

# NOTES ON THE FINANCIAL STATEMENTS

for the year ended 31 December 2005

## 1 STATUS OF THE COMPANY

China Petroleum & Chemical Corporation (the “Company”) was established on 25 February 2000 as a joint stock limited company.

According to the State Council’s approval to the “Preliminary Plan for the Reorganisation of China Petrochemical Corporation” (the “Reorganisation”), the Company was established by China Petrochemical Corporation (“Sinopec Group Company”), which transferred its core businesses together with the related assets and liabilities at 30 September 1999 to the Company. Such assets and liabilities had been valued jointly by China United Assets Appraisal Corporation, Beijing Zhong Zheng Appraisal Company, CIECC Assets Appraisal Corporation and Zhong Fa International Properties Valuation Corporation (“registered valuers”). The net asset value was determined at RMB 98,249,084,000. The valuation was reviewed and approved by the Ministry of Finance (the “MOF”) (Cai Ping Zi [2000] No. 20 “Comments on the Review of the Valuation Regarding the Formation of a Joint Stock Limited Company by China Petrochemical Corporation”).

In addition, pursuant to the notice Cai Guan Zi [2000] No. 34 “Reply to the Issue Regarding Management of State-Owned Equity by China Petroleum and Chemical Corporation” issued by the MOF, 68.8 billion domestic state-owned shares with a par value of RMB 1.00 each were issued to Sinopec Group Company, the amount of which is equivalent to 70% of the above net asset value transferred from Sinopec Group Company to the Company in connection with the Reorganisation.

Pursuant to the notice Guo Jing Mao Qi Gai [2000] No. 154 “Reply on the Formation of China Petroleum and Chemical Corporation”, the Company obtained the approval from the State Economic and Trade Commission on 21 February 2000 for the formation of a joint stock limited company.

The Company took over the exploration, development and production of crude oil and natural gas, refining, chemicals and related sales and marketing business of Sinopec Group Company after the establishment of the Company.

Pursuant to the resolution passed at the Extraordinary General Meeting held on 24 August 2001, the Company acquired the entire equity interest of Sinopec National Star Petroleum Company (“Sinopec National Star”) from Sinopec Group Company for a consideration of RMB 6.45 billion.

Pursuant to the resolution passed at the Board of Directors’ meeting held on 28 October 2003, the Company acquired the principal assets and associated liabilities related to the 380 kiloton ethylene production and distribution equipment from Sinopec Group Maoming Petrochemical Company (“Sinopec Maoming”), for a consideration of RMB 3.3 billion (hereinafter referred to as the “Acquisition of Ethylene Assets”).

Pursuant to the resolution passed at the Board of Directors’ meeting held on 29 December 2003, the Company acquired the entire operating assets and liabilities of Tahe Oilfield Petrochemical Factory (“Tahe Petrochemical”) and Xi’an Petrochemical Main Factory (“Xi’an Petrochemical”) from Sinopec Group Company, for considerations of RMB 0.14 billion and RMB 0.22 billion, respectively (hereinafter referred to as the “Acquisition of Refining Assets”).

Pursuant to the resolutions passed at the Extraordinary General Meeting held on 21 December 2004, the Company acquired certain operating assets and associated liabilities of refining, petrochemicals, catalysts and gas stations (the “Acquisition of Acquired Assets”) from Sinopec Group Company for a consideration of RMB 5.36 billion. In connection with these acquisitions, the Group disposed of certain assets and liabilities related to its oilfield downhole operation (the “Disposal of Downhole Assets”) to Sinopec Group Company for a consideration receivable of RMB 1.71 billion, resulting in a net consideration of RMB 3.65 billion payable to Sinopec Group Company.

## 2 SIGNIFICANT ACCOUNTING POLICIES

The significant accounting policies adopted by the Company and its subsidiaries (“the Group”) are in conformity with the Accounting Standards for Business Enterprises and “Accounting Regulations for Business Enterprises” and other relevant regulations issued by the Ministry of Finance of the PRC.

### (a) Accounting year

The accounting year of the Group is from 1 January to 31 December.

### (b) Basis of consolidation

The Group prepared the consolidated financial statements according to “Accounting Regulations for Business Enterprises” and Cai Kuai Zi [1995] No.11 “Provisional regulations on consolidated financial statements” issued by the MOF.

The consolidated financial statements include the financial statements of the Company and all of its principal subsidiaries. A subsidiary is a company held by the Company directly or indirectly, of more than 50% (excluding 50%) of the equity interest, or the Company holds less than 50% of the equity interest of a company but has effective controlling power. The consolidated income statement of the Company only includes the results of the subsidiaries during the period when the Company holds more than 50% of the equity interests or holds less than 50% of equity interest but has effective controlling power. The effect of minority interests on equity and profit/loss attributable to minority shareholders are separately shown in the consolidated financial statements. For those subsidiaries whose assets and results of operation are not significant and have no significant effect on the Group’s consolidated financial statements, the Company does not consolidate these subsidiaries, but accounts for under the equity method in the long-term equity investments.

Where the accounting policies adopted by the subsidiaries are different from the policies adopted by the Company, the financial statements of the subsidiaries have been adjusted in accordance with the accounting policies adopted by the Company on consolidation. All significant inter-company balances and transactions, and any unrealised gains arising from inter-company transactions, have been eliminated on consolidation.

For those jointly controlled entities which the Company has joint control with other investors under contractual arrangement, the Company consolidates their assets, liabilities, revenues, costs and expenses based on the proportionate consolidation method according to its percentage of holding of equity interest in those entities in the consolidated financial statements.

### (c) Basis of preparation and measurement basis

The financial statements of the Group have been prepared on an accrual basis under the historical costs convention, unless otherwise stated.

**2 SIGNIFICANT ACCOUNTING POLICIES** (Continued)

**(d) Reporting currency and translation of foreign currencies**

The Group's reporting currency is Renminbi.

Foreign currency transactions during the year are translated into Renminbi at exchange rates quoted by the People's Bank of China ("PBOC rates") prevailing on the transaction dates. Foreign currency monetary assets and liabilities are translated into Renminbi at the PBOC rates at the balance sheet date. Exchange gains and losses on foreign currency translation, except for those directly relating to the construction of fixed assets (see note 2(i)), are dealt with in the income statement.

The results of overseas subsidiaries are translated into Renminbi at the annual average PBOC rates. The balance sheet items are translated into Renminbi at the PBOC rates at the balance sheet date. The resulting exchange gains or losses are accounted for as foreign currency exchange differences.

**(e) Cash equivalents**

Cash equivalents held by the Group are short-term and highly liquid investments which are readily convertible into known amounts of cash and are subject to an insignificant risk of change in value.

**(f) Allowance for doubtful accounts**

Trade accounts receivable showing signs of uncollectibility are identified individually and allowance is then made based on the probability of being uncollectible. In respect of trade accounts receivable showing no sign of uncollectibility, allowance is made with reference to the ageing analysis and management's estimation based on past experience. Allowances for other receivables are determined based on the nature and corresponding collectibility. Specific approval from management is required for allowances made in respect of significant doubtful accounts.

**(g) Inventories**

Inventories, other than spare parts and consumables, are stated at the lower of cost and net realisable value.

Inventories are measured at their actual cost upon acquisition. The cost of inventories is calculated using the weighted average method. In addition to the purchase cost of raw material, work in progress and finished goods include direct labour and an appropriate allocation of manufacturing overheads.

Any excess of the cost over the net realisable value of each item of inventories is recognised as a provision for diminution in the value of inventories. Net realisable value is the estimated selling price in the normal course of business less the estimated costs to completion and the estimated expenses and related taxes to make the sale.

Spare parts and consumables are stated at cost less any provision for obsolescence. Consumables are expensed when being consumed.

Inventories are recorded by perpetual method.

**(h) Long-term equity investments**

Where the Group has the power to control, jointly control or exercise significant influence over an investee enterprise, the investment is accounted for under the equity method whereby the investment is initially recorded at cost and adjusted thereafter for any post acquisition change in the Group's share of the shareholders' funds in the investee enterprise.

Equity investment difference, which is the difference between the initial investment cost and the Group's share of shareholders' funds of the investee enterprise, is accounted for as follows:

- Any excess of the initial investment cost over the share of shareholders' funds of the investee enterprise is amortised on a straight-line basis. The amortisation period is determined according to the investment period as stipulated in the relevant agreement, or not more than 10 years if the investment period is not specified in the agreement. The unamortised balance is included in long-term equity investments at the year end.
- Any shortfall of the initial investment cost over the share of shareholders' funds of the investee is recognised in capital reserve – reserve for equity investment acquired after the issuance of Cai Kuai [2003] No.10 "Questions and answers on implementing Accounting Regulations for Business Enterprises and related accounting standards (II)". If the investment was acquired before the issuance of Cai Kuai [2003] No.10 "Questions and answers on implementing Accounting Regulations for Business Enterprises and related accounting standards (II)", such shortfall is amortised on a straight-line basis over the investment period as stipulated in the relevant agreement, or 10 years if the investment period is not specified in the agreement. The unamortised balance is included in long-term equity investments at the year end.

Where the Group does not control, jointly control or exercise significant influence over an investee enterprise, the investment is accounted for under the cost method, stating it at the initial investment cost. Investment income is recognised when the investee enterprise declares a cash dividend or distributes profits.

Upon the disposal or transfer of long-term equity investments, the difference between the proceeds received and the carrying amount of the investments is recognised in the income statement.

The Group makes provision for impairment losses on long-term equity investments (see note 2(w)).

**2 SIGNIFICANT ACCOUNTING POLICIES** (Continued)

**(i) Fixed assets and construction in progress**

Fixed assets represent the assets held by the Group for use in the production of goods and for administrative purposes with useful life over 1 year and comparatively high unit value.

Fixed assets are stated in the balance sheet at cost or revalued amount less accumulated depreciation and impairment losses (see note 2(w)). Construction in progress is stated in the balance sheet at cost or revalued amount less impairment losses (see note 2(w)). The revalued amount represents the amount of assets, which is determined by revaluation carried out in accordance with the relevant rules and regulations.

All direct and indirect costs related to the purchase or construction of fixed assets, incurred before the assets are ready for their intended uses, are capitalised as construction in progress. Those costs include borrowing costs (including foreign exchange differences arising from the loan principal and the related interest) on specific borrowings for the construction of the fixed assets during the construction period.

Construction in progress is transferred to fixed assets when the asset is ready for its intended use. No depreciation is provided against construction in progress.

Fixed assets of the Group are depreciated using the straight-line method over their estimated useful lives. The estimated useful lives and the estimated rate of residual values adopted for respective classes of fixed assets are as follows:

	Estimated useful lives	Estimated rate of residual value
Land and buildings	15-45 years	3%-5%
Oil and gas properties	10-14 years	0%-3%
Plant, machinery, equipment, vehicles and others	4-18 years	3%
Oil depots and storage tanks	8-14 years	3%
Service stations	25 years	3%-5%

**(j) Oil and gas properties**

Costs of development wells and the related support equipment are capitalised. The cost of exploratory wells is initially capitalised as construction in progress pending determination of whether the well has found proved reserves. Exploratory well costs are charged to expenses upon the determination that the well has not found proved reserves. However, in the absence of a determination of the discovery of proved reserves, exploratory well costs are not carried as an asset for more than one year following completion of drilling. If, after one year has passed, a determination of the discovery of proved reserves cannot be made, the exploratory well costs are impaired and charged to expense. All other exploration costs, including geological and geophysical costs, are charged to the income statement in the period as incurred.

**(k) Intangible assets**

Intangible assets are stated in the balance sheet at cost or revalued amount less accumulated amortisation and provision for impairment losses (see note 2(w)). Amortisation is provided on a straight-line basis. The amortisation period is the shorter of the contracted beneficial period and the effective period stipulated by law. Amortisation is provided over 10 years if it is not specified in contracts or stipulated by law.

Intangible assets include exploration and production right. Exploration and production right are amortised on a straight-line basis over the average period of the production rights of the related oil fields.

**(l) Pre-operating expenditures**

Except for the acquisition and constructions of fixed assets, all expenses incurred during the start-up period are aggregated in long-term deferred expenses and then fully charged to the income statement in the month operations commence.

**(m) Debentures payable**

Debentures payable is stated in the balance sheet based on the proceeds received upon issuance. Interest expenses are calculated based on actual interest rate.

**(n) Revenue recognition**

Revenues associated with the sale of crude oil, natural gas, petroleum and chemical products and all other items are recorded when the customer accepts the goods and the significant risks and rewards of ownership and title have been transferred to the buyer. No revenue is recognised if there are significant uncertainties regarding recovery of the consideration due, the possible return of goods, or when the amount of revenue and the costs incurred or to be incurred in respect of the transaction cannot be measured reliably.

Revenue from the rendering of services only involving in one accounting year is recognised in the income statement upon completion. If a transaction lasts more than one accounting years, when the outcome of the transaction involving the rendering of services can be estimated reliably, revenue from the rendering of services is recognised in the income statement in proportion to the stage of completion of the transaction based on the progress of work performed; or when the outcome of the transaction involving the rendering of services cannot be estimated reliably, revenues recognised only to the extent that costs incurred are expected to be recoverable.

Interest income is recognised on a time proportion basis according to the principal outstanding and the applicable rate.

**2 SIGNIFICANT ACCOUNTING POLICIES** (Continued)

**(o) Income tax**

Income tax is recognised using the tax effect accounting method. Income tax for the year comprises current tax paid and payable and movement of deferred tax assets and liabilities.

Current tax is calculated at the applicable tax rate on taxable income.

Deferred tax is provided using the liability method, for timing differences between accounting profit before tax and the taxable income arising from the differences in the tax and accounting treatment of income and expenses or loss.

The tax value of losses expected to be available for utilisation against future taxable income is set off against the deferred tax liability within the same legal tax unit and jurisdiction. A valuation allowance is provided for the tax value of losses to reduce the deferred tax asset to the amount that is more likely than not to be realised through future taxable income.

**(p) Borrowing costs**

Borrowing costs incurred on specific borrowings for the construction of fixed assets are capitalised into the cost of the fixed assets during the construction period until the fixed assets are ready for their intended uses.

Except for the above, other borrowing costs are recognised as financial expenses in the income statement when incurred.

**(q) Repairs and maintenance expenses**

Repairs and maintenance expenses are recognised in the income statement when incurred.

**(r) Environmental expenditures**

Environmental expenditures relating to circumstances arising as a result of the current or past businesses are recognised in the income statement when incurred.

**(s) Research and development costs**

Research and development costs are recognised in the income statement when incurred.

**(t) Operating leases**

Operating lease payments are charged as expenses on a straight-line basis over the period of the respective leases.

**(u) Dividends**

Dividends appropriated to shareholders are recognised in the income statement and profit appropriation statement when approved. Dividends proposed or approved after the balance sheet date but before the date on which the financial statements are authorised for issue are separately disclosed under shareholders' funds in the balance sheet.

**(v) Retirement benefits**

Pursuant to the relevant laws and regulations in the PRC, the Group has joined a defined contribution retirement plan for the employees arranged by a governmental organisation. The Group makes contributions to the retirement scheme at the applicable rate(s) based on the employees' salaries. The contributions are charged to the income statement on an accrual basis. After the payment of the contributions under the retirement plan, the Group does not have any other obligations in this respect.

**(w) Provision for impairment**

The carrying amounts of assets (including long-term equity investments, fixed assets, construction in progress, intangible assets and other assets) are reviewed regularly to determine whether their recoverable amounts have declined below their carrying amounts. Assets are tested for impairment whenever events or changes in circumstances indicate that their recorded carrying amounts may not be recoverable. When such a decline has occurred, the carrying amount is reduced to the recoverable amount. The amount by which the carrying amount is reduced is the impairment loss.

The recoverable amount is the greater of the net selling price and the present value of the estimated future cash flows arising from the continuous use of the asset and from the disposal of the asset at the end of its useful life.

Provision for impairment loss is calculated on an item by item basis and recognised as an expense in the income statement. However, when a deficit between the initial investment cost and the Group's share of the shareholders' funds of the investee enterprise has been credited to the capital reserve, any impairment losses for long-term equity investment are firstly set off against the difference initially recognised in the capital reserve relating to the investment and any excess impairment losses are then recognised in the income statement.

If there is an indication that there has been a change in the estimates used to determine the recoverable amount and as a result the estimated recoverable amount is greater than the carrying amount of the asset, the impairment loss recognised in prior years is reversed. Reversals of impairment losses are recognised in the income statement. Impairment losses are reversed to the extent of the asset's carrying amount that would have been determined had no impairment loss been recognised in prior years. In respect of the reversal of an impairment loss for a long-term equity investment, the reversal starts with the impairment losses that had previously been recognised in the income statement and then the impairment losses that had been charged to capital reserve.

**(x) Related parties**

If the Group has the power, directly or indirectly, to control, jointly control or exercise significant influence over another party, or vice versa, or where the Group and one or more parties are subject to common control from another party, they are considered to be related parties. Related parties may be individuals or enterprises.

## NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2005

### 2 SIGNIFICANT ACCOUNTING POLICIES (Continued)

#### (y) Provisions and contingent liabilities

Provisions are recognised when the Group has a present obligation as a result of a past event, it is probable that an outflow of economic benefits will be required to settle the obligations and a reliable estimate can be made.

Where it is not probable that the settlement of the above obligation will cause an outflow of economic benefits, or the amount of the outflow cannot be estimated reliably, the obligation is disclosed as a contingent liability.

### 3 TAXATION

Major taxes applicable to the Group and the Company comprise income tax, consumption tax, resources tax and value added tax.

Income tax rate is 33% and that of certain branches and subsidiaries is 15%.

Consumption tax is levied on gasoline and diesel at a rate of RMB 277.6 per tonne and RMB 117.6 per tonne respectively.

For the period from 1 January 2005 to 30 June 2005, resources tax is levied on crude oil and natural gas at rates ranging from RMB 8 per tonne to RMB 30 per tonne and RMB 2 to RMB 15 per 1000 cubic metres respectively. For the period from 1 July 2005 to 31 December 2005, resources tax is levied on crude oil and natural gas at rates ranging from RMB 14 per tonne to RMB 30 per tonne and RMB 7 to RMB 15 per 1000 cubic metres respectively.

Value added tax rate for liquefied petroleum gas, natural gas and certain agricultural products is 13% and that for other products is 17%.

The branches, subsidiaries and jointly controlled entities granted with tax concession are set out below:

Name of branches, subsidiaries and jointly controlled entities	Preferential tax rate	Reasons for granting concession
Sinopec National Star Xinan Branch	15%	Tax preferential policy in the western part of China
Sinopec National Star Xibei Branch	15%	Tax preferential policy in the western part of China
Sinopec Southern Exploration Branch	15%	Tax preferential policy in the western part of China
Sinopec Shanghai Petrochemical Company Limited	15%	The first batch of joint stock enterprise which successfully got listed overseas
Sinopec Yizheng Chemical Fibre Company Limited	15%	The first batch of joint stock enterprise which successfully got listed overseas
Sinopec Yangzi Petrochemical Company Limited	15%	High technology enterprise
Sinopec Zhongyuan Petroleum Company Limited	15%	High technology enterprise
Petro-CyberWorks Information Technology Company Limited	15%	High technology enterprise
Shanghai Secco Petrochemical Company Limited	2-year exemption and 3-year 50% reduction	Foreign investment enterprise
BASF-YPC Company Limited	2-year exemption and 3-year 50% reduction	Foreign investment enterprise

### 4 CASH AT BANK AND IN HAND

#### The Group

	2005			2004		
	Original currency millions	Exchange rates	RMB millions	Original currency millions	Exchange rates	RMB millions
Cash in hand						
Renminbi			207			115
Cash at bank						
Renminbi			9,229			12,621
US Dollars	76	8.0702	616	96	8.2765	795
Hong Kong Dollars	63	1.0403	66	47	1.0637	50
Japanese Yen	277	0.0687	19	220	0.0797	18
Euro	2	9.5797	21	1	11.2627	10
			<b>10,158</b>			<b>13,609</b>
Deposits at related parties						
Renminbi			4,588			4,657
US Dollars	—	8.0702	1	2	8.2765	14
<b>Total cash at bank and in hand</b>			<b>14,747</b>			<b>18,280</b>

## NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2005

### 4 CASH AT BANK AND IN HAND (Continued)

#### The Company

	2005			2004		
	Original currency millions	Exchange rates	RMB millions	Original currency millions	Exchange rates	RMB millions
Cash in hand						
Renminbi			12			107
Cash at bank						
Renminbi			3,075			4,892
US Dollars	1	8.0702	10	1	8.2765	6
			<b>3,097</b>			<b>5,005</b>
Deposits at related parties						
Renminbi			2,026			1,280
US Dollars	—	8.0702	1	2	8.2765	14
<b>Total cash at bank and in hand</b>			<b>5,124</b>			<b>6,299</b>

Deposits at related parties represent deposits placed at Sinopec Finance Company Limited. Deposits interest is calculated based on market rate.

### 5 BILLS RECEIVABLE

Bills receivable represents mainly the bills of acceptance issued by banks for sales of goods and products.

### 6 TRADE ACCOUNTS RECEIVABLE

	The Group		The Company	
	2005 RMB millions	2004 RMB millions	2005 RMB millions	2004 RMB millions
Amounts due from subsidiaries	—	—	6,252	5,026
Amounts due from Sinopec Group Company and fellow subsidiaries	3,049	2,349	518	858
Amounts due from associates	572	89	10	19
Amounts due from jointly controlled entities	505	—	229	—
Others	13,546	10,989	4,136	5,179
	<b>17,672</b>	<b>13,427</b>	<b>11,145</b>	<b>11,082</b>
Less: Allowance for doubtful accounts	3,140	3,671	2,319	2,837
<b>Total</b>	<b>14,532</b>	<b>9,756</b>	<b>8,826</b>	<b>8,245</b>

Allowance for doubtful accounts is analysed as follows:

	The Group		The Company	
	2005 RMB millions	2004 RMB millions	2005 RMB millions	2004 RMB millions
Balance at 1 January	3,671	3,185	2,837	2,299
Provision for the year	328	931	186	708
Written back for the year	(503)	(85)	(424)	(37)
Written off for the year	(356)	(360)	(280)	(133)
<b>Balance at 31 December</b>	<b>3,140</b>	<b>3,671</b>	<b>2,319</b>	<b>2,837</b>

## NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2005

### 6 TRADE ACCOUNTS RECEIVABLE (Continued)

Ageing analysis on trade accounts receivable is as follows:

	The Group							
	2005				2004			
	Amount RMB millions	%	Allowance RMB millions	%	Amount RMB millions	%	Allowance RMB millions	%
Within one year	14,320	81.0	49	0.3	9,546	71.1	390	4.1
Between one and two years	279	1.6	101	36.2	308	2.3	83	26.9
Between two and three years	158	0.9	115	72.8	527	3.9	361	68.5
Over three years	2,915	16.5	2,875	98.6	3,046	22.7	2,837	93.1
<b>Total</b>	<b>17,672</b>	<b>100.0</b>	<b>3,140</b>		<b>13,427</b>	<b>100.0</b>	<b>3,671</b>	

	The Company							
	2005				2004			
	Amount RMB millions	%	Allowance RMB millions	%	Amount RMB millions	%	Allowance RMB millions	%
Within one year	8,721	78.1	45	0.5	8,103	73.1	275	3.4
Between one and two years	164	1.5	52	31.7	193	1.8	66	34.2
Between two and three years	95	0.9	70	73.7	334	3.0	251	75.1
Over three years	2,165	19.5	2,152	99.4	2,452	22.1	2,245	91.6
<b>Total</b>	<b>11,145</b>	<b>100.0</b>	<b>2,319</b>		<b>11,082</b>	<b>100.0</b>	<b>2,837</b>	

Major trade accounts receivable of the Group at 31 December 2005 are set out below:

Name of debtor	Balance RMB millions	Percentage on trade accounts receivable %
Guangdong Nanhua Petroleum Company Limited	921	5.2
Dongxing Oil Industry Limited	697	3.9
Sinopec Railway Oil Marketing Company Limited	330	1.9
SK Corporation	232	1.3
Sinochem Singapore Petroleum International Company Limited	216	1.2

Major trade accounts receivable of the Group at 31 December 2004 are set out below:

Name of debtor	Balance RMB millions	Percentage on trade accounts receivable %
Baling Petrochemical Yueyang Petrochemical Company	393	2.9
Qingdao Petrochemical Plant	379	2.8
Petrolimex Vietnam	311	2.3
Phibro GmbH	294	2.2
Maoming Petrochemical Shihua Company Limited	248	1.8

Except for the balances disclosed in Note 41, there is no amount due from shareholders who hold 5% or more voting right of the Company included in the balance of trade accounts receivable.

During the years ended 31 December 2005 and 2004, the Group and the Company had no individually significant trade accounts receivable been fully or substantially provided for.

During the years ended 31 December 2005 and 2004, the Group and the Company had no individually significant write off or recover of doubtful debts which had been fully or substantially provided for in prior years.

At 31 December 2005 and 2004, the Group and the Company had no individually significant trade accounts receivable that aged over three years.

## NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2005

### 7 OTHER RECEIVABLES

	The Group		The Company	
	2005	2004	2005	2004
	RMB millions	RMB millions	RMB millions	RMB millions
Amounts due from subsidiaries	—	—	1,740	11,004
Amounts due from Sinopec Group Company and fellow subsidiaries	3,059	6,135	2,708	5,616
Amounts due from associates	521	308	501	260
Others	11,419	9,515	7,855	6,168
	<b>14,999</b>	<b>15,958</b>	<b>12,804</b>	<b>23,048</b>
Less: Allowance for doubtful accounts	3,512	3,496	3,200	3,423
<b>Total</b>	<b>11,487</b>	<b>12,462</b>	<b>9,604</b>	<b>19,625</b>

Allowance for doubtful accounts is analysed as follows:

	The Group		The Company	
	2005	2004	2005	2004
	RMB millions	RMB millions	RMB millions	RMB millions
Balance at 1 January	3,496	2,348	3,423	1,967
Provision for the year	446	1,245	176	1,514
Written back for the year	(415)	(41)	(386)	(26)
Written off for the year	(15)	(56)	(13)	(32)
<b>Balance at 31 December</b>	<b>3,512</b>	<b>3,496</b>	<b>3,200</b>	<b>3,423</b>

Ageing analysis of other receivables is as follows:

	The Group							
	2005				2004			
	Amount RMB millions	%	Allowance RMB millions	%	Amount RMB millions	%	Allowance RMB millions	%
Within one year	9,167	61.1	15	0.2	8,577	53.8	14	0.2
Between one and two years	676	4.5	33	4.9	485	3.0	17	3.5
Between two and three years	447	3.0	338	75.6	3,549	22.2	430	12.1
Over three years	4,709	31.4	3,126	66.4	3,347	21.0	3,035	90.7
<b>Total</b>	<b>14,999</b>	<b>100.0</b>	<b>3,512</b>		<b>15,958</b>	<b>100.0</b>	<b>3,496</b>	

	The Company							
	2005				2004			
	Amount RMB millions	%	Allowance RMB millions	%	Amount RMB millions	%	Allowance RMB millions	%
Within one year	7,127	55.7	5	0.1	16,168	70.1	12	0.1
Between one and two years	491	3.8	19	3.9	923	4.0	592	64.1
Between two and three years	748	5.8	622	83.1	2,620	11.4	48	1.8
Over three years	4,438	34.7	2,554	57.5	3,337	14.5	2,771	83.0
<b>Total</b>	<b>12,804</b>	<b>100.0</b>	<b>3,200</b>		<b>23,048</b>	<b>100.0</b>	<b>3,423</b>	

Major other receivables of the Group at 31 December 2005 are set out below:

Name of debtor	Particulars	Balance RMB millions	Percentage on other receivables %
China Petrochemical Corporation	Current Account	1,507	10.0
Fujian Quanzhou Qu Finance Bureau	Current Account	375	2.5
Jinhuang Real Estate Company Limited	Current Account	208	1.4
Ningbo Taiyi Real Estate Company Limited	Current Account	192	1.3
Qingdao Qirun Petrochemical Company Limited	Current Account	162	1.0



## NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2005

### 7 OTHER RECEIVABLES (Continued)

Major other receivables of the Group at 31 December 2004 are set out below:

Name of debtor	Particulars	Percentage on	
		Balance	other receivables
		RMB millions	%
China Petrochemical Corporation	Current Account	2,502	15.7
Jinhuang Real Estate Company Limited	Current Account	219	1.4
China Ruilian Industrial Group Corporation	Current Account	184	1.2
Anhui Jinyu Highway Development Company Limited	Current Account	121	0.8
Anhui He Chao Wu Highway Company Limited	Current Account	107	0.7

Except for the balances disclosed in Note 41, there is no amount due from shareholders who hold 5% or more voting right of the Company included in the balance of other receivables.

During the years ended 31 December 2005 and 2004, the Group and the Company had no individually significant other receivables been fully or substantially provided for.

During the years ended 31 December 2005 and 2004, the Group and the Company had no individually significant write off or recover of doubtful debts which had been fully or substantially provided for in prior years.

At 31 December 2005 and 2004, the Group and the Company had no individually significant other receivables that aged over three years.

### 8 ADVANCE PAYMENTS

All advance payments are aged within one year.

Except for the balances disclosed in Note 41, there is no amount due from shareholders who hold 5% or more voting right of the Company included in the balance of advance payments.

### 9 INVENTORIES

	The Group		The Company	
	2005	2004	2005	2004
	RMB millions	RMB millions	RMB millions	RMB millions
Raw materials	53,350	32,581	25,471	14,544
Work in progress	9,422	8,341	4,659	3,605
Finished goods	23,163	20,804	17,980	15,163
Spare parts and consumables	3,893	3,098	2,061	1,033
	<b>89,828</b>	<b>64,824</b>	<b>50,171</b>	<b>34,345</b>
Less: Provision for diminution in value of inventories	892	906	309	394
	<b>88,936</b>	<b>63,918</b>	<b>49,862</b>	<b>33,951</b>

All of the above inventories are purchased or self-manufactured.

Provision for diminution in value of inventories is mainly against finished goods and spare parts.

Provision for diminution in value of inventories is analysed as follows:

	The Group		The Company	
	2005	2004	2005	2004
	RMB millions	RMB millions	RMB millions	RMB millions
Balance at 1 January	906	519	394	226
Provision for the year	262	621	64	314
Written back for the year	(180)	(188)	(81)	(124)
Written off	(96)	(46)	(68)	(22)
<b>Balance at 31 December</b>	<b>892</b>	<b>906</b>	<b>309</b>	<b>394</b>

The cost of inventories recognised as costs and expenses by the Group and the Company amounted to RMB 683,375 million (2004: RMB 473,724 million) and RMB 488,592 million (2004: RMB 343,269 million) for the year ended 31 December 2005, respectively.

## NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2005

### 10 LONG-TERM EQUITY INVESTMENTS

#### The Group

	Listed stock investment RMB millions	Unlisted stock and other equity investment RMB millions	Equity investment differences RMB millions	Provision for impairment losses RMB millions	Total RMB millions
Balance at 1 January 2005	790	12,589	383	(353)	13,409
Additions for the year	—	2,942	1,820	—	4,762
Share of profits less losses from investments accounted for under the equity method	81	754	—	—	835
Long-term equity investments accounted for as a jointly controlled entity	—	(3,516)	—	—	(3,516)
Dividends receivable/received	(48)	(407)	—	—	(455)
Disposals for the year	—	(715)	—	—	(715)
Amortisation for the year	—	—	(200)	—	(200)
Movement of provision for impairment losses	—	—	—	26	26
<b>Balance at 31 December 2005</b>	<b>823</b>	<b>11,647</b>	<b>2,003</b>	<b>(327)</b>	<b>14,146</b>

#### The Company

	Listed stock investment RMB millions	Unlisted stock and other equity investment RMB millions	Equity investment differences RMB millions	Provision for impairment losses RMB millions	Total RMB millions
Balance at 1 January 2005	49,731	74,235	400	(155)	124,211
Additions for the year	—	9,821	1,818	—	11,639
Reclassification	(6,856)	6,856	—	—	—
Share of profits less losses from investments accounted for under the equity method	8,371	26,444	—	—	34,815
Dividends receivable/received	(2,682)	(34,404)	—	—	(37,086)
Disposals for the year	—	(227)	—	—	(227)
Amortisation for the year	—	—	(201)	—	(201)
Movement of provision for impairment losses	—	—	—	52	52
<b>Balance at 31 December 2005</b>	<b>48,564</b>	<b>82,725</b>	<b>2,017</b>	<b>(103)</b>	<b>133,203</b>

Provision for impairment losses is analysed as follows:

	The Group		The Company	
	2005 RMB millions	2004 RMB millions	2005 RMB millions	2004 RMB millions
Balance at 1 January	353	271	155	160
Additions for the year	77	96	14	2
Written back for the year	(17)	(8)	—	(2)
Written off	(86)	(6)	(66)	(5)
<b>Balance at 31 December</b>	<b>327</b>	<b>353</b>	<b>103</b>	<b>155</b>

At 31 December 2005 and 2004, the Group and the Company had no individually significant long-term equity investments which had been provided for.

Other equity investments represent the Group's interests in PRC domiciled enterprises which are mainly engaged in non-oil and gas and chemical activities and operations. This includes non-consolidated investments which the Group has over 50% equity interest but the costs of investment are not significant or the Group has no control on the entities. Stock investments of the Company represent investments in subsidiaries, associates and jointly controlled entities. Details of the Company's principal subsidiaries are set out in Note 42.

## NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2005

### 10 LONG-TERM EQUITY INVESTMENTS (Continued)

At 31 December 2005, details of listed stock investment of the Group (associates) are as follows:

Name of investee enterprise	Type of equity interest	No. of shares millions	Percentage of equity interest held by the Group	Initial investment cost RMB millions	Balance at 1 January 2005 RMB millions	Shares of profits accounted for under the equity method RMB millions	Dividends receivable/ received RMB millions	Balance at 31 December 2005 RMB millions	Market price as at 31 December 2005*
									RMB millions
Sinopec Shengli Oil Field Dynamic Co Ltd	Legal person shares	96	26.33%	223	461	62	(29)	494	722
Sinopec Shandong Taishan Petroleum Co Ltd	Legal person shares	186	38.68%	124	329	19	(19)	329	547
					<b>790</b>	<b>81</b>	<b>(48)</b>	<b>823</b>	

\* Information of market price is sourced from Shenzhen Stock Exchange.

At 31 December 2005, details of principal unlisted stock and other equity investment of the Group (including associates) are as follows:

Name of investee enterprise	Initial investment cost RMB millions	Investment period	Percentage of equity interest held by the Group	Balance at 1 January 2005 RMB millions	Addition for the year RMB millions	Share of profits accounted for under the equity method RMB millions	Dividends receivable/ received RMB millions	Balance at 31 December 2005
								RMB millions
Sinopec Finance Company Limited (i) (ii)	1,205	—	40%	1,311	—	262	(56)	1,517
China Aviation Oil Supply Company Limited (ii)	1,102	—	29%	—	1,102	—	—	1,102
Shanghai Petroleum National Gas Corporation (i) (ii)	300	—	30%	912	—	241	(195)	958
Shanghai Chemical Industry Park Development Company Limited (ii)	608	30 years	38%	651	—	10	(2)	659
China Shipping & Sinopec Suppliers Company Limited (ii)	438	—	50%	468	—	41	—	509
Sinopec Changjiang Fuel Company Limited (ii)	190	20 years	50%	251	—	41	(39)	253
Hunan Highway Industrial Development Company Limited (i) (ii)	215	—	49%	218	—	5	(2)	221
Beijing International Trust and Investment Company Limited	200	—	8%	—	200	—	—	200
Zhejiang Express Petroleum Development Company Limited (i) (ii)	174	30 years	50%	—	174	3	—	177
China Gas Holdings Ltd	136	—	11%	136	—	—	—	136
Sinopec Railway Oil Marketing Company Limited (ii)	74	20 years	50%	110	24	40	(48)	126

(i) These entities are principal associates of the Company.

(ii) These entities are principal associates of the Group.

No provision for individually significant impairment losses or individually significant equity investment difference was made for the long-term equity investments as set out above.

At 31 December 2005, the Group's and the Company's proportion of the total investments to the net assets was 7% (2004: 7%) and 61% (2004: 66%), respectively.

At 31 December 2005, the Group's and the Company's equity investment differences represent mainly the equity investment difference resulting from the acquisition of the minority interests of Sinopec Beijing Yanhua Petrochemical Company Limited in 2005. The equity investment difference is amortised on a straight-line basis over 10 years. The balance at 31 December 2005 is RMB 1,041 million.

## NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2005

### 11 FIXED ASSETS

#### The Group – by segment

	Exploration and production RMB millions	Refining RMB millions	Marketing and distribution RMB millions	Chemicals RMB millions	Others RMB millions	Total RMB millions
<b>Cost/valuation:</b>						
At 1 January 2005	170,457	117,063	64,775	163,075	4,092	519,462
Addition for the year	151	172	934	307	150	1,714
Transferred from construction in progress	22,094	8,066	13,687	18,370	381	62,598
Proportionate share of a new jointly controlled entity	—	—	—	1,315	—	1,315
Reclassification	(157)	(432)	204	289	96	—
Disposals	(3,419)	(2,860)	(2,927)	(3,173)	(245)	(12,624)
<b>At 31 December 2005</b>	<b>189,126</b>	<b>122,009</b>	<b>76,673</b>	<b>180,183</b>	<b>4,474</b>	<b>572,465</b>
<b>Accumulated depreciation:</b>						
At 1 January 2005	86,550	56,614	11,657	87,282	1,407	243,510
Depreciation charge for the year	11,217	6,913	2,986	9,447	282	30,845
Reclassification	(78)	(214)	78	160	54	—
Written back on disposal	(2,948)	(2,153)	(1,245)	(2,204)	(194)	(8,744)
<b>At 31 December 2005</b>	<b>94,741</b>	<b>61,160</b>	<b>13,476</b>	<b>94,685</b>	<b>1,549</b>	<b>265,611</b>
<b>Net book value:</b>						
<b>At 31 December 2005</b>	<b>94,385</b>	<b>60,849</b>	<b>63,197</b>	<b>85,498</b>	<b>2,925</b>	<b>306,854</b>
<b>At 31 December 2004</b>	<b>83,907</b>	<b>60,449</b>	<b>53,118</b>	<b>75,793</b>	<b>2,685</b>	<b>275,952</b>

#### The Company – by segment

	Exploration and production RMB millions	Refining RMB millions	Marketing and distribution RMB millions	Chemicals RMB millions	Others RMB millions	Total RMB millions
<b>Cost/valuation:</b>						
At 1 January 2005	61,025	87,893	61,413	57,719	3,070	271,120
Addition for the year	151	113	267	38	120	689
Transferred from construction in progress	13,213	5,676	9,033	2,063	371	30,356
Transferred to subsidiaries	—	—	(577)	—	—	(577)
Reclassification	(130)	(176)	276	(2)	32	—
Disposals	(1,781)	(1,546)	(2,864)	(978)	(213)	(7,382)
<b>At 31 December 2005</b>	<b>72,478</b>	<b>91,960</b>	<b>67,548</b>	<b>58,840</b>	<b>3,380</b>	<b>294,206</b>
<b>Accumulated depreciation:</b>						
At 1 January 2005	26,483	42,803	11,117	32,112	1,057	113,572
Depreciation charge for the year	4,559	4,688	2,873	2,886	180	15,186
Transferred to subsidiaries	—	—	(66)	—	—	(66)
Reclassification	(65)	(49)	99	(1)	16	—
Written back on disposal	(1,631)	(1,181)	(1,214)	(734)	(185)	(4,945)
<b>At 31 December 2005</b>	<b>29,346</b>	<b>46,261</b>	<b>12,809</b>	<b>34,263</b>	<b>1,068</b>	<b>123,747</b>
<b>Net book value:</b>						
<b>At 31 December 2005</b>	<b>43,132</b>	<b>45,699</b>	<b>54,739</b>	<b>24,577</b>	<b>2,312</b>	<b>170,459</b>
<b>At 31 December 2004</b>	<b>34,542</b>	<b>45,090</b>	<b>50,296</b>	<b>25,607</b>	<b>2,013</b>	<b>157,548</b>

## NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2005

### 11 FIXED ASSETS (Continued)

#### The Group – by asset class

	Land and buildings	Oil and gas properties	Oil depots, storage tanks and service stations	Plant, machinery, equipment, vehicles and others	Total
	RMB millions	RMB millions	RMB millions	RMB millions	RMB millions
<b>Cost/valuation:</b>					
At 1 January 2005	47,107	151,945	59,963	260,447	519,462
Addition for the year	730	64	228	692	1,714
Transferred from construction in progress	2,462	20,985	13,521	25,630	62,598
Proportionate share of a new jointly controlled entity	469	—	—	846	1,315
Reclassification	(406)	(802)	650	558	—
Disposals	(1,044)	(2,251)	(2,145)	(7,184)	(12,624)
<b>At 31 December 2005</b>	<b>49,318</b>	<b>169,941</b>	<b>72,217</b>	<b>280,989</b>	<b>572,465</b>
<b>Accumulated depreciation:</b>					
At 1 January 2005	19,988	77,666	10,493	135,363	243,510
Depreciation charge for the year	1,778	10,593	2,878	15,596	30,845
Reclassification	(98)	(430)	153	375	—
Written back on disposal	(538)	(1,933)	(786)	(5,487)	(8,744)
<b>At 31 December 2005</b>	<b>21,130</b>	<b>85,896</b>	<b>12,738</b>	<b>145,847</b>	<b>265,611</b>
<b>Net book value:</b>					
<b>At 31 December 2005</b>	<b>28,188</b>	<b>84,045</b>	<b>59,479</b>	<b>135,142</b>	<b>306,854</b>
<b>At 31 December 2004</b>	<b>27,119</b>	<b>74,279</b>	<b>49,470</b>	<b>125,084</b>	<b>275,952</b>

#### The Company – by asset class

	Land and buildings	Oil and gas properties	Oil depots, storage tanks and service stations	Plant, machinery, equipment, vehicles and others	Total
	RMB millions	RMB millions	RMB millions	RMB millions	RMB millions
<b>Cost/valuation:</b>					
At 1 January 2005	25,187	53,307	56,824	135,802	271,120
Addition for the year	132	64	174	319	689
Transferred from construction in progress	989	12,266	9,033	8,068	30,356
Transferred to subsidiaries	(9)	—	(529)	(39)	(577)
Reclassification	(469)	(551)	651	369	—
Disposals	(552)	(944)	(2,097)	(3,789)	(7,382)
<b>At 31 December 2005</b>	<b>25,278</b>	<b>64,142</b>	<b>64,056</b>	<b>140,730</b>	<b>294,206</b>
<b>Accumulated depreciation:</b>					
At 1 January 2005	9,672	24,299	10,116	69,485	113,572
Depreciation charge for the year	1,046	4,193	2,488	7,459	15,186
Transferred to subsidiaries	(3)	—	(41)	(22)	(66)
Reclassification	(111)	(309)	154	266	—
Written back on disposal	(275)	(825)	(774)	(3,071)	(4,945)
<b>At 31 December 2005</b>	<b>10,329</b>	<b>27,358</b>	<b>11,943</b>	<b>74,117</b>	<b>123,747</b>
<b>Net book value:</b>					
<b>At 31 December 2005</b>	<b>14,949</b>	<b>36,784</b>	<b>52,113</b>	<b>66,613</b>	<b>170,459</b>
<b>At 31 December 2004</b>	<b>15,515</b>	<b>29,008</b>	<b>46,708</b>	<b>66,317</b>	<b>157,548</b>

The fixed assets and construction in progress of the Group at 30 September 1999 were revalued by registered valuers in the PRC. The valuation was reviewed and approved by the MOF (Note 1). Surplus on revaluation was RMB 29,093 million and deficit on revaluation was RMB 3,210 million. A net surplus on revaluation of RMB 25,883 million was resulted which has been incorporated in the Group's financial statements since the year ended 31 December 1999.

## NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2005

### 11 FIXED ASSETS (Continued)

In accordance with the relevant rules and regulations in respect of the acquisition of Sinopec National Star, the fixed assets and construction in progress of Sinopec National Star have been revalued by a firm of independent valuers in the PRC. Surplus on revaluation of RMB 541 million has been incorporated in the Group's financial statements since the year ended 31 December 2001.

In accordance with the relevant rules and regulations in respect of the Acquisition of Ethylene Assets, the fixed assets and construction in progress of Sinopec Maoming have been revalued by a firm of independent valuers in the PRC. Deficit on revaluation of RMB 86 million has been incorporated in the Group's financial statements since the year ended 31 December 2003.

In accordance with the relevant rules and regulations in respect of the Acquisition of Refining Assets, the fixed assets and construction in progress of Tahe Petrochemical and Xi'an Petrochemical have been revalued by a firm of independent valuers in the PRC. Surplus on revaluation of RMB 82 million has been incorporated in the Group's financial statements since the year ended 31 December 2003.

In accordance with the relevant rules and regulations in respect of the Acquisition of Acquired Assets, the related fixed assets and construction in progress have been revalued by a firm of independent valuers in the PRC. Surplus on revaluation of RMB 492 million has been incorporated in the Group's financial statements since the year ended 31 December 2004.

At 31 December 2005, the carrying amounts of fixed assets that were pledged by the Group and the Company were RMB 83 million (2004: RMB 123 million) and RMB 10 million (2004: RMB 10 million), respectively.

Provision for impairment losses on fixed assets is analysed as follows:

#### The Group – by segment

	Exploration and production RMB millions	Refining RMB millions	Marketing and distribution RMB millions	Chemicals RMB millions	Total RMB millions
At 1 January 2005	783	64	1,769	3,200	5,816
Addition for the year	60	—	366	1,425	1,851
Written off for the year	—	(53)	(865)	(515)	(1,433)
<b>At 31 December 2005</b>	<b>843</b>	<b>11</b>	<b>1,270</b>	<b>4,110</b>	<b>6,234</b>

#### The Company – by segment

	Exploration and production RMB millions	Refining RMB millions	Marketing and distribution RMB millions	Chemicals RMB millions	Total RMB millions
At 1 January 2005	720	13	1,737	1,568	4,038
Addition for the year	60	—	351	671	1,082
Written off for the year	—	(2)	(847)	(80)	(929)
<b>At 31 December 2005</b>	<b>780</b>	<b>11</b>	<b>1,241</b>	<b>2,159</b>	<b>4,191</b>

#### The Group – by asset class

	Land and buildings RMB millions	Oil and gas properties RMB millions	Oil depots, storage tanks and service stations RMB millions	Plant, machinery, equipment, vehicles and others RMB millions	Total RMB millions
At 1 January 2005	331	783	1,249	3,453	5,816
Addition for the year	79	60	261	1,451	1,851
Written off for the year	(59)	—	(593)	(781)	(1,433)
<b>At 31 December 2005</b>	<b>351</b>	<b>843</b>	<b>917</b>	<b>4,123</b>	<b>6,234</b>

## NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2005

### 11 FIXED ASSETS (Continued)

#### The Company – by asset class

	Land and buildings	Oil and gas properties	Oil depots, storage tanks and service stations	Plant, machinery, equipment, vehicles and others	Total
	RMB millions	RMB millions	RMB millions	RMB millions	RMB millions
At 1 January 2005	184	720	1,249	1,885	4,038
Addition for the year	21	60	261	740	1,082
Written off for the year	(51)	—	(575)	(303)	(929)
<b>At 31 December 2005</b>	<b>154</b>	<b>780</b>	<b>935</b>	<b>2,322</b>	<b>4,191</b>

Provision for impairment losses recognised on fixed assets of the chemicals segment of the Group of RMB 1,425 million (2004: RMB 2,747 million) for the year ended 31 December 2005 relate to certain chemicals production facilities that are held for use. The carrying values of these facilities were written down to their recoverable values. The primary factor resulting in the provision for impairment losses of the chemicals segment was due to higher operating and production costs caused by the increase in the prices of raw materials that are not expected to be recovered through an increase in selling price.

Provision for impairment losses recognised on fixed assets of the marketing and distribution segment of the Group of RMB 366 million (2004: RMB 1,769 million) for the year ended 31 December 2005 primarily relate to certain service stations that were closed during the year. In measuring the amounts of impairment charges, the carrying amounts of these assets were compared to the present value of the expected future cash flows of the assets, as well as information about sales and purchases of similar properties in the same geographic area.

The factors resulting in the exploration and production segment of the Group provision for impairment losses of RMB 60 million (2004: RMB 98 million) for the year ended 31 December 2005 were unsuccessful development drilling and high operating and development costs for certain small oil fields. The carrying values of these oil and gas properties were written down to a recoverable value which was determined based on the present values of the expected future cash flows of the assets. The oil and gas pricing was a factor used in the determination of the present values of the expected future cash flows of the assets and had an impact on the recognition of the asset impairment.

At 31 December 2005 and 2004, the Group and the Company had no individually significant fixed assets which were temporarily idle or pending for disposal.

At 31 December 2005 and 2004, the Group and the Company had no individually significant fully depreciated fixed assets which were still in use.

### 12 CONSTRUCTION MATERIALS

At 31 December 2005 and 2004, the Group's and the Company's construction materials mainly represent the actual cost of materials such as steel and copper to be used for construction projects.

## NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2005

### 13 CONSTRUCTION IN PROGRESS

#### The Group

	Exploration and production	Refining	Marketing and distribution	Chemicals	Others	Total
	RMB millions	RMB millions	RMB millions	RMB millions	RMB millions	RMB millions
At 1 January 2005	9,262	8,215	13,451	13,535	1,513	45,976
Addition for the year	25,894	14,036	10,192	9,003	1,014	60,139
Addition for the year of jointly controlled entities	814	—	—	1,830	—	2,644
Proportionate share of a new jointly controlled entity	—	—	—	5,461	—	5,461
Dry hole costs written off	(2,992)	—	—	—	—	(2,992)
Transferred to fixed assets and other assets	(22,094)	(8,066)	(13,687)	(18,927)	(381)	(63,155)
<b>At 31 December 2005</b>	<b>10,884</b>	<b>14,185</b>	<b>9,956</b>	<b>10,902</b>	<b>2,146</b>	<b>48,073</b>

The interest rates per annum at which borrowing costs were capitalised during the year by the Group ranged from 3.3% to 6.6% (2004: 3.1% to 6.0%).

The Group's proportionate share of the jointly controlled entities' construction in progress at 31 December 2005 in the exploration and production and the chemicals segments were RMB 2,888 million (2004: RMB 2,053 million) and RMB 504 million (2004: RMB 8,171 million), respectively.

At 31 December 2005, major construction projects of the Group are as follows:

Project name	Budgeted amount	At 1 January 2005	Addition for the year	At 31 December 2005	Percentage of completion	Source of funding	Accumulated interest capitalised at 31 December 2005
	RMB millions	RMB millions	RMB millions	RMB millions			RMB millions
<b>The Group</b>							
Yizheng-Changling Crude Oil Pipeline Project	4,820	893	2,994	3,887	81%	Bank loans & self-financing	45
1,000,000 tonnes Ethylene Reconstruction and Expansion Project	7,494	509	2,008	2,517	34%	Bank loans & self-financing	33
Middle East Sour Crude Processing and Clean Fuel Production Supporting Project	4,438	350	2,100	2,450	55%	Bank loans & self-financing	14
Chaoyang Square Project	2,800	906	200	1,106	40%	Self-financing	—
Coal in replacement of Oil Technology Improvement Project	1,256	603	468	1,071	85%	Bank loans & self-financing	29

#### The Company

	Exploration and production	Refining	Marketing and distribution	Chemicals	Others	Total
	RMB millions	RMB millions	RMB millions	RMB millions	RMB millions	RMB millions
At 1 January 2005	6,607	6,759	9,941	3,978	1,494	28,779
Addition for the year	16,528	12,119	7,445	5,778	915	42,785
Dry hole costs written off	(2,271)	—	—	—	—	(2,271)
Transferred to fixed assets	(13,213)	(5,676)	(9,033)	(2,063)	(371)	(30,356)
<b>At 31 December 2005</b>	<b>7,651</b>	<b>13,202</b>	<b>8,353</b>	<b>7,693</b>	<b>2,038</b>	<b>38,937</b>

The interest rates per annum at which borrowing costs were capitalised for the year ended 31 December 2005 by the Company ranged from 3.3% to 6.6% (2004: 3.1% to 6.0%).



## NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2005

### 14 INTANGIBLE ASSETS

#### The Group

	Computer software license RMB millions	Technical know-how RMB millions	Exploration and production right RMB millions	Others RMB millions	Total RMB millions
<b>Cost:</b>					
At 1 January 2005	852	2,286	3,163	635	6,936
Addition for the year	183	660	—	1,134	1,977
Disposals	(2)	—	—	(166)	(168)
Other decrease	—	—	—	(287)	(287)
<b>At 31 December 2005</b>	<b>1,033</b>	<b>2,946</b>	<b>3,163</b>	<b>1,316</b>	<b>8,458</b>
<b>Accumulated Amortisation:</b>					
At 1 January 2005	185	841	468	97	1,591
Amortisation charge for the year	490	315	117	64	986
Written back on disposal	(2)	—	—	(26)	(28)
Other decrease	—	—	—	(15)	(15)
<b>At 31 December 2005</b>	<b>673</b>	<b>1,156</b>	<b>585</b>	<b>120</b>	<b>2,534</b>
<b>Net book value:</b>					
<b>At 31 December 2005</b>	<b>360</b>	<b>1,790</b>	<b>2,578</b>	<b>1,196</b>	<b>5,924</b>
<b>At 31 December 2004</b>	<b>667</b>	<b>1,445</b>	<b>2,695</b>	<b>538</b>	<b>5,345</b>

Except for the exploration and production right, the above intangible assets were acquired from third parties. The Company acquired Sinopec National Star together with the exploration and production right from Sinopec Group Company. The exploration and production right was valued with reference to the proved reserves of the associated oil fields. The amortisation period of the exploration and production right was 27 years. The amortisation periods of other intangible assets range from 4 to 40 years. At 31 December 2005, the remaining amortisation period of the exploration and production right was 22 years.

#### The Company

	Computer software license RMB millions	Technical know-how RMB millions	Exploration and production right RMB millions	Others RMB millions	Total RMB millions
<b>Cost:</b>					
At 1 January 2005	671	1,316	3,163	421	5,571
Addition for the year	155	2	—	713	870
Disposals	(1)	—	—	(163)	(164)
<b>At 31 December 2005</b>	<b>825</b>	<b>1,318</b>	<b>3,163</b>	<b>971</b>	<b>6,277</b>
<b>Accumulated Amortisation:</b>					
At 1 January 2005	120	673	468	49	1,310
Amortisation charge for the year	467	130	117	41	755
Written back on disposal	(1)	—	—	(25)	(26)
<b>At 31 December 2005</b>	<b>586</b>	<b>803</b>	<b>585</b>	<b>65</b>	<b>2,039</b>
<b>Net book value:</b>					
<b>At 31 December 2005</b>	<b>239</b>	<b>515</b>	<b>2,578</b>	<b>906</b>	<b>4,238</b>
<b>At 31 December 2004</b>	<b>551</b>	<b>643</b>	<b>2,695</b>	<b>372</b>	<b>4,261</b>

Except for the exploration and production right, the above intangible assets were acquired from third parties. The Company acquired Sinopec National Star together with the exploration and production right from Sinopec Group Company. The exploration and production right was valued with reference to the proved reserves of the associated oil fields. The amortisation period of the exploration and production right was 27 years. The amortisation periods of other intangible assets range from 4 to 40 years. At 31 December 2005, the remaining amortisation period of the exploration and production right was 22 years.

### 15 LONG-TERM DEFERRED EXPENSES

Long-term deferred expenses primarily represent prepaid rental expenses over one year and catalysts expenditures.

## NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2005

### 16 DEFERRED TAX ASSETS AND LIABILITIES

#### The Group

	Deferred tax assets		Deferred tax liabilities		Net balance	
	2005	2004	2005	2004	2005	2004
	RMB millions	RMB millions	RMB millions	RMB millions	RMB millions	RMB millions
<i>Current</i>						
Receivables and inventories	3,900	2,524	—	—	3,900	2,524
<i>Non-current</i>						
Fixed assets	1,642	1,566	—	(198)	1,642	1,368
Tax value of losses carried forward	128	66	—	—	128	66
Others	31	10	—	—	31	10
<b>Deferred tax assets/(liabilities)</b>	<b>5,701</b>	<b>4,166</b>	<b>—</b>	<b>(198)</b>	<b>5,701</b>	<b>3,968</b>

#### The Company

	Deferred tax assets		Deferred tax liabilities		Net balance	
	2005	2004	2005	2004	2005	2004
	RMB millions	RMB millions	RMB millions	RMB millions	RMB millions	RMB millions
<i>Current</i>						
Receivables and inventories	1,635	2,245	—	—	1,635	2,245
<i>Non-current</i>						
Fixed assets	1,553	1,457	—	(16)	1,553	1,441
Others	15	6	—	—	15	6
<b>Deferred tax assets/(liabilities)</b>	<b>3,203</b>	<b>3,708</b>	<b>—</b>	<b>(16)</b>	<b>3,203</b>	<b>3,692</b>

### 17 SHORT-TERM LOANS

The Group's and the Company's short-term loans represent:

	The Group		The Company	
	2005	2004	2005	2004
	RMB millions	RMB millions	RMB millions	RMB millions
Short-term bank loans	15,392	20,009	3,094	10,527
Loans from Sinopec Group Company and fellow subsidiaries	732	6,714	3,846	5,727
<b>Total</b>	<b>16,124</b>	<b>26,723</b>	<b>6,940</b>	<b>16,254</b>

The Group's and the Company's weighted average interest rates per annum on short-term loans were 4.0% (2004: 3.9%) and 3.2% (2004: 4.0%) respectively at 31 December 2005. The majority of the above loans are unsecured.

Except for the balance disclosed in Note 41, there is no amount due to shareholders who hold 5% or more voting right of the Company included in the balance of short-term loans.

At 31 December 2005 and 2004, the Group and the Company had no significant overdue short-term loan.

### 18 BILLS PAYABLE

Bills payable primarily represented bank accepted bills for the purchase of material, goods and products. The repayment term is normally from three to six months.

### 19 TRADE ACCOUNTS PAYABLE

The ageing analysis of trade accounts payable is as follows:

	The Group			
	2005		2004	
	RMB millions	%	RMB millions	%
Within 3 months	40,932	77.3	12,868	54.1
Between 3 and 6 months	10,542	19.9	9,110	38.3
Over 6 months	1,493	2.8	1,814	7.6
<b>Total</b>	<b>52,967</b>	<b>100.0</b>	<b>23,792</b>	<b>100.0</b>

	The Company			
	2005		2004	
	RMB millions	%	RMB millions	%
Within 3 months	22,129	76.7	13,462	63.7
Between 3 and 6 months	5,792	20.1	6,183	29.3
Over 6 months	912	3.2	1,492	7.0
<b>Total</b>	<b>28,833</b>	<b>100.0</b>	<b>21,137</b>	<b>100.0</b>

Except for the balances disclosed in Note 41, there is no amount due to shareholders who hold 5% or more voting right of the Company included in the balance of trade accounts payable.

At 31 December 2005 and 2004, the Group and the Company had no individually significant trade accounts payable aged over three years.

## NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2005

### 20 RECEIPTS IN ADVANCE

Except for the balances disclosed in Note 41, there is no amount due to shareholders who hold 5% or more voting right of the Company included in the balance of receipts in advance.

At 31 December 2005 and 2004, the Group and the Company had no individually significant receipts in advance aged over one year.

### 21 TAXES PAYABLE

	The Group		The Company	
	2005	2004	2005	2004
	RMB millions	RMB millions	RMB millions	RMB millions
Value added tax	(2,240)	(1,119)	(1,796)	(1,377)
Consumption tax	1,348	1,443	1,031	1,146
Income tax	5,029	5,391	2,494	3,142
Business tax	45	99	25	37
Other taxes	1,080	927	321	222
<b>Total</b>	<b>5,262</b>	<b>6,741</b>	<b>2,075</b>	<b>3,170</b>

The provision for PRC current income tax is based on a statutory rate of 33% of the assessable income of the Group and the Company as determined in accordance with the relevant tax rules and regulations of the PRC during the years ended 31 December 2005 and 2004, except for certain branches and subsidiaries of the Company, which are taxed at a preferential rate of 15%, and certain jointly controlled entities of the Company, which are entitled to a tax holiday of a tax-free period for the first two years and a 50% reduction in income tax for the following three years.

### 22 OTHER PAYABLES

At 31 December 2005 and 2004, the Group's and the Company's other payables primarily represented payables for resources compensation fee and education surcharge.

### 23 OTHER CREDITORS

At 31 December 2005 and 2004, the Group's and the Company's other creditors primarily represented payables for constructions.

Except for the balances disclosed in Note 41, there is no amount due to shareholders who hold 5% or more voting right of the Company included in the balance of other creditors.

At 31 December 2005 and 2004, the Group and the Company had no individually significant other creditors aged over three years.

### 24 ACCRUED EXPENSES

At 31 December 2005 and 2004, the Group's and the Company's accrued expenses primarily represented accrued interest expenses, repair and maintenance expenses, research and development expenses and other production expenses.

### 25 CURRENT PORTION OF LONG-TERM LOANS

The Group's and the Company's current portion of long-term loans represent:

	The Group		The Company	
	2005	2004	2005	2004
	RMB millions	RMB millions	RMB millions	RMB millions
<b>Long-term bank loans</b>				
— Renminbi loans	11,952	8,500	9,694	6,247
— Japanese Yen loans	615	805	615	798
— US Dollar loans	2,206	2,841	1,710	2,341
— Euro loans	24	28	24	28
— Hong Kong Dollar loans	82	3	—	—
	<b>14,879</b>	<b>12,177</b>	<b>12,043</b>	<b>9,414</b>
<b>Long-term bank loans of jointly controlled entities</b>				
— Renminbi loans	82	—	—	—
— US Dollar loans	111	—	—	—
	<b>193</b>	<b>—</b>	<b>—</b>	<b>—</b>
<b>Long-term other loans</b>				
— Renminbi loans	22	88	—	61
— US Dollar loans	4	33	1	31
	<b>26</b>	<b>121</b>	<b>1</b>	<b>92</b>
<b>Long-term loans from Sinopec Group Company and fellow subsidiaries</b>				
— Renminbi loans	100	2,000	100	2,000
<b>Total current portion of long-term loans</b>	<b>15,198</b>	<b>14,298</b>	<b>12,144</b>	<b>11,506</b>

At 31 December 2005 and 2004, the Group and the Company had no significant overdue long-term loan.

## NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2005

### 26 LONG-TERM LOANS

The Group's and the Company's long-term loans represent:

Interest rate and final maturity	The Group		The Company		
	2005	2004	2005	2004	
	RMB millions	RMB millions	RMB millions	RMB millions	
<b>Third parties debts</b>					
<b>Long-term bank loans</b>					
Renminbi loans	Interest rates ranging from interest free to 5.8% per annum at 31 December 2005 with maturities through 2013	59,769	52,227	54,792	45,233
Japanese Yen loans	Interest rates ranging from 2.6% to 5.8% per annum at 31 December 2005 with maturities through 2024	3,394	4,562	3,394	4,556
US Dollar loans	Interest rates ranging from interest free to 7.4% per annum at 31 December 2005 with maturities through 2031	5,056	7,729	3,571	5,278
Euro loans	Fixed rate at 6.7% per annum at 31 December 2005 with maturities through 2010	117	165	117	165
Hong Kong Dollar loans	Floating rate at Hong Kong Prime Rate plus 0.8% to 1.1% per annum at 31 December 2005 with maturities through 2007	94	5	—	—
Less: Current portion		14,879	12,177	12,043	9,414
<b>Long-term bank loans</b>		<b>53,551</b>	<b>52,511</b>	<b>49,831</b>	<b>45,818</b>
<b>Long-term bank loans of jointly controlled entities</b>					
Renminbi loans	Floating rate at 90% of PBOC's base lending rate per annum at 31 December 2005 with maturities through 2021	5,710	2,415	—	—
US Dollar loans	Floating rate at London Interbank Offer Rate plus 0.4% to 0.7% per annum at 31 December 2005 with maturities through 2021	4,296	2,048	—	—
Less: Current portion		193	—	—	—
<b>Long-term bank loans of jointly controlled entities</b>		<b>9,813</b>	<b>4,463</b>	<b>—</b>	<b>—</b>
<b>Long-term other loans</b>					
Renminbi loans	Interest rates ranging from interest free to 5.0% per annum at 31 December 2005 with maturities through 2008	170	359	37	200
US Dollar loans	Interest rates ranging from interest free to 2.0% per annum at 31 December 2005 with maturities through 2015	51	110	34	89
Less: Current portion		26	121	1	92
<b>Long-term other loans</b>		<b>195</b>	<b>348</b>	<b>70</b>	<b>197</b>
<b>Long-term loans from Sinopec Group Company and fellow subsidiaries</b>					
Renminbi loans	Interest free with maturity in 2020	35,561	35,561	35,561	35,561
Renminbi loans	Interest rates ranging from 5.0% to 5.2% per annum at 31 December 2005 with maturities through 2009	4,401	3,204	3,751	2,756
Less: Current portion		100	2,000	100	2,000
<b>Long-term loans from Sinopec Group Company and fellow subsidiaries</b>		<b>39,862</b>	<b>36,765</b>	<b>39,212</b>	<b>36,317</b>
<b>Long-term loans of jointly controlled entities from Sinopec Group Company and fellow subsidiaries</b>					
Renminbi loans	Floating rate at 90% of PBOC's base lending rate applicable to three-year tenor loan per annum at 31 December 2005 with maturities through 2021	71	—	—	—
<b>Long-term loans of jointly controlled entities from Sinopec Group Company and fellow subsidiaries</b>		<b>71</b>	<b>—</b>	<b>—</b>	<b>—</b>
		<b>103,492</b>	<b>94,087</b>	<b>89,113</b>	<b>82,332</b>

## NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2005

### 26 LONG-TERM LOANS (Continued)

The maturity analysis of the Group's and the Company's long-term loans is as follows:

	The Group		The Company	
	2005	2004	2005	2004
	RMB millions	RMB millions	RMB millions	RMB millions
Between one and two years	18,787	15,886	16,420	12,363
Between two and five years	39,142	36,041	34,771	31,279
After five years	45,563	42,160	37,922	38,690
<b>Total long-term loans</b>	<b>103,492</b>	<b>94,087</b>	<b>89,113</b>	<b>82,332</b>

At 31 December 2005, the Group and the Company had secured loans from third parties amounting to RMB 35 million (2004: RMB 40 million) and RMB 13 million (2004: RMB 9 million) respectively. At 31 December 2005, the Group had loans secured by long-term investments from third parties amounting to RMB 3,899 million (2004: RMB nil). All long-term other loans are unsecured.

Except for the balances disclosed in Note 41, there is no amount due to shareholders who hold 5% or more voting right of the Company included in the balance of long-term loans.

### 27 DEBENTURES PAYABLE

	Interest rate and final maturity	The Group and the Company	
		2005	2004
		RMB millions	RMB millions
Short-term corporate bonds	Effective rate at 2.54% per annum, redeemable in April 2006 (i)	9,921	—
Corporate bonds	Fixed rate at 4.61% per annum, redeemable in February 2014 (ii)	3,500	3,500

(i) The Company issued six-month corporate bonds of face value at RMB 10 billion to corporate investors in PRC debenture market on 24 October 2005, at a discounted value of RMB 98.75 per RMB 100 par value, with an effective yield at 2.54% per annum with maturity in April 2006.

(ii) The Company issued ten years corporate bonds of RMB 3.5 billion to PRC citizens as well as PRC legal and non-legal persons on 24 February 2004, guaranteed by Sinopec Group Company with a fixed interest rate at 4.61% per annum and annual interest payment schedule. Interest payable for the current period was included in accrued expenses.

### 28 OTHER LONG-TERM LIABILITIES

Other long-term liabilities primarily represent provision for future dismantlement of oil and gas properties, the costs arising from environmental restoration and specific research and development projects.

### 29 SHARE CAPITAL

	The Group and the Company	
	2005	2004
	RMB millions	RMB millions
<b>Registered, issued and fully paid:</b>		
67,121,951,000 domestic state-owned A shares of RMB 1.00 each	67,122	67,122
16,780,488,000 H shares of RMB 1.00 each	16,780	16,780
2,800,000,000 A shares of RMB 1.00 each	2,800	2,800
	<b>86,702</b>	<b>86,702</b>

The Company was established on 25 February 2000 with a registered capital of 68.8 billion state-owned domestic shares with a par value of RMB 1.00 each, which were all held by Sinopec Group Company (see Note 1).

Pursuant to the resolutions passed in the Extraordinary General Meeting of the Company held on 25 July 2000 and the approval from relevant authorities, the Company issued 15,102,439,000 H shares with a par value of RMB 1.00 each in its initial global offering in October 2000. The shares include 12,521,864,000 H shares and 25,805,750 American Depositary Shares ("ADSs", each representing 100 H shares) at prices of HK\$ 1.59 and US\$ 20.645 respectively. As part of the offering, 1,678,049,000 shares were offered in placing to Hong Kong and overseas investors.

In July 2001, the Company issued 2,800,000,000 domestic listed A shares with a par value of RMB 1.00 each at RMB 4.22.

All the domestic ordinary shares and H shares rank pari passu in all material aspects.

KPMG Huazhen had verified the above paid-in capital. The capital verification reports, KPMG-C (2000) CV No. 0007, KPMG-C (2001) CV No. 0002 and KPMG-C (2001) CV No. 0006 were issued on 22 February 2000, 27 February 2001 and 23 July 2001 respectively.

## NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2005

### 30 CAPITAL RESERVE

The movements in capital reserve are as follows:

	The Group		The Company	
	2005	2004	2005	2004
	RMB millions	RMB millions	RMB millions	RMB millions
Balance at 1 January	37,121	36,852	37,797	36,852
Government grants (i)	—	269	—	269
Reserve for equity investment (ii)	—	—	—	676
<b>Balance at 31 December</b>	<b>37,121</b>	<b>37,121</b>	<b>37,797</b>	<b>37,797</b>

(i) During the year ended 31 December 2004, the Group received subsidy on investments amounted to RMB 269 million, pursuant to Fa Gai Tou Zi [2004] No. 1248 "Notice on the Enterprise Technology Reform and Industry Upgrade regarding the First Batch State Debt's Project Fund Plan in 2004" issued by the National Development and Reform Commission and the MOF. This fund is used for technology improvement projects.

(ii) During the year ended 31 December 2004, the Company invested in certain newly established subsidiaries with certain non-monetary assets. The initial investment costs are determined based on the assets' revalued amount. The shortfalls of the initial investment costs over the Company's share of the shareholders' funds in these subsidiaries resulting from the surplus of the assets' revalued amount over the carrying amount are recognised in the Company's capital reserve. Such reserve for equity investment has been eliminated in the Group's consolidated financial statements.

### 31 SURPLUS RESERVES

Movements in surplus reserves are as follows:

	The Group and the Company			Total
	Statutory surplus reserve	Statutory public welfare fund	Discretionary surplus reserve	
	RMB millions	RMB millions	RMB millions	RMB millions
At 1 January 2004	6,330	6,330	7,000	19,660
Appropriation of net profit	3,228	3,228	—	6,456
<b>At 31 December 2004</b>	<b>9,558</b>	<b>9,558</b>	<b>7,000</b>	<b>26,116</b>
At 1 January 2005	9,558	9,558	7,000	26,116
Appropriation of net profit	3,956	3,956	—	7,912
<b>At 31 December 2005</b>	<b>13,514</b>	<b>13,514</b>	<b>7,000</b>	<b>34,028</b>

The Articles of Association of the Company and the following profit appropriation plans had been approved at the Extraordinary General Meeting held on 25 July 2000:

- 10% of the net profit is transferred to the statutory surplus reserve;
- 5% to 10% of the net profit is transferred to the statutory public welfare fund; and
- after the transfer to the statutory surplus reserve and the statutory public welfare fund, a transfer to discretionary surplus reserve can be made upon the passing of a resolution at the shareholders' meeting.

### 32 INCOME FROM PRINCIPAL OPERATIONS

The income from principal operations represents revenue from sales of crude oil, natural gas, petroleum and chemical products net of value added tax. The Group's segmental information is set out in Note 46.

During the year ended 31 December 2005, revenue from sales to top five customers amounted to RMB 62,115 million (2004: RMB 58,691 million) which accounted for 8% (2004: 10%) of income from principal operations of the Group.

### 33 SALES TAXES AND SURCHARGES

	The Group		The Company	
	2005	2004	2005	2004
	RMB millions	RMB millions	RMB millions	RMB millions
Consumption tax	12,430	11,847	8,932	7,981
City construction tax	2,575	2,505	1,297	1,261
Education surcharge	1,305	1,243	658	624
Resources tax	634	452	201	114
Business tax	208	156	161	114
<b>Total</b>	<b>17,152</b>	<b>16,203</b>	<b>11,249</b>	<b>10,094</b>

## NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2005

### 34 FINANCIAL EXPENSES

	The Group		The Company	
	2005	2004	2005	2004
	RMB millions	RMB millions	RMB millions	RMB millions
Interest expenses incurred	7,166	4,909	4,596	3,067
Less: Capitalised interest expenses	601	327	455	231
<b>Net interest expenses</b>	<b>6,565</b>	<b>4,582</b>	<b>4,141</b>	<b>2,836</b>
Interest income	(382)	(359)	(123)	(144)
Foreign exchange losses	79	167	17	130
Foreign exchange gains	(996)	(59)	(496)	(52)
<b>Total</b>	<b>5,266</b>	<b>4,331</b>	<b>3,539</b>	<b>2,770</b>

### 35 EXPLORATION EXPENSES

Exploration expenses include geological and geophysical expenses and written off of dry hole costs.

### 36 INVESTMENT INCOME

	The Group		The Company	
	2005	2004	2005	2004
	RMB millions	RMB millions	RMB millions	RMB millions
Investment income accounted for under the cost method	255	216	76	84
Amortisation of equity investment differences	(200)	(186)	(201)	(157)
Impairment losses of investment	(77)	(96)	(14)	(2)
Investment income accounted for under the equity method	835	1,154	51,785	39,449
<b>Total</b>	<b>813</b>	<b>1,088</b>	<b>51,646</b>	<b>39,374</b>

### 37 SUBSIDY INCOME

The Group received a cash government grant from the Ministry of Finance of the PRC of RMB 9,415 million (2004: RMB nil) as a compensation of loss incurred due to the distortion of the correlation of domestic refined petroleum product prices and the crude oil prices during the year ended 31 December 2005. There are no unfilled conditions and other contingencies attached to the receipt of this government grant. There is no assurance that the Group will continue to receive such grant in the future.

### 38 NON-OPERATING EXPENSES

	The Group		The Company	
	2005	2004	2005	2004
	RMB millions	RMB millions	RMB millions	RMB millions
Loss on disposal of fixed assets	2,422	4,304	1,826	2,733
Impairment losses on fixed assets	1,851	4,628	1,082	3,417
Fines, penalties and compensation	160	280	149	273
Donations	203	275	144	91
Employee reduction expenses (Note)	369	919	119	745
Others	964	765	647	620
<b>Total</b>	<b>5,969</b>	<b>11,171</b>	<b>3,967</b>	<b>7,879</b>

Note: During the year ended 31 December 2005, in accordance with the Group's voluntary employee reduction plan, the Group recorded employee reduction expenses of RMB 369 million relating to the reduction of approximately 7,000 employees.

During the year ended 31 December 2004, in accordance with the Group's voluntary employee reduction plan, and in connection with the Acquisition of Acquired Assets from and Disposal of Downhole Assets to Sinopec Group Company, the Group recorded employee reduction expenses of RMB 919 million relating to the reduction of approximately 24,000 employees.

## NOTES ON THE FINANCIAL STATEMENTS

for the year ended 31 December 2005

### 39 INCOME TAX

	The Group		The Company	
	2005	2004	2005	2004
	RMB millions	RMB millions	RMB millions	RMB millions
Provision for PRC income tax for the year	20,159	18,405	17,137	16,815
Deferred taxation	(1,733)	(2,439)	489	(2,198)
Adjustment for provision for income tax in respect of proceeding year	477	94	512	152
<b>Total</b>	<b>18,903</b>	<b>16,060</b>	<b>18,138</b>	<b>14,769</b>

### 40 DIVIDENDS

#### (a) Dividends of ordinary shares proposed after the balance sheet date

Pursuant to a resolution passed at the Board of Directors' meeting on 31 March 2006, a final dividend in respect of the year ended 31 December 2005 of RMB 0.09 per share totalling RMB 7,803 million was proposed for shareholders' approval at the Annual General Meeting.

#### (b) Dividends of ordinary shares declared during the year

Pursuant to the Articles of Association of the Company and the resolution passed at the Directors' meeting on 26 August 2005, an interim dividend for the year ending 31 December 2005 of RMB 0.04 (2004: RMB 0.04) per share totalling RMB 3,468 million (2004: RMB 3,468 million) was declared.

Pursuant to the shareholders' approval at the Annual General Meeting on 18 May 2005, a final dividend of RMB 0.08 per share totalling RMB 6,936 million in respect of the year ended 31 December 2004 was declared and paid on 18 May 2005.

Pursuant to the shareholders' approval at the Annual General Meeting on 18 May 2004, a final dividend of RMB 0.06 per share totalling RMB 5,202 million in respect of the year ended 31 December 2003 was declared and paid on 28 June 2004.

### 41 RELATED PARTIES AND RELATED PARTY TRANSACTIONS

#### (a) Related parties having the ability to exercise control over the Group

The name of the company	:	China Petrochemical Corporation
Registered address	:	No. 6A, Huixin East Street, Chaoyang District, Beijing
Principal activities	:	Processing crude oil into refined products and petrochemical products, petrochemical products which include: petrochemical products made from crude oil and natural gas; production, sale and import and export of synthetic fibre and synthetic fibre monomer.
Relationship with the Group	:	Ultimate holding company
Types of legal entity	:	State-owned
Authorised representative	:	Chen Tonghai
Registered capital	:	RMB 104,912 million

There is no movement in the above registered capital for the year ended 31 December 2005.

Change of the Company's equity interests held by Sinopec Group Company is as follows:

From 1 January 2005 to 19 December 2005	67.92%
From 20 December 2005 to 31 December 2005	71.23%

#### (b) Related parties not having the ability to exercise control over the Group

*Related parties under common control of a parent company with the Company:*

Sinopec Finance Company Limited  
 Nanjing Chemical Industry Company Limited  
 Sichuan Vinylon Company  
 Nanjing Petrochemical Company  
 Qingjiang Petrochemical Limited Liability Company  
 Baoding Petrochemical Company  
 Baling Petrochemical Yueyang Petrochemical Company  
 Tianjin United Chemical Company  
 Zhanjiang Dongxing Petroleum Corporation Company Limited  
 Qingdao Petrochemical Company  
 Baling Petrochemical Company Limited  
 Jinling Petrochemical Company Limited  
 Yangzi Petrochemical Company Limited  
 Guangdong Nanhua Petroleum Company Limited

*Associates of the Company:*

Sinopec Railway Oil Marketing Company Limited  
 Sinopec Changjiang Fuel Company Limited  
 China Shipping & Sinopec Suppliers Company Limited



## NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2005

### 41 RELATED PARTIES AND RELATED PARTY TRANSACTIONS (Continued)

(b) Related parties not having the ability to exercise control over the Group (Continued)

*Jointly controlled entities of the Group:*

Shanghai Secco Petrochemical Company Limited  
 BASF-YPC Company Limited  
 Yueyang Sinopec and Shell Coal Gasification Company Limited  
 Block A Oil Field in the Western Area Chengdao in Bohai Bay

(c) The principal related party transactions carried out in the ordinary course of business are as follows:

	Note	2005 RMB millions	2004 RMB millions
Sales of goods	(i)	95,123	72,015
Purchases	(ii)	48,454	40,911
Transportation and storage	(iii)	1,959	2,003
Exploration and development services	(iv)	17,001	14,446
Production related services	(v)	10,653	9,123
Ancillary and social services	(vi)	1,790	1,776
Operating lease charges	(vii)	3,213	3,365
Agency commission income	(viii)	48	41
Intellectual property license fee paid	(ix)	9	10
Interest received	(x)	52	59
Interest paid	(xi)	994	622
Net deposits (withdrawn from)/placed with related parties	(xii)	(82)	407
Net loans (paid to)/obtained from related parties	(xiii)	(4,714)	3,787

The amounts set out in the table above in respect of the years ended 31 December 2005 and 2004 represent the relevant costs to the Group and income from related parties as determined by the corresponding contracts with the related parties.

At 31 December 2005 and 2004, there were no guarantees given to banks by the Group in respect of banking facilities to Sinopec Group Company and fellow subsidiaries.

The directors of the Company are of the opinion that the above transactions with related parties were conducted in the ordinary course of business and on normal commercial terms or in accordance with the agreements governing such transactions, and this has been confirmed by the independent non-executive directors.

Notes:

- (i) Sales of goods represent the sale of crude oil, intermediate petrochemical products, petroleum products and ancillary materials.
- (ii) Purchases represent the purchase of material and utility supplies directly related to the Group's operations such as the procurement of raw and ancillary materials and related services, supply of water, electricity and gas.
- (iii) Transportation and storage represent the cost for the use of railway, road and marine transportation services, pipelines, loading, unloading and storage facilities.
- (iv) Exploration and development services comprise direct costs incurred in the exploration of crude oil such as geophysical, drilling, well testing and well measurement services.
- (v) Production related services represent ancillary services rendered in relation to the Group's operations such as equipment repair and general maintenance, insurance premium, technical research, communications, fire fighting, security, product quality testing and analysis, information technology, design and engineering, construction which includes the construction of oilfield ground facilities, refineries and chemical plants, manufacture of replacement parts and machinery, installation, project management and environmental protection.
- (vi) Ancillary and social services represent expenditures for social welfare and support services such as educational facilities, media communication services, sanitation, accommodation, canteens, property maintenance and management services.
- (vii) Operating lease charges represent the rental paid to Sinopec Group Company for operating leases in respect of land, buildings and equipments.
- (viii) Agency commission income represents commission earned for acting as an agent in respect of sales of products and purchase of goods of certain entities owned by Sinopec Group Company.
- (ix) Intellectual property license fee represents reimbursement paid to Sinopec Group Company for fees required to maintain the validity of certain licenses for trademarks, patents, technology and computer software.
- (x) Interest received represents interest received from deposits placed with Sinopec Finance Company Limited, a finance company controlled by Sinopec Group Company. The applicable interest rate is determined in accordance with the prevailing saving deposit rate.
- (xi) Interest paid represents interest charges on the loans obtained from Sinopec Group Company and Sinopec Finance Company Limited.
- (xii) Deposits were withdrawn from/placed with Sinopec Finance Company Limited.
- (xiii) The Group obtained/repaid loans from/to Sinopec Group Company and Sinopec Finance Company Limited. The calculated periodic balance of average loan for the year ended 31 December 2005, which is based on monthly average balances, was RMB 42,518 million (2004: RMB 42,696 million).

## NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2005

### 41 RELATED PARTIES AND RELATED PARTY TRANSACTIONS (Continued)

In connection with the Reorganisation, the Company and Sinopec Group Company entered into a number of agreements under which 1) Sinopec Group Company will provide goods and products and a range of ancillary, social and supporting services to the Group and 2) the Group will sell certain goods to Sinopec Group Company. These agreements impacted the operating results of the Group for the year ended 31 December 2005. The terms of these agreements are summarised as follows:

(a) The Company entered into an Agreement for Mutual Provision of Products and Ancillary Services (“Mutual Provision Agreement”) with Sinopec Group Company in which Sinopec Group Company has agreed to provide the Group with certain ancillary production services, construction services, information advisory services, supply services and other services and products. While each of Sinopec Group Company and the Company is permitted to terminate the Mutual Provision Agreement upon at least six months’ notice, Sinopec Group Company agrees not to terminate the agreement if the Group is unable to obtain comparable services from a third party. The pricing policy for these services and products provided by Sinopec Group Company to the Group is as follows:

- the government-prescribed price;
- where there is no government-prescribed price, the government guidance price;
- where there is neither a government-prescribed price nor a government guidance price, the market price; or
- where none of the above is applicable, the price to be agreed between the parties, which shall be based on a reasonable cost incurred in providing such services plus a profit margin not exceeding 6%.

(b) The Company has entered into an Agreement for Provision of Cultural and Educational, Health Care and Community Services with Sinopec Group Company effective from 1 January 2000 in which Sinopec Group Company has agreed to provide the Group with certain cultural, educational, health care and community services on the same pricing terms and termination conditions as agreed to in the above Mutual Provision Agreement.

(c) The Company has entered into a number of lease agreements with Sinopec Group Company to lease certain land and buildings at a rental of approximately RMB 2,557 million and RMB 568 million, respectively, per annum. The Company and Sinopec Group Company can renegotiate the rental amount every three years for land and every year for buildings, such amount not to exceed the market price as determined by an independent third party. The Group has the option to terminate these leases upon six months notice to Sinopec Group Company.

(d) The Company has entered into agreements with Sinopec Group Company effective from 1 January 2000 under which the Group has been granted the right to use certain trademarks, patents, technology and computer software developed by Sinopec Group Company. The Group will reimburse Sinopec Group Company for fees required to maintain the validity of these licenses.

(e) The Company has entered into a service station franchise agreement with Sinopec Group Company under which its service station and retail stores would exclusively sell the refined products supplied by the Group.

(d) Balances with related parties

The balances with the Group’s related parties at 31 December 2005 and 2004 are as follows:

	The ultimate holding company		Other related companies	
	2005	2004	2005	2004
	RMB millions	RMB millions	RMB millions	RMB millions
Cash and cash equivalent	—	—	4,589	4,671
Trade accounts receivable	—	—	4,126	2,438
Advance payments and other receivables	1,507	2,502	1,986	3,391
Trade accounts payable	—	—	3,005	1,527
Receipts in advance	—	—	1,726	1,218
Other creditors	986	4,851	4,432	4,828
Short-term loans	—	—	732	6,714
Long-term loans (including current portion) (Note)	—	—	40,033	38,765

Note: The Sinopec Group Company had borrowed an interest free loan for 20 years amounted to RMB 35,561 million to the Group through Sinopec Finance Company Limited which was included in the long-term loans.

## NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2005

### 42 PRINCIPAL SUBSIDIARIES

The Company's principal subsidiaries are limited companies operating in the PRC and had been consolidated into the Group's financial statements for the year ended 31 December 2005. Except for Sinopec Kantons Holdings Limited, which is incorporated in Bermuda, the companies below are incorporated in the PRC. The following list contains only the particulars of subsidiaries which principally affected the results or assets of the Group:

Name of enterprise	Registered capital/paid-up capital RMB millions	Percentage of equity interest held by the Group %	Principal activities
China Petrochemical International Company Limited	1,704	100.00	Trading of crude oil and petrochemical products
Sinopec Beijing Yanshan Petrochemical Company Limited ("Beijing Yanhua") (i)	3,404	100.00	Manufacturing of chemical products
Sinopec Sales Company Limited	1,700	100.00	Marketing and distribution of refined petroleum products
Sinopec Shengli Oilfield Company Limited	29,000	100.00	Exploration and production of crude oil and natural gas
Sinopec Fujian Petrochemical Company Limited (ii)	2,253	50.00	Manufacturing of plastics, intermediate petrochemical products and petroleum products
Sinopec Qilu Petrochemical Company Limited	1,950	82.05	Manufacturing of intermediate petrochemical products and petroleum products
Sinopec Shanghai Petrochemical Company Limited	7,200	55.56	Manufacturing of synthetic fibres, resin and plastics, intermediate petrochemical products and petroleum products
Sinopec Shijiazhuang Refining Chemical Company Limited	1,154	79.73	Manufacturing of intermediate petrochemical products and petroleum products
Sinopec Kantons Holdings Limited	HK\$104	72.40	Trading of crude oil and petroleum products
Sinopec Wuhan Petroleum Group Company Limited (ii)	147	46.25	Marketing and distribution of refined petroleum products
Sinopec Wuhan Phoenix Company Limited (ii)	519	40.72	Manufacturing of petrochemical products and petroleum products
Sinopec Yangzi Petrochemical Company Limited	2,330	84.98	Manufacturing of intermediate petrochemical products and petroleum products
Sinopec Yizheng Chemical Fibre Company Limited (ii)	4,000	42.00	Production and sale of polyester chips and polyester fibres
Sinopec Zhenhai Refining and Chemical Company Limited	2,524	71.32	Manufacturing of intermediate petrochemical products and petroleum products
Sinopec Zhongyuan Petroleum Company Limited	875	70.85	Exploration and production of crude oil and natural gas
Zhongyuan Petrochemical Company Limited	2,400	93.51	Manufacturing of chemical products
Sinopec Shell (Jiangsu) Petrochemical Marketing Company Limited	830	60.00	Marketing and distribution of refined petroleum products
BP Sinopec (Zhejiang) Petrochemical Company Limited	800	60.00	Marketing and distribution of refined petroleum products
Sinopec Qingdao Refining and Chemical Company Limited	800	85.00	Manufacturing of intermediate petrochemical products and petroleum products

(i) During the year the Group acquired the entire 1,012,000,000 H shares, representing approximately 29.99% of the issued share capital of Beijing Yanhua.

(ii) The Company consolidated the results of these entities because the Company controlled the board of these entities and had the power to govern their financial and operating policies.

## NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2005

### 43 PRINCIPAL JOINTLY CONTROLLED ENTITIES

At 31 December 2005, the Group's and the Company's principal jointly controlled entities are as follows:

Name of jointly controlled entities	Registered capital/paid-up capital	Percentage of equity interest held by the Company	Percentage of equity interest held by the Group's subsidiaries	Principal activities
Shanghai Secco Petrochemical Company Limited	Registered capital USD 901,440,964	30.00	20.00	Manufacturing and distribution of petrochemical products
BASF-YPC Company Limited	Registered capital RMB 8,793,000,000	30.00	10.00	Manufacturing and distribution of petrochemical products
Yueyang Sinopec and Shell Coal Gasification Company Limited	Registered capital USD 45,588,700	50.00	—	Manufacturing and distribution of industrial gas
Block A Oil Field in the Western Area Chengdao in Bohai Bay	—	—	43.00	Exploration and production of crude oil and natural gas

### 44 COMMITMENTS

#### Operating lease commitments

The Group and the Company lease service stations and other equipment through non-cancellable operating leases. These operating leases do not contain provisions for contingent lease rentals. None of the rental agreements contain escalation provisions that may require higher future rental payments.

At 31 December 2005, the future minimum lease payments of the Group and the Company under operating leases are as follows:

	The Group		The Company	
	2005 RMB millions	2004 RMB millions	2005 RMB millions	2004 RMB millions
Within one year	3,593	3,452	3,424	3,272
Between one and two years	3,442	3,343	3,363	3,237
Between two and three years	3,388	3,278	3,319	3,213
Between three and four years	3,357	3,245	3,292	3,188
Between four and five years	3,353	3,225	3,290	3,170
After five years	95,176	97,527	93,601	95,968
<b>Total</b>	<b>112,309</b>	<b>114,070</b>	<b>110,289</b>	<b>112,048</b>

#### Capital commitments

At 31 December 2005, the capital commitments are as follows:

	2005 RMB millions	2004 RMB millions
<b>The Group</b>		
Authorised and contracted for	71,666	43,001
Authorised but not contracted for	84,213	60,173
	<b>155,879</b>	<b>103,174</b>
<b>Jointly controlled entities</b>		
Authorised and contracted for	2,160	3,157
Authorised but not contracted for	60	2,088
	<b>2,220</b>	<b>5,245</b>
<b>The Company</b>		
Authorised and contracted for	55,496	28,143
Authorised but not contracted for	45,938	37,619
	<b>101,434</b>	<b>65,762</b>

These capital commitments relate to oil and gas exploration and development, refining and petrochemical production capacity expansion projects, the construction of service stations and oil depots, and capital contributions to the Group's investments and interests in associates.

## NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2005

### 44 COMMITMENTS (Continued)

#### Exploration and production licenses

Exploration licenses for exploration activities are registered with the Ministry of Land and Resources. The maximum term of the Group's exploration licenses is 7 years, and may be renewed twice within 30 days prior to expiration of the original term with each renewal being for a two-year term. The Group is obligated to make progressive annual minimum exploration investment relating to the exploration blocks in respect of which the license is issued. The Ministry of Land and Resources also issues production licenses to the Group on the basis of the reserve reports approved by relevant authorities. The maximum term of a full production license is 30 years unless a special dispensation was given by the State Council. The maximum term of the production licenses issued to the Group is 55 years as a special dispensation was given by the State Council. The Group's production license is renewable upon application by the Group 30 days prior to expiration.

The Group is required to make payments of exploration license fees and production right usage fees to the Ministry of Land and Resources annually which are expensed as incurred. Payments incurred were approximately RMB 208 million for the year ended 31 December 2005 (2004: RMB 189 million).

Estimated future annual payments are as follows:

	The Group		The Company	
	2005	2004	2005	2004
	RMB millions	RMB millions	RMB millions	RMB millions
Within one year	107	90	74	60
Between one and two years	112	120	81	85
Between two and three years	59	75	49	47
Between three and four years	67	67	58	55
Between four and five years	56	74	49	64
After five years	239	279	108	143
<b>Total</b>	<b>640</b>	<b>705</b>	<b>419</b>	<b>454</b>

### 45 CONTINGENT LIABILITIES

(a) The Company has been advised by its PRC lawyers that, except for liabilities constituting or arising out of or relating to the business assumed by the Company in the Reorganisation, no other liabilities were assumed by the Company, and the Company is not jointly and severally liable for other debts and obligations incurred by Sinopec Group Company prior to the Reorganisation.

(b) At 31 December 2005, guarantees given by the Group and the Company to banks in respect of banking facilities granted to the parties below are as follows:

	The Group		The Company	
	2005	2004	2005	2004
	RMB millions	RMB millions	RMB millions	RMB millions
Subsidiaries	—	—	2,583	2,656
Associates and jointly controlled entities	79	4,828	11,986	12,059
<b>Total</b>	<b>79</b>	<b>4,828</b>	<b>14,569</b>	<b>14,715</b>

The Company monitors the conditions that are subject to the guarantees to identify whether it is probable that a loss has occurred, and recognises any such losses under guarantees when those losses are estimable. At 31 December 2005 and 2004, it is not probable that the Company will be required to make payments under the guarantees. Thus no liability has been accrued for a loss related to the Company's obligation under the guarantees arrangement.

#### Environmental contingencies

To date, the Group has not incurred any significant expenditure for environmental remediation, is currently not involved in any environmental remediation, and has not accrued any amounts for environmental remediation relating to its operations. Under existing legislation, management believes that there are no probable liabilities that will have a material adverse effect on the financial position or operating results of the Group. The PRC government, however, has moved and may move further towards more rigorous enforcement of applicable laws, and towards the adoption of more stringent environmental standards. Environmental liabilities are subject to considerable uncertainties which affect the Group's ability to estimate the ultimate cost of remediation efforts. These uncertainties include: i) the exact nature and extent of the contamination at various sites including, but not limited to refineries, oil fields, service stations, terminals and land development areas, whether operating, closed or sold; ii) the extent of required cleanup efforts; iii) varying costs of alternative remediation strategies; iv) changes in environmental remediation requirements; and v) the identification of new remediation sites. The amount of such future cost is indeterminable due to such factors as the unknown magnitude of possible contamination and the unknown timing and extent of the corrective actions that may be required. Accordingly, the outcome of environmental liabilities under proposed or future environmental legislation cannot reasonably be estimated at present, and could be material. The Group paid normal routine pollutant discharge fee of approximately RMB 493 million for the year ended 31 December 2005 (2004: RMB 248 million).

#### Legal contingencies

The Group is a defendant in certain lawsuits as well as the named party in other proceedings arising in the ordinary course of business. While the outcomes of such contingencies, lawsuits or other proceedings cannot be determined at present, management is of the opinion that any resulting liabilities will not have a material adverse effect on the financial position or operating results of the Group.

## NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2005

### 46 SEGMENTAL INFORMATION

The Group has five operating segments as follows:

- (i) Exploration and production – which explores and develops oil fields, produces crude oil and natural gas and sells such products to the refining segment of the Group and external customers.
- (ii) Refining – which processes and purifies crude oil, which is sourced from the exploration and production segment of the Group and external suppliers, and manufactures and sells petroleum products to the chemicals and marketing and distribution segments of the Group and external customers.
- (iii) Marketing and distribution – which owns and operates oil depots and service stations in the PRC, and distributes and sells refined petroleum products (mainly gasoline and diesel) in the PRC through wholesale and retail sales networks.
- (iv) Chemicals – which manufactures and sells petrochemical products, derivative petrochemical products and other chemical products to external customers.
- (v) Others – which largely comprise the trading activities of the import and export companies of the Group and research and development undertaken by other subsidiaries.

The segments were determined primarily because the Group manages its exploration and production, refining, marketing and distribution, chemicals, and others businesses separately. The reportable segments are each managed separately because they manufacture and/or distribute distinct products with different production processes and due to their distinct operating and gross margin characteristics. In view of the fact that the Company and its subsidiaries operate mainly in the PRC, no geographical segment information is presented.

The Group evaluates the performance and allocates resources to its operating segments on an operating income basis, without considering the effects of finance costs or investment income. The accounting policies of the Group's segments are the same as those described in the principal accounting policies (see Note 2). Corporate administrative costs and assets are not allocated to the operating segments; instead, operating segments are billed for direct corporate services. Inter-segment transfer pricing is based on cost plus an appropriate margin, as specified by the Group's policy.

Reportable information on the Group's operating segments is as follows:

	2005	2004
	RMB millions	RMB millions
<b>Income from principal operations</b>		
Exploration and production		
External sales	19,862	16,109
Inter-segment sales	84,423	59,914
	<b>104,285</b>	<b>76,023</b>
Refining		
External sales	82,810	71,333
Inter-segment sales	386,456	281,215
	<b>469,266</b>	<b>352,548</b>
Marketing and distribution		
External sales	459,292	342,840
Inter-segment sales	3,172	2,831
	<b>462,464</b>	<b>345,671</b>
Chemicals		
External sales	160,783	112,078
Inter-segment sales	12,199	10,040
	<b>172,982</b>	<b>122,118</b>
Others		
External sales	76,368	48,272
Inter-segment sales	44,897	30,873
	<b>121,265</b>	<b>79,145</b>
Elimination of inter-segment sales	(531,147)	(384,873)
<b>Income from principal operations</b>	<b>799,115</b>	<b>590,632</b>
<b>Cost of sales, sales taxes and surcharges</b>		
Exploration and production	40,118	36,073
Refining	477,843	340,360
Marketing and distribution	427,308	306,309
Chemicals	149,431	96,994
Others	118,152	78,410
Elimination of inter-segment cost of sales	(527,451)	(382,736)
<b>Cost of sales, sales taxes and surcharges</b>	<b>685,401</b>	<b>475,410</b>
<b>Profit from principal operations</b>		
Exploration and production	59,732	37,997
Refining	(7,838)	12,005
Marketing and distribution	35,156	39,362
Chemicals	23,551	25,123
Others	3,113	735
<b>Profit from principal operations</b>	<b>113,714</b>	<b>115,222</b>

## NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2005

### 47 POST BALANCE SHEET EVENTS

On 12 November 2005, the Group announced its proposal to privatise Sinopec Zhenhai Refining & Chemical Company Limited (“Zhenhai”), a non-wholly owned subsidiary in which the Group holds approximately 71.3% of the equity interests. According to the proposal, the Group will acquire the entire 723,754,468 H shares, representing approximately 28.7% of the issued share capital of Zhenhai at HK\$ 10.60 per share. The total consideration required to be paid by the Group is approximately HK\$ 7,762 million which will be settled in cash. Pursuant to the resolution passed in the Special General Meeting of Zhenhai on 12 January 2006, the shareholders of H shares in Zhenhai agreed to dispose of and sell their shares in Zhenhai to the Group at the above mentioned price.

On 15 February 2006, the Group announced its proposals of voluntary general offers for Sinopec Qilu Petrochemical Company Limited, Sinopec Yangzi Petrochemical Company Limited, Sinopec Zhongyuan Petroleum Company Limited and Sinopec Shengli Oilfield Dynamic Company Limited, being non-wholly owned subsidiaries and an associate in which the Group holds approximately 82%, 85%, 71% and 26% of the equity interests, respectively. According to the proposals, the Group will acquire the entire shares not held by the Group in Sinopec Qilu Petrochemical Company Limited, Sinopec Yangzi Petrochemical Company Limited, Sinopec Zhongyuan Petroleum Company Limited and Sinopec Shengli Oilfield Dynamic Company Limited. The acquisitions have been approved by the relevant PRC governmental and regulatory bodies on 6 March 2006. The total consideration required to be paid by the Group is approximately RMB 14,247 million which will be settled in cash.

### 48 EXTRAORDINARY GAINS AND LOSSES

Pursuant to “Questions and answers in the prepayment of information disclosures of companies issuing public shares, No.1 — Extraordinary gains and losses” (2004 revised), the extraordinary gains and losses of the Group are as follows:

	2005	2004
	RMB millions	RMB millions
<b>Extraordinary gains and losses for the year:</b>		
Loss on disposal of fixed assets	2,422	4,304
Employee reduction expenses	369	919
Donations	203	275
Gain on disposal of long-term equity investments	(25)	(2)
Other non-operating income and expenses, excluding impairment losses on long-lived assets	757	380
Written back of provisions for impairment losses in previous years	(1,115)	(322)
Subsidy income	(9,415)	—
Tax effect	2,245	(1,833)
<b>Total</b>	<b>(4,559)</b>	<b>3,721</b>

### 49 OTHER SIGNIFICANT EVENTS

The Group had no any other significant event required to disclose as at the approval date of these financial statements.