and its associates for the agency sales of the Company's petrochemical products shall not, in aggregate, exceed the caps of RMB74 million (equivalent to HK\$71 million), RMB153 million (equivalent to HK\$147 million) and RMB192 million (equivalent to HK\$184 million), respectively.

The caps referred to above are determined with reference to:

- (a) the sales amounts of the Company's of petrochemical products in the past. For the three years ended 31 December 2004, the sales of the Company's petrochemical products amounted to RMB1,947 million, RMB3,068 million and RMB6,339 million, respectively;
- (b) the Company's estimate of the increase in the overall demand for petrochemical products in the PRC;
- (c) the Company's estimate of its business growth; and
- (d) the Company's estimate of the prevailing market percentage commission of the agency sales of petrochemical products.

Additionally, in 2004 the Company's comprehensive processing capacity was 16 million tpa. Since 2004, the Company has commenced the 20 million tpa refining capacity expansion project. In April 2005, the Company completed the construction and commenced operation of a 1 million tpa delayed coking unit, which led to an increase in comprehensive processing capacity to 18.5 million tpa. It is expected that by the end of 2006, the Company will complete construction and commence operation of a 1.5 million tpa hydrocracking unit and related auxiliary facilities, and will increase its comprehensive processing capacity to 20 million tpa. The completion of the new projects will significantly increase the production capacity of the Company. Accordingly, the Company expects its sales through its agents will increase as a result of the Company's enlarged production capacity.

As such, the Company expects that the commissions payable to Sinopec Group Company and its associates in relation to agency sales of the Company's petrochemical products will increase in 2005, 2006 and 2007. Taking into account these factors, the Company arrives at the caps above.

2.3.4 Construction and Overhaul of Production or Other Facilities Services

Background: Since the Company's initial public offer on 15 November 1994, the Company has from time to time obtained in the ordinary and usual course construction and overhaul services from Sinopec Group Company and its associates, in order to construct and overhaul its production or other facilities. The construction and overhaul also requires the purchase of equipment from Sinopec Group Company and its associates. The table below sets forth the historical figures of the total construction and overhaul fees the Company paid to Sinopec Group Company's associates for each of the three years ended 31 December 2004:

	Historical Figures for the year ended 31 December		
	2002 <i>(RMB million)</i>	2003 <i>(RMB million)</i>	2004 <i>(RMB million)</i>
Construction fee expenses	167	347	384
Purchase of equipment and related service fee charge	<u>216</u>	<u>831</u>	<u>404</u>
	<u><u>383</u></u>	<u><u>1,178</u></u>	<u><u>788</u></u>

Source: Annual reports of the Company for 2003 and 2004.

The Company proposes to enter into the Comprehensive Services Framework Agreement to continue to obtain construction and overhaul services (including equipment purchase and related services) from Sinopec Group Company and its associates for the three years ending 31 December 2007.

Reasons for such transactions: Major specialist teams on petrochemical construction and overhaul services are concentrated in Sinopec Group Company and its associates. Using these teams allows the Company to obtain stable, reliable and high-quality services for its construction and overhaul of production and other facilities.

By purchasing equipment through the associates of Sinopec Group Company, the Company can share their professional service network and obtain a better bargaining position through group purchase. The Company believes that this will ensure the Company to obtain reliable equipment purchase and related services at stable prices, whereby reducing the total cost of constructing and overhauling production or other facilities.

Pricing: Pursuant to the Comprehensive Services Framework Agreement, the fees payable to Sinopec Group Company and its associates in relation to the provision of construction and overhaul services (including equipment purchase) are priced as follows:

- (a) if there are applicable State (central and local governments) tariffs, the pricing of the construction and overhaul shall be bound by the State tariffs; or
- (b) if there are no State tariffs, but there are applicable State guided prices, the pricing of the construction and overhaul shall be bound by the State guided prices; or
- (c) if there are no applicable State tariffs or State guided prices, the pricing of construction and overhaul shall be determined in accordance with the prevailing market price (including any bidding price); or
- (d) if none of the above applies, the Company's construction and overhaul pricing shall be determined on a cost plus basis. The margin shall be fixed at a rate not exceeding 6%.

The Company will settle the service fees by way of cash payments.

Caps: For the three years ending 31 December 2007, the annual fees payable to Sinopec Group Company and its associates in relation to the provision of construction and overhaul services (including equipment purchase) shall not, in aggregate, exceed the caps of RMB3.1 billion (equivalent to HK\$2.9 billion), RMB12.2 billion (equivalent to HK\$11.6 billion) and RMB13.4 billion (equivalent to HK\$12.9 billion), respectively.

The caps referred to above are determined with reference to:

- (a) the previous transactions conducted and transaction amounts in respect of provision of construction and overhaul services by Sinopec Group Company and its associates;
- (b) the Company's estimate of the need of construction and overhaul services for the Company's existing and future development; and
- (c) the Company's estimate of the increase in the market price of construction and overhaul services.

Contracts on major construction projects for the 2005–2007 period include: (a) the Company will invest from 2005 to 2007 a sum of RMB4.1 billion to complete the 20 million tpa refinery capacity expansion project; (b) from 2005 onwards, the Company will commence the 1 million tpa ethylene project with a total investment estimated at RMB21.5 billion; and (c) the major overhaul in 2006 and scattered maintenance projects to be carried annually is estimated to have annual transaction values of approximately RMB500 million. In light of the possibility of a certain degree of increase in equipment and material prices when actual investment takes place, and in light of the possibility that certain projects may be carried out earlier or later than the schedule due to adjustments made to the actual investment in each year in accordance with

market situation and project progress, the caps for 2006 and 2007 are determined by allowing a 10% rise on the estimated total investment for each of the years 2006 and 2007, plus of 20% of the caps for the previous year in the caps for the following year.

	Unit: RMB million		
	2005	2006	2007
20 million tpa refining capacity expansion project	1,600	1,500	1,000
1 million tpa ethylene project	1,000	8,500	8,500
Overhaul	<u>500</u>	<u>500</u>	<u>500</u>
Total for the year	<u>3,100</u>	<u>10,500</u>	<u>10,000</u>
Caps on the construction and overhaul services	3,100	12,170	13,434

2.3.5 Financial Services

Background: As mentioned above, the Company sells petroleum products to Sinopec Corp and its associates. Sinopec Corp and its associates make payment to the Company through Sinopec Finance Company Limited at which the Company has opened a settlement account. The Company earns interest on the outstanding balance of the settlement account prior to the funds being transferred to Company's accounts opened with commercial banks. Sinopec Finance Company Limited is a non-bank finance company approved and regulated by the People's Bank of China ("PBOC") and the China Banking Regulatory Commission ("CBRC"), and is an associate of Sinopec Group Company.

The table below sets forth the historical figures of the aggregate balance of the Company's settlement account with Sinopec Finance Company and net interest income for each of the three years ended 31 December 2004:

	Historical Figures for the year ended 31 December		
	2002	2003	2004
	<i>(RMB million)</i>	<i>(RMB million)</i>	<i>(RMB million)</i>
Settlement account balance	419	669	1,627
Net interest income	1	0.7	1.5

Source: Annual reports of the Company for 2003 and 2004.

The settlement account balance should not be treated deposits with Sinopec Finance Company as they are proceeds from sales to Sinopec Corp and its associates and such proceeds normally stay in the settlement account for a couple of days before they are remitted to the Company's other bank accounts.

To better manage its cashflow position, the Company proposes to enter into the Comprehensive Services Framework Agreement to obtain the following financial services from Sinopec Finance Company for the three years ending 31 December 2007:

- payment collection services: the Company will use Sinopec Finance Company for collecting and making payments
- deposit account and related interest income: the Company will open a deposit account to replace the settlement account with Sinopec Finance Company

- loan services: the Company may borrow money from Sinopec Finance Company in time of capital shortage. Loans will be granted by Sinopec Finance Company on normal commercial terms and on an unsecured basis to the Company. As such, pursuant to rule 14A.65(4) of the Listing Rules, such loans will be considered to be financial assistance, exempt from reporting, announcement and independent shareholders' approval requirements.

Reasons for such transactions: The Company believes that having reliable and cooperative financial services are important to its business as the nature of the Company's business means that transactions often involve large sums of money. The ability to obtain timely financial services in respect of collecting and making payments, deposit and loan facilities is essential to the Company's management of its cashflow requirements, allowing the Company to earn higher return on excess cash and obtain necessary financial resources in time of capital shortage.

Pricing: Pursuant to the Comprehensive Services Framework Agreement, (i) the collection and payment services will be provided by Sinopec Finance Company free of charge; and (ii) Sinopec Finance Company shall accept deposits from the Company at interest rates not lower, and thus no less favourable, than the relevant standard rates set by the PBOC for similar deposits.

Sinopec Finance Company will settle the Company the deposit balance and interest income by way of cash payments.

Caps: For the three years ending 31 December 2007, the maximum of the deposit account (including related interest income) during the year with Sinopec Finance Company shall not, in aggregate, exceed the caps of RMB1,752 million (equivalent to HK\$1,683 million), RMB1,902 million (equivalent to HK\$1,827 million) and RMB1,952 million (equivalent to HK\$1,875 million), respectively.

The caps in respect of deposit services referred to above are determined with reference to:

- (a) the previous balances of the settlement account with Sinopec Finance Company Limited;
- (b) the Company's estimate of its business growth; and
- (c) the volume of the Company's sale with Sinopec Corp and its associates.

2.3.6 Insurance Services

Background: Since the Company's initial public offer on 15 November 1994, the Company has been, in the ordinary and usual course of its business, maintaining with a subsidiary of Sinopec Group Company insurance coverage for its property, facilities and inventory pursuant to the administrative measures of Sinopec Group Company. The funds received for security and protection measures from Sinopec Group Company were aimed at strengthening the security and protection measures or carrying out specific research projects.

The table below sets forth the historical figures of the aggregate insurance premium the Company paid to Sinopec Group Company and the funds received for security and protection measures for each of the three years ended 31 December 2004:

	Historical Figures for the year ended 31 December		
	2002 <i>(RMB million)</i>	2003 <i>(RMB million)</i>	2004 <i>(RMB million)</i>
Insurance premium expenses	41	45	54
Safety funds received	19	18	17

Source: Annual reports of the Company for 2003 and 2004.

The Company proposes to enter into the Comprehensive Services Framework Agreement to continue to obtain insurance services from Sinopec Group Company and its associates for the three years ending 31 December 2007.

Reasons for such transactions: Captive insurance has been widely adopted in the petrochemical industry. The Ministry of Finance of the PRC has already granted approval for Sinopec Group Company to provide captive insurance services to its affiliates. Owing to the size of the Company's operation, the Company finds it difficult to identify suitable insurance firms to provide insurance coverage for its property, facilities and inventory at a reasonable insurance premium in the PRC. The Company believes that maintaining a suitable insurance coverage over the Company's operation is important and minimises the Company's risk exposure. Obtaining insurance services from Sinopec Group Company allows the Company to secure essential insurance coverage over the Company's operation and is therefore beneficial to the Company.

Pricing: Pursuant to the Comprehensive Services Framework Agreement, the premium payable to Sinopec Group Company and its associates in relation to the provision of insurance services is priced as follows:

- (a) if there are applicable State (central and local governments) tariffs, the pricing of the premium shall be bound by the State tariffs; or
- (b) if there are no State tariffs, but there are applicable State guided prices, the pricing of the premium shall be bound by the State guided prices; or
- (c) if there are no applicable State tariffs or State guided prices, the pricing of the premium shall be determined in accordance with the prevailing market price (including any bidding price); or
- (d) if none of the above applies, the premium shall be determined on a cost plus basis. A reasonable margin shall be fixed in accordance with the actual situation at the time of transaction.

The Company will pay the premium by way of cash payments.

Caps: For the three years ending 31 December 2007, the annual insurance premium payable to Sinopec Group Company and its associates shall not, in aggregate, exceed the caps of RMB56.00 million (equivalent to HK\$53.80 million), RMB66.24 million (equivalent to HK\$63.41 million) and RMB82.56 million (equivalent to HK\$79.75 million), respectively. For the three years ending 31 December 2007, the annual safety funds received from Sinopec Group and its associates will not exceed RMB20 million (equivalent to HK\$19 million), RMB25 million (equivalent to HK\$24 million) and RMB33 million (equivalent to HK\$32 million).

The caps referred to above are determined with reference to:

- (a) the previous transactions conducted and transaction amounts in respect of provision of insurance services by Sinopec Group Company and its associates;
- (b) the Company's estimate of the growth in the value of its facilities in view of the Company's existing and future development;
- (c) the increase in the risk exposure of the Company; and
- (d) the Company's estimate of the increase in the market price of insurance services.

Additionally, in 2004 the Company's comprehensive processing capacity was 16 million tpa. Since 2004, the Company has commenced the 20 million tpa refining capacity expansion project. In April 2005, the Company completed the construction and commenced operation of a 1 million tpa delayed coking unit, which led to an increase in the comprehensive processing capacity to 18.5 million tpa. It is expected that by the end of 2006, the Company will complete construction

and commence operation of a 1.5 million tpa hydrocracking unit and related auxiliary facilities, and will increase its comprehensive processing capacity to 20 million tpa. Apart from the aforesaid refining projects, the Company will, from 2005 onwards, commence the 1 million tpa ethylene project; the ethylene properties and facilities will be covered by insurance. Accordingly, the Company expects its insurance premium for 2005, 2006 and 2007 will increase, so that sufficient insurance coverage is ensured for these new facilities.

2.3.7 Research and Development Services

Background: The Company, pursuant to the administrative measures applicable to all the companies under Sinopec Corp, participates in the research and development projects of Sinopec Corp. Since the Company's initial public offer on 15 November 1994, Sinopec Corp and its associates have been providing corresponding research and technical services to the Company's research and development. Meanwhile, the Company has been undertaking certain research and development projects of Sinopec Corp. In 2004, the Company, pursuant to Sinopec Corp's administrative measures, undertook research and development projects on its own. Accordingly, no paid or payable research and development fees to Sinopec Corp and its associates had incurred. However, the construction of the 1 million tpa ethylene project may require the Company to obtain research and development support from Sinopec Group Company and its associates. Research and development funds had been received from Sinopec Corp for carrying out research and development projects with extensive application value for refineries under Sinopec Corp.

The table below sets forth the historical figures of the aggregate research and development fees the Company paid to Sinopec Corp and its associates and research and development subventions received from Sinopec Corp for each of the three years ended 31 December 2004:

	Historical Figures for the year ended 31 December		
	2002 <i>(RMB million)</i>	2003 <i>(RMB million)</i>	2004 <i>(RMB million)</i>
Research and development fees	35	35	0
Research and development subventions received	5	8	0

Source: Annual reports of the Company for 2003 and 2004.

The Company proposes to enter into the Comprehensive Services Framework Agreement to continue to obtain research and development services from Sinopec Group Company, Sinopec Corp and their associates for the three years ending 31 December 2007.

Reasons for such transactions: Sinopec Corp and its associates as well as Sinopec Group Company have strong research and development capability in the industry. The Company has, since its initial public offer, been obtaining services from that institution. The transaction entered into helps promote the Company's technical advancement and product development.

Pricing: Pursuant to the Comprehensive Services Framework Agreement, the research and development fees payable to Sinopec Corp and its associates in relation to the provision of the research and development services are priced as follows:

- (a) if there are applicable State (central and local governments) tariffs, the research and development fees shall be bound by the State tariffs; or
- (b) if there are no State tariffs, but there are applicable State guided prices, the research and development fees shall be bound by the State guided prices; or

- (c) if there are no applicable State tariffs or State guided prices, the research and development fees shall be determined in accordance with the prevailing market price (including any bidding price); or
- (d) if none of the above applies, the research and development fees shall be determined on a cost plus basis.

The Company will settle the research and development fees by way of cash payments.

Caps: For the three years ending 31 December 2007, the annual research and development fees payable to Sinopec Corp and its associates in relation to the provision of research and development services shall not, in aggregate, exceed the caps of RMB35 million (equivalent to HK\$34 million), RMB35 million (equivalent to HK\$34 million) and RMB35 million (equivalent to HK\$34 million), respectively. The annual research and development subventions received from Sinopec Corp and its associates shall not, in aggregate, exceed the caps of RMB10 million (equivalent to HK\$10 million), RMB12 million (equivalent to HK\$12 million) and RMB18 million (equivalent to HK\$17 million), respectively.

The caps referred to above are determined with reference to:

- (a) the previous transactions conducted and transaction amounts in respect of the provision of research and development services by Sinopec Corp and its associates;
- (b) the Company's estimate of the need of research and development for its existing and future development;
- (c) the Company's estimate of the increase in the market price of research and development services.

2.3.8 Land Management and Leasing Services

Background: Sinopec Group Company, in a letter of undertaking to the Company, has granted the Company the first refusal right to purchase a piece of land, located adjacent to the Company and with an area of approximately 9.51 million square metres, for the Company's future expansion. Should the Company purchase the land from Sinopec Group Company in the future, it will constitute a connected transaction and will be subject to the regulations on connected transactions as stipulated in Chapter 14 of the Listing Rules. The Company currently leases the land for its operation. The waiver the Company obtained at the time of its initial public offer on 15 November 1994 does not include land management and leasing services. According to Rule 14.07 of the Listing Rules, in 2004 the relevant applicable ratios were below 0.1% for the land management and leasing services which constituted a Continuous Connected Transaction exempted from the requirements for reporting, announcement and approval of Independent Shareholders.

The table below sets forth the historical figures of the land management and leasing fees paid to Sinopec Group Company for each of the three years ended 31 December 2004:

	Historical Figures for the year ended 31 December		
	2002	2003	2004
	<i>(RMB million)</i>	<i>(RMB million)</i>	<i>(RMB million)</i>
Operating lease expense in respect of land	0	0	13

Source: Annual reports of the Company for 2003 and 2004.

The Company proposes to enter into the Comprehensive Services Framework Agreement to continue to obtain the land management and leasing services from Sinopec Group Company and its associates for the three years ending 31 December 2007.

Reasons for such transactions: Sinopec Group Company owns the land lot, which is adjacent to the Company and occupies an area of approximately 9.51 million square metres. The transaction allows the Company to use the site for construction usage at a relatively low cost.

Pricing: Pursuant to the Comprehensive Services Framework Agreement, the land management and leasing service fees payable to Sinopec Group Company and its associates are priced as follows:

- (a) if there are applicable State (central and local governments) tariffs, the land management and leasing fees shall be bound by the State tariffs; or
- (b) if there are no State tariffs, but there are applicable State guided prices, the land management and leasing fees shall be bound by the State guided prices; or
- (c) if there are no applicable State tariffs or State guided prices, the land management and leasing fees shall be determined in accordance with the prevailing market price (including any bidding price).

The Company will settle the service fees by way of cash payments.

Caps: For the three years ending 31 December 2007, the annual fees for land management and leasing services payable to Sinopec Group Company and its associates shall not, in aggregate, exceed the caps of RMB15 million (equivalent to HK\$14 million), RMB29 million (equivalent to HK\$28 million) and RMB36 million (equivalent to HK\$35 million), respectively.

The caps referred to above are determined with reference to:

- (a) the previous transactions conducted and transaction amounts in respect of the provision of land management and leasing services provided by Sinopec Group Company and its associates;
- (b) the Company's estimate of the need of land management and leasing services for its existing and future development;
- (c) the Company's estimate of the increase in the market price of land management and leasing services.

3. BOARD APPROVAL & APPROVAL OF INDEPENDENT SHAREHOLDERS

On 19 August 2005, the Board approved each of the Continuing Connected Transactions and the execution of the Framework Agreements.

The Board takes the view that the terms of the Continuing Connected Transactions and the Framework Agreements are fair and reasonable, on normal commercial terms and are entered into in the usual and ordinary course of business and that the Continuing Connected Transactions and the Framework Agreements are in the interests of the Company and its Shareholders as a whole. The view of the independent non-executive directors, as well as the advice of Partners Capital, will be stated in a circular to be dispatched to the Shareholders.

The purchases of raw materials, sales of products and services, construction and overhaul services and financial services whose relative applicable ratios exceed 2.5% constitute non-exempt Continuing Connected Transactions and subject to reporting, announcement and Independent Shareholders' approval. Agency sales of products, whose relevant applicable ratio exceed 0.1% but less than 2.5%, are also non-exempt Continuing Connected Transactions as they are aggregated in the same category

of sales of products and services. Insurance services, research and development services, as well as land management and leasing services, whose relevant applicable ratios exceed 0.1% but less than 2.5%, constitute Continuing Connected Transactions subject to reporting and announcement.

The Company will seek Independent Shareholders' approval of the Non-Exempt Continuing Connected Transactions and the terms of the Framework Agreements, as well as the Caps for the three years ending 31 December 2007 on the Non-Exempt Continuing Connected Transactions. In addition, the Company shall comply with the relevant requirements under Chapter 14A of the Listing Rules in relation to the Continuing Connected Transactions and the execution of the Framework Agreements.

An Independent Board Committee has been established to advise the Independent Shareholders as to the terms of the Non-Exempt Continuing Connected Transactions and the caps on the relevant Continuing Connected Transactions for the three years ending 31 December 2007.

4. DESPATCH OF SHAREHOLDERS' CIRCULAR

The Company has appointed Partners Capital as the independent financial adviser to advise the independent board committee in respect of the Non-Exempt Continuing Connected Transactions. A circular containing, amongst other things, details of the terms of the Continuing Connected Transactions and of the Framework Agreements, letters from the Independent Board Committee and from Partners Capital and a notice to Shareholders convening an extraordinary general meeting of the Company to approve the terms of the Non-Exempt Continuing Connected Transactions and the Framework Agreements and the caps for the three years ending 31 December 2007 on the relevant Continuing Connected Transactions will be despatched to the Shareholders as soon as practicable.

5. GENERAL INFORMATION

The Company is an integrated refining and chemical enterprise, processing crude oil into petroleum products, intermediate petrochemical products, asphalt, urea and petrochemical products such as PX and PP.

6. DEFINITIONS

In this announcement, unless the context otherwise requires, the following expressions have the following meanings:

“associate”	has the meaning given to it by the Listing Rules
“Board”	the board of directors of the Company
“Company”	Sinopec Zhenhai Refining & Chemical Company Limited (中國石化鎮海煉油化工股份有限公司), a joint stock limited company established in the PRC and listed on the Main Board of the Hong Kong Stock Exchange
“Comprehensive Services Framework Agreement”	the Framework Agreement dated 19 August 2005 entered into between the Company and Sinopec Group Company on the provision of certain services by Sinopec Group Company and its associates
“connected person”	has the meaning given to it by the Listing Rules
“Continuing Connected Transactions”	the on-going connected transactions listed in Section 2.1 and to be conducted by the Company and Sinopec Group Company, Sinopec Corp. and their associates

“Director(s)”	director(s) of the Company, including independent non-executive directors
“Framework Agreements”	Comprehensive Services Framework Agreement and Mutual Supply Framework Agreement
“HK\$”	Hong Kong dollars, the lawful currency of Hong Kong
“Hong Kong”	Hong Kong Special Administrative Region of the PRC
“Hong Kong Stock Exchange”	The Stock Exchange of Hong Kong Limited
“Independent Board Committee”	the committee of independent non-executive Directors, consisting of Qiu Yun, Sun Yongsen, Cen Kefa and Li Linghong, formed to advise the Independent Shareholders in respect of the terms of the Non-Exempt Continuing Connected Transactions and the caps for the three years ending 31 December 2007 on the relevant Continuing Connected Transactions
“Independent Shareholders”	shareholders other than Sinopec Corp and its associates
“Listing Rules”	the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited
“Mutual Supply Framework Agreement”	the Framework Agreement dated 19 August 2005 entered into between the Company and Sinopec Corp on the purchases and sales of certain raw materials, petroleum products and petrochemical products and services
“Non-Exempt Continuing Connected Transactions”	the on-going connected transactions (1), (2), (3), (4) and (5) listed in Section 2.1 and to be conducted by the Company and Sinopec Group Company, Sinopec Corp. and their associates
“Partners Capital”	Partners Capital International Limited, a licensed corporation to carry on types 1 and 6 regulated activities (dealing in securities and advising on corporate finance) under the Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong) and the independent financial adviser to the Independent Board Committee in respect of the Non-Exempt Continuing Connected Transactions
“PRC”	the People’s Republic of China
“PX”	paraxylene
“RMB”	Renminbi, the lawful currency of the PRC
“SECCO”	Shanghai SECCO Petrochemical Company Limited (上海賽科石油化工有限公司), a limited liability company incorporated in Shanghai
“Shareholders”	the shareholders of the Company

“Sinopec Corp”	China Petroleum & Chemical Corporation (中國石油化工股份有限公司), a joint stock limited company established in the PRC and listed on the Main Board of the Hong Kong Stock Exchange as well as in New York, London and Shanghai
“Sinopec Group Company”	China Petrochemical Corporation (中國石油化工集團公司), a wholly State-owned company established in the PRC
“tpa”	tonnes per annum
“Yizheng”	Sinopec Yizheng Chemical Fibre Company Limited (中國石化儀征化纖股份有限公司), a joint stock limited company incorporated in the PRC whose H shares are listed on the Hong Kong Stock Exchange and listed A shares are traded on the Shanghai Stock Exchange

Note: Solely for reference purpose, this announcement contains translations of certain RMB amounts into HK\$ at the rate of RMB1.04 to HK\$1.00. It should not be construed that these translations are representations that RMB amounts could actually be converted into any HK\$ at the rates indicated or at all.

As at the date of this announcement, the executive directors of the Company are Sun Weijun, Zhan Juping, Xu Liqiao, Sun Jianli and Yu Renming; the non-executive directors of the Company are Wang Lisheng and Hu Weiqing, and the independent non-executive directors of the Company are Sun Yongsen, Cen Kefa, Li Linghong and Qiu Yun.

By Order of the Board
Su Dewen
Company Secretary

26 August 2005, Ningbo, the PRC

Please also refer to the published version of this announcement in (South China Morning Post)