

NOTES ON THE FINANCIAL STATEMENTS

for the year ended 31 December 2006

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.

The Company and its subsidiaries (the “Group”) engage in the oil and gas and chemical operations and businesses, including:

- (1) the exploration, development and production of crude oil and natural gas;
- (2) the refining, transportation, storage and marketing of crude oil and petroleum products, and
- (3) the production and sale of chemicals.

Pursuant to the resolution passed at the Directors’ meeting on 10 October 2006, the Company acquired equity interests in Sinopec Hainan Refining and Chemical Company Limited (“Sinopec Hainan”) by way of capital injection of RMB 2,990 million (hereinafter referred to as the “Acquisition of Sinopec Hainan”). Upon the completion of the capital increase, the Company will hold 75% of the equity interests in Sinopec Hainan.

Pursuant to the resolution passed at the Directors’ meeting on 6 December 2006, the Company acquired the equity interests in certain oil and gas companies (“Oil Production Plants”) from Sinopec Group Company, for a total consideration of RMB 3,500 million (hereinafter referred to as the “Acquisition of Oil Production Plants”).

2 SIGNIFICANT ACCOUNTING POLICIES

The significant accounting policies adopted by 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 “Provisional regulations on consolidated financial statements” Cai Kuai Zi [1995] No.11 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.

All income statement items of overseas subsidiaries are translated into Renminbi at the annual average PBOC rates. The asset and liability items are translated into Renminbi at the PBOC rates at the balance sheet date. The equity items, excluding the item of "Retained Profit", are translated into Renminbi on the transaction 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.

Cost includes the cost of purchase and processing, and other cost. 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 life	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.

The premium/discount on debentures is amortised on a straight-line basis, over the period from the issue date to the maturity date.

(n) Revenue recognition

Revenue is recognised only when it is probable that economic benefits will flow to the enterprises, and the amount of the inflow of economic benefits can be measured reliably. Revenue is recognised according to the following measures:

(i) Revenues from sales of goods

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.

(ii) Revenues from rendering services

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.

(iii) Interest Income

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 (including overhauling expenses) 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 2006

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, value added tax and special oil income levy.

Income tax rate is 33% and that of certain 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. Effective from 1 April 2006, the Ministry of Finance prescribed new tax rates on refined oil products. New tax rates levied upon naphtha, solvent oil, lubricant oil, fuel oil and jet fuel oil were RMB 277.0 per tonne, RMB 256.4 per tonne, RMB 225.2 per tonne, RMB 101.5 per tonne and RMB 124.6 per tonne respectively. The consumption tax on jet fuel oil is temporarily exempted while others are temporarily imposed on 30% of the taxable amounts.

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 metre respectively. Since 1 July 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 metre respectively.

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

With effective from 26 March 2006, the Ministry of Finance imposed a special oil income levy on any income derived from the sale by an oil exploration and production enterprise of locally produced crude oil exceeding a standard price. The levy starts at USD 40 per barrel and the imposed rate ranges from 20% to 40%.

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 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
Sinopec Hainan Refining and Chemical Company Limited	2-year exemption and 3-year 50% reduction	Foreign investment enterprise

4 CASH AT BANK AND IN HAND

The Group

	2006			2005		
	Original currency millions	Exchange rates	RMB millions	Original currency millions	Exchange rates	RMB millions
Cash in hand						
Renminbi			15			207
Cash at bank						
Renminbi			7,192			9,229
US Dollars	97	7.8087	760	76	8.0702	616
Hong Kong Dollars	27	1.0047	27	63	1.0403	66
Japanese Yen	259	0.0656	17	277	0.0687	19
Euro	2	10.2665	23	2	9.5797	21
			8,034			10,158
Deposits at related parties						
Renminbi			688			4,588
US Dollars	—	7.8087	1	—	8.0702	1
Total cash at bank and in hand			8,723			14,747

NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2006

4 CASH AT BANK AND IN HAND (Continued)

The Company

	Original currency millions	2006		Original currency millions	2005	
		Exchange rates	RMB millions		Exchange rates	RMB millions
Cash in hand						
Renminbi			5			12
Cash at bank						
Renminbi			2,745			3,075
US Dollars	—	7.8087	1	1	8.0702	10
			2,751			3,097
Deposits at related parties						
Renminbi			231			2,026
US Dollars	—	7.8087	1	—	8.0702	1
Total cash at bank and in hand			2,983			5,124

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

As at 31 December 2006, time deposits with financial institutions of the Group and the Company amounted to RMB 635 million (2005: RMB 1,002 million) and RMB 220 million (2005: RMB 110 million), respectively.

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	
	2006 RMB millions	2005 RMB millions	2006 RMB millions	2005 RMB millions
Amounts due from subsidiaries	—	—	5,570	6,252
Amounts due from Sinopec Group Company and fellow subsidiaries	3,396	3,049	923	518
Amounts due from associates	380	572	8	10
Amounts due from jointly controlled entities	547	505	377	229
Amounts due from others	14,601	13,546	4,622	4,136
	18,924	17,672	11,500	11,145
Less: Allowance for doubtful accounts	3,334	3,140	2,668	2,319
Total	15,590	14,532	8,832	8,826

Allowance for doubtful accounts is analysed as follows:

	The Group		The Company	
	2006 RMB millions	2005 RMB millions	2006 RMB millions	2005 RMB millions
Balance at 1 January	3,140	3,671	2,319	2,837
Provision for the year	438	328	261	186
Written back for the year	(153)	(503)	(128)	(424)
Written off for the year	(91)	(356)	(78)	(280)
Transferred from subsidiaries	—	—	294	—
Balance at 31 December	3,334	3,140	2,668	2,319

Ageing analysis on trade accounts receivable is as follows:

	The Group				The Company			
	2006		2005		2006		2005	
	Amount RMB millions	Allowance % RMB millions						
Within one year	15,432	81.5	94	0.6	14,320	81.0	49	0.3
Between one and two years	295	1.6	126	42.7	279	1.6	101	36.2
Between two and three years	242	1.3	186	76.9	158	0.9	115	72.8
Over three years	2,955	15.6	2,928	99.1	2,915	16.5	2,875	98.6
Total	18,924	100.0	3,334		17,672	100.0	3,140	

NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2006

6 TRADE ACCOUNTS RECEIVABLE (Continued)

	The Company									
	2006					2005				
	Amount RMB millions	%	Allowance RMB millions	%	Amount RMB millions	%	Allowance RMB millions	%		
Within one year	8,655	75.3	47	0.5	8,721	78.1	45	0.5		
Between one and two years	219	1.9	61	27.9	164	1.5	52	31.7		
Between two and three years	144	1.3	101	70.1	95	0.9	70	73.7		
Over three years	2,482	21.5	2,459	99.1	2,165	19.5	2,152	99.4		
Total	11,500	100.0	2,668		11,145	100.0	2,319			

Major trade accounts receivable of the Group at 31 December 2006 are set out below:

Name of debtor	Balance RMB millions	Percentage on trade accounts receivable %
Heilongjiang Union Oil and Chemicals Company Limited	913	4.8
North Petroleum International Company Limited	828	4.4
Shell International Eastern Trading Company	699	3.7
Petroleo Brasileiro S.A.	481	2.5
BP Singapore Pte. Limited	453	2.4

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

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 2006 and 2005, the Group and the Company had no individually significant trade accounts receivable been fully or substantially provided for.

During the years ended 31 December 2006 and 2005, 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 2006 and 2005, the Group and the Company had no individually significant trade accounts receivable that aged over three years.

7 OTHER RECEIVABLES

	The Group		The Company	
	2006 RMB millions	2005 RMB millions	2006 RMB millions	2005 RMB millions
Amounts due from subsidiaries	—	—	3,592	1,740
Amounts due from Sinopec Group Company and fellow subsidiaries	2,102	3,059	1,784	2,708
Amounts due from associates	306	521	284	501
Amounts due from others	11,659	11,419	6,501	7,855
	14,067	14,999	12,161	12,804
Less: Allowance for doubtful accounts	3,470	3,512	3,699	3,200
Total	10,597	11,487	8,462	9,604

Allowance for doubtful accounts is analysed as follows:

	The Group		The Company	
	2006 RMB millions	2005 RMB millions	2006 RMB millions	2005 RMB millions
Balance at 1 January	3,512	3,496	3,200	3,423
Provision for the year	107	446	80	176
Written back for the year	(113)	(415)	(81)	(386)
Written off for the year	(36)	(15)	(31)	(13)
Transferred from subsidiaries	—	—	531	—
Balance at 31 December	3,470	3,512	3,699	3,200

NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2006

7 OTHER RECEIVABLES (Continued)

Ageing analysis of other receivables is as follows:

	The Group							
	2006				2005			
	Amount RMB millions	%	Allowance RMB millions	%	Amount RMB millions	%	Allowance RMB millions	%
Within one year	7,250	51.5	25	0.3	9,167	61.1	15	0.2
Between one and two years	1,747	12.4	49	2.8	676	4.5	33	4.9
Between two and three years	397	2.9	296	74.6	447	3.0	338	75.6
Over three years	4,673	33.2	3,100	66.3	4,709	31.4	3,126	66.4
Total	14,067	100.0	3,470		14,999	100.0	3,512	

	The Company							
	2006				2005			
	Amount RMB millions	%	Allowance RMB millions	%	Amount RMB millions	%	Allowance RMB millions	%
Within one year	6,171	50.7	9	0.1	7,127	55.7	5	0.1
Between one and two years	566	4.7	31	5.5	491	3.8	19	3.9
Between two and three years	254	2.1	41	16.1	748	5.8	622	83.1
Over three years	5,170	42.5	3,618	70.0	4,438	34.7	2,554	57.5
Total	12,161	100.0	3,699		12,804	100.0	3,200	

Major other receivables of the Group at 31 December 2006 are set out below:

Name of debtor	Particulars	Balance RMB millions	Percentage on other receivables %
China Petrochemical Company	Current Account	806	5.7
Land Development Center of Quangang District, Quanzhou	Current Account	417	3.0
Qingdao Huacheng Petro Chemical Property Development Co. Ltd.	Current Account	288	2.0
Ningbo Taiyi Real Estate Company Limited	Current Account	192	1.4
CPC Ningbo Construction Co., Ltd	Current Account	182	1.3

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

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 2006 and 2005, the Group and the Company had no individually significant other receivables been fully or substantially provided for.

During the years ended 31 December 2006 and 2005, 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 2006 and 2005, except for the current account with China Petrochemical Company, 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.

NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2006

9 INVENTORIES

	The Group		The Company	
	2006	2005	2006	2005
	RMB millions	RMB millions	RMB millions	RMB millions
Raw materials	54,245	53,350	28,972	25,471
Work in progress	9,828	9,422	5,061	4,659
Finished goods	25,762	23,163	17,574	17,980
Spare parts and consumables	4,072	3,893	2,454	2,061
	93,907	89,828	54,061	50,171
Less: Provision for diminution in value of inventories	866	892	469	309
	93,041	88,936	53,592	49,862

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	
	2006	2005	2006	2005
	RMB millions	RMB millions	RMB millions	RMB millions
Balance at 1 January	892	906	309	394
Provision for the year	419	262	154	64
Written back for the year	(317)	(180)	(41)	(81)
Written off	(128)	(96)	(59)	(68)
Transferred from subsidiaries	—	—	106	—
Balance at 31 December	866	892	469	309

The cost of inventories recognised as costs and expenses by the Group and the Company amounted to RMB 898,465 million (2005: RMB 683,375 million) and RMB 675,493 million (2005: RMB 488,592 million) for the year ended 31 December 2006, respectively.

10 LONG-TERM EQUITY INVESTMENTS

The Group

	Listed stock investment	Unlisted stock and other equity investment	Equity investment differences	Provision for impairment losses	Total
	RMB millions	RMB millions	RMB millions	RMB millions	RMB millions
Balance at 1 January 2006	823	11,647	2,003	(327)	14,146
Addition for the year	—	2,606	12,493	—	15,099
Share of profits less losses from investments accounted for under the equity method	25	922	—	—	947
Long-term equity investments accounted for as a subsidiary	(494)	—	—	—	(494)
Dividends receivable/received	(11)	(332)	—	—	(343)
Disposal for the year	—	(709)	(16)	—	(725)
Amortisation for the year	—	—	(1,158)	—	(1,158)
Movement of provision for impairment losses	—	—	—	11	11
Balance at 31 December 2006	343	14,134	13,322	(316)	27,483

The Company

	Listed stock investment	Unlisted stock and other equity investment	Equity investment differences	Provision for impairment losses	Total
	RMB millions	RMB millions	RMB millions	RMB millions	RMB millions
Balance at 1 January 2006	48,564	82,725	2,017	(103)	133,203
Addition for the year	—	21,512	12,470	—	33,982
Reclassification	(32,817)	32,817	—	—	—
Share of profits less losses from investments accounted for under the equity method	(771)	17,048	—	—	16,277
Dividends receivable/received	(445)	(2,303)	—	—	(2,748)
Disposal for the year	—	(169)	(14)	—	(183)
Acquired equity interests in subsidiaries (Note)	—	(50,259)	—	—	(50,259)
Amortisation for the year	—	—	(1,162)	—	(1,162)
Movement of provision for impairment losses	—	—	—	(9)	(9)
Balance at 31 December 2006	14,531	101,371	13,311	(112)	129,101

Note: During the year ended 31 December 2006, the Company acquired all the assets and liabilities of Sinopec Shengli Oilfield Company Limited, Sinopec Beijing Yanhua Petrochemical Company Limited ("Beijing Yanhua") and Sinopec Zhenhai Refining and Chemical Company Limited ("Sinopec Zhenhai"). The above companies no longer existed as at 31 December 2006.

NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2006

10 LONG-TERM EQUITY INVESTMENTS (Continued)

Provision for impairment losses is analysed as follows:

	The Group		The Company	
	2006	2005	2006	2005
	RMB millions	RMB millions	RMB millions	RMB millions
Balance at 1 January	327	353	103	155
Addition for the year	48	77	20	14
Written back for the year	—	(17)	—	—
Written off	(59)	(86)	(11)	(66)
Balance at 31 December	316	327	112	103

At 31 December 2006 and 2005, 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 natural 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.

At 31 December 2006, 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	Balance at 1	Shares of profits	Dividends receivable/ received	Balance at 31
				investment cost	January 2006	accounted for under the equity method		December 2006
				RMB millions	RMB millions	RMB millions	RMB millions	RMB millions
Sinopec Shandong Taishan Petroleum Co Ltd	Legal person shares	186	38.68%	124	329	25	(11)	343

At 31 December 2006, details of principal unlisted stock and other equity investment of the Group (including associates) are as follows:

Name of investee enterprise	Initial investment cost	Investment period	Percentage of equity interest held by the Group	Balance at 1	Addition	Share of profits	Dividends receivable/ received	Balance at 31
				January 2006	for the year	accounted for under the equity method		December 2006
	RMB millions			RMB millions	RMB millions	RMB millions	RMB millions	RMB millions
Sinopec Finance Company Limited (i) (ii)	2,712	—	49%	1,517	1,507	235	—	3,259
China Aviation Oil Supply Company Limited (ii)	1,102	—	29%	1,102	—	53	—	1,155
Shanghai Petroleum National Gas Corporation (i) (ii)	300	—	30%	958	—	236	(180)	1,014
Shanghai Chemical Industry Park Development Company Limited (ii)	608	—	38%	659	—	4	(2)	661
China Shipping & Sinopec Suppliers Company Limited (ii)	438	—	50%	509	—	15	—	524
Qingdao Shihua Crude Oil Terminal Co Ltd (i) (ii)	346	30 years	50%	—	346	—	—	346
Sinopec Changjiang Fuel Company Limited (ii)	190	20 years	50%	253	—	56	(34)	275
Hunan Highway Industrial Development Company Limited (i) (ii)	215	—	49%	221	—	4	(5)	220
Beijing International Trust and Investment Company Limited	200	—	8%	200	—	—	—	200
Zhejiang Express Petroleum Development Company Limited (i) (ii)	174	30 years	50%	177	—	(7)	(13)	157
China Gas Holdings Ltd	136	—	11%	136	—	—	—	136
Sinopec Railway Oil Marketing Company Limited (ii)	74	20 years	50%	126	—	46	(32)	140

(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 2006, the Group's and the Company's proportion of the total investments to the net assets was 11% (2005: 7%) and 50% (2005: 61%), respectively.

At 31 December 2006, the Group's and the Company's equity investment differences represent mainly the equity investment differences resulting from the acquisitions of the minority interests of Beijing Yanhua, Sinopec Zhenhai Refining and Chemical Company Limited, Sinopec Qilu Petrochemical Company Limited, Sinopec Yangzi Petrochemical Company Limited, Sinopec Zhongyuan Petroleum Company Limited, and Sinopec Shengli Oilfield Dynamic Company Limited. The equity investment differences are amortised on a straight-line basis over 10 years. The carrying values of the equity investment differences as at 31 December 2006 are RMB 11,851 million.

NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2006

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
Cost/valuation:						
Balance at 1 January 2006	189,126	122,009	76,673	180,183	4,474	572,465
Addition for the year	249	145	1,280	280	456	2,410
Transferred from construction in progress	26,504	26,849	9,707	15,792	161	79,013
Acquisition of a subsidiary	10,621	16	—	—	—	10,637
Reclassification	(56)	(600)	—	725	(69)	—
Disposals	(5,448)	(1,527)	(2,280)	(4,428)	(153)	(13,836)
Balance at 31 December 2006	220,996	146,892	85,380	192,552	4,869	650,689
Accumulated depreciation:						
Balance at 1 January 2006	94,741	61,160	13,476	94,685	1,549	265,611
Depreciation charge for the year	12,759	7,635	3,371	9,440	422	33,627
Acquisition of a subsidiary	2,330	3	—	—	—	2,333
Reclassification	(23)	(392)	—	420	(5)	—
Written back on disposal	(5,143)	(1,315)	(961)	(2,893)	(108)	(10,420)
Balance at 31 December 2006	104,664	67,091	15,886	101,652	1,858	291,151
Net book value:						
Balance at 31 December 2006	116,332	79,801	69,494	90,900	3,011	359,538
Balance at 31 December 2005	94,385	60,849	63,197	85,498	2,925	306,854

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
Cost/valuation:						
Balance at 1 January 2006	72,478	91,960	67,548	58,840	3,380	294,206
Addition for the year	192	109	1,276	7	11	1,595
Transferred from construction in progress	25,317	14,920	7,735	11,717	52	59,741
Transferred from subsidiaries	107,949	2,702	—	15,761	—	126,412
Transferred to subsidiaries	—	—	(746)	—	—	(746)
Reclassification	(56)	(600)	—	725	(69)	—
Disposals	(5,313)	(1,242)	(2,158)	(1,723)	(105)	(10,541)
Balance at 31 December 2006	200,567	107,849	73,655	85,327	3,269	470,667
Accumulated depreciation:						
Balance at 1 January 2006	29,346	46,261	12,809	34,263	1,068	123,747
Depreciation charge for the year	12,011	5,702	3,031	3,843	235	24,822
Transferred from subsidiaries	60,961	1,470	—	9,356	—	71,787
Transferred to subsidiaries	—	—	(74)	—	—	(74)
Reclassification	(23)	(395)	—	423	(5)	—
Written back on disposal	(5,091)	(1,083)	(908)	(1,230)	(71)	(8,383)
Balance at 31 December 2006	97,204	51,955	14,858	46,655	1,227	211,899
Net book value:						
Balance at 31 December 2006	103,363	55,894	58,797	38,672	2,042	258,768
Balance at 31 December 2005	43,132	45,699	54,739	24,577	2,312	170,459

NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2006

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
Cost/valuation:					
Balance at 1 January 2006	49,318	169,941	72,217	280,989	572,465
Addition for the year	668	—	1,071	671	2,410
Transferred from construction in progress	2,674	24,554	14,169	37,616	79,013
Acquisition of a subsidiary	1,053	8,990	—	594	10,637
Reclassification	(1,569)	10	3,170	(1,611)	—
Disposals	(880)	(5,171)	(1,658)	(6,127)	(13,836)
Balance at 31 December 2006	51,264	198,324	88,969	312,132	650,689
Accumulated depreciation:					
Balance at 1 January 2006	21,130	85,896	12,738	145,847	265,611
Depreciation charge for the year	1,850	12,095	3,692	15,990	33,627
Acquisition of a subsidiary	103	2,046	—	184	2,333
Reclassification	(495)	(45)	1,072	(532)	—
Written back on disposal	(385)	(4,974)	(747)	(4,314)	(10,420)
Balance at 31 December 2006	22,203	95,018	16,755	157,175	291,151
Net book value:					
Balance at 31 December 2006	29,061	103,306	72,214	154,957	359,538
Balance at 31 December 2005	28,188	84,045	59,479	135,142	306,854

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
Cost/valuation:					
Balance at 1 January 2006	25,278	64,142	64,056	140,730	294,206
Addition for the year	61	—	1,046	488	1,595
Transferred from construction in progress	959	23,683	12,213	22,886	59,741
Transferred from subsidiaries	3,288	101,287	—	21,837	126,412
Transferred to subsidiaries	—	—	(746)	—	(746)
Reclassification	(2,512)	10	2,845	(343)	—
Disposals	(321)	(5,144)	(1,531)	(3,545)	(10,541)
Balance at 31 December 2006	26,753	183,978	77,883	182,053	470,667
Accumulated depreciation:					
Balance at 1 January 2006	10,329	27,358	11,943	74,117	123,747
Depreciation charge for the year	928	11,513	3,095	9,286	24,822
Transferred from subsidiaries	1,054	55,576	—	15,157	71,787
Transferred to subsidiaries	—	—	(74)	—	(74)
Reclassification	(555)	(45)	1,060	(460)	—
Written back on disposal	(217)	(4,948)	(696)	(2,522)	(8,383)
Balance at 31 December 2006	11,539	89,454	15,328	95,578	211,899
Net book value:					
Balance at 31 December 2006	15,214	94,524	62,555	86,475	258,768
Balance at 31 December 2005	14,949	36,784	52,113	66,613	170,459

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.

In connection with the acquisitions of certain entities and related operations from Sinopec Group Company in prior years, the related fixed assets were revalued by independent valuers in accordance with relevant PRC rules and regulations. Surplus on these revaluations of RMB 1,029 million has been incorporated in the Group's financial statements.

In connection with the Acquisition of Oil Production Plants, the fixed assets and construction of progress of the Oil Production Plants were revalued by a firm of independent valuers in accordance with the relevant PRC rules and regulations. The value of the fixed assets and construction of progress of the Oil Production Plants pursuant to the valuation approximated the net historical carrying value of the assets.

At 31 December 2006, the carrying amounts of fixed assets that were pledged by the Group and the Company were RMB 288 million (2005: RMB 83 million) and RMB 75 million (2005: RMB 10 million), respectively.

NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2006

11 FIXED ASSETS (Continued)

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
Balance at 1 January 2006	843	11	1,270	4,110	6,234
Addition for the year	327	—	23	250	600
Written off for the year	(53)	—	(142)	(614)	(809)
Balance at 31 December 2006	1,117	11	1,151	3,746	6,025

The Company – by segment

	Exploration and production RMB millions	Refining RMB millions	Marketing and distribution RMB millions	Chemicals RMB millions	Total RMB millions
Balance at 1 January 2006	780	11	1,241	2,159	4,191
Addition for the year	308	—	23	200	531
Transferred from subsidiaries	—	2	—	—	2
Written off for the year	(53)	—	(142)	(155)	(350)
Balance at 31 December 2006	1,035	13	1,122	2,204	4,374

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
Balance at 1 January 2006	351	843	917	4,123	6,234
Addition for the year	118	307	23	152	600
Reclassification	143	—	149	(292)	—
Written off for the year	(90)	(52)	(87)	(580)	(809)
Balance at 31 December 2006	522	1,098	1,002	3,403	6,025

The Company – 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
Balance at 1 January 2006	154	780	935	2,322	4,191
Addition for the year	118	307	23	83	531
Transferred from subsidiaries	2	—	—	—	2
Reclassification	143	—	149	(292)	—
Written off for the year	(13)	(52)	(87)	(198)	(350)
Balance at 31 December 2006	404	1,035	1,020	1,915	4,374

The factors resulting in the exploration and production segment of the Group provision for impairment losses of RMB 327 million (2005: RMB 60 million) for the year ended 31 December 2006 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.

Provision for impairment losses recognised on fixed assets of the chemicals segment of the Group of RMB 250 million (2005: RMB 1,425 million) for the year ended 31 December 2006 relate to certain chemicals production facilities that are held for use. The carrying values of these facilities were written down to their recoverable values that were determined based on the asset held for use model using the present value of estimated future cash flows of the production facilities. 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 23 million (2005: RMB 366 million) for the year ended 31 December 2006 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.

At 31 December 2006 and 2005, the Group and the Company had no individually significant fixed assets which were temporarily idle or pending for disposal.

At 31 December 2006 and 2005, the Group and the Company had no individually significant fully depreciated fixed assets which were still in use.

NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2006

12 CONSTRUCTION MATERIALS

At 31 December 2006 and 2005, 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.

13 CONSTRUCTION IN PROGRESS

The Group

	Exploration and production RMB millions	Refining RMB millions	Marketing and distribution RMB millions	Chemicals RMB millions	Others RMB millions	Total RMB millions
Balance at 1 January 2006	10,884	14,185	9,956	10,902	2,146	48,073
Addition for the year	35,447	21,714	9,902	12,195	1,714	80,972
Addition for the year of jointly controlled entities	91	—	—	138	—	229
Acquisition of a subsidiary	462	5,994	—	—	—	6,456
Dry hole costs written off	(3,960)	—	—	—	—	(3,960)
Transferred to fixed assets	(26,504)	(26,849)	(9,707)	(15,792)	(161)	(79,013)
Balance at 31 December 2006	16,420	15,044	10,151	7,443	3,699	52,757

The interest rates per annum at which borrowing costs were capitalised for the year ended 31 December 2006 by the Group ranged from 3.6% to 6.1% (2005: 3.3% to 6.6%).

The Group's proportionate share of the jointly controlled entities' construction in progress at 31 December 2006 in the exploration and production and the chemicals segments were RMB 2,980 million (2005: RMB 2,888 million) and RMB 603 million (2005: RMB 504 million), respectively.

At 31 December 2006, major construction projects of the Group are as follows:

Project name	Budgeted amount RMB millions	At 1 January 2006 RMB millions	Addition for the year RMB millions	At 31 December 2006 RMB millions	Percentage of completion	Source of funding	Accumulated interest capitalised at 31 December 2006 RMB millions
The Group							
Qingdao Refinery Construction Project	12,499	149	3,002	3,151	25%	Bank loans & self-financing	1
Crude oil transportation and storage project for Tianjing Refinery and Chemistry Incorporation program	22,924	72	2,230	2,302	10%	Bank loans & self-financing	1
10,000,000 tonnes Refinery Plant Reform	2,521	1,029	1,212	2,241	89%	Bank loans & self-financing	41
Sichuan Natural Gas Pipeline Project	25,554	14	1,917	1,931	8%	Self-financing	—
15,000 million cubic per year Natural Gas Capacity Improvement Project	29,059	—	1,883	1,883	6%	Self-financing	—

The Company

	Exploration and production RMB millions	Refining RMB millions	Marketing and distribution RMB millions	Chemicals RMB millions	Others RMB millions	Total RMB millions
Balance at 1 January 2006	7,651	13,202	8,353	7,693	2,038	38,937
Addition for the year	32,487	14,210	8,093	8,236	1,056	64,082
Transferred from subsidiaries	927	34	—	237	—	1,198
Dry hole costs written off	(3,950)	—	—	—	—	(3,950)
Transferred to fixed assets	(25,317)	(14,920)	(7,735)	(11,717)	(52)	(59,741)
Balance at 31 December 2006	11,798	12,526	8,711	4,449	3,042	40,526

The interest rates per annum at which borrowing costs were capitalised for the year ended 31 December 2006 by the Company ranged from 3.6% to 6.1% (2005: 3.3% to 6.6%).

NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2006

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
Cost:					
Balance at 1 January 2006	1,033	2,946	3,163	1,316	8,458
Addition for the year	104	608	—	673	1,385
Balance at 31 December 2006	1,137	3,554	3,163	1,989	9,843
Accumulated Amortisation:					
Balance at 1 January 2006	673	1,156	585	120	2,534
Amortisation charge for the year	72	308	117	136	633
Balance at 31 December 2006	745	1,464	702	256	3,167
Net book value:					
Balance at 31 December 2006	392	2,090	2,461	1,733	6,676
Balance at 31 December 2005	360	1,790	2,578	1,196	5,924

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 2006, the remaining amortisation period of the exploration and production right was 21 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
Cost:					
Balance at 1 January 2006	825	1,318	3,163	971	6,277
Addition for the year	93	608	—	449	1,150
Transferred from subsidiaries	—	208	—	—	208
Balance at 31 December 2006	918	2,134	3,163	1,420	7,635
Accumulated Amortisation:					
Balance at 1 January 2006	586	803	585	65	2,039
Amortisation charge for the year	43	163	117	45	368
Transferred from subsidiaries	—	62	—	—	62
Balance at 31 December 2006	629	1,028	702	110	2,469
Net book value:					
Balance at 31 December 2006	289	1,106	2,461	1,310	5,166
Balance at 31 December 2005	239	515	2,578	906	4,238

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 2006, the remaining amortisation period of the exploration and production right was 21 years.

15 LONG-TERM DEFERRED EXPENSES

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

16 DEFERRED TAX ASSETS AND LIABILITIES

	The Group		The Company	
	2006 RMB millions	2005 RMB millions	2006 RMB millions	2005 RMB millions
<i>Current</i>				
Provisions, primarily for receivables and inventories	3,526	3,444	3,334	1,226
Accruals	865	456	814	409
<i>Non-current</i>				
Fixed assets	2,220	1,642	1,674	1,553
Tax value of losses carried forward	53	128	—	—
Others	46	31	17	15
Deferred tax assets	6,710	5,701	5,839	3,203

NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2006

17 SHORT-TERM LOANS

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

	The Group		The Company	
	2006	2005	2006	2005
	RMB millions	RMB millions	RMB millions	RMB millions
Short-term bank loans	25,666	15,392	15,045	3,094
Loans from Sinopec Group Company and fellow subsidiaries	4,849	732	806	3,846
Total	30,515	16,124	15,851	6,940

The Group's and the Company's weighted average interest rates per annum on short-term loans were 5.2% (2005: 4.0%) and 4.7% (2005: 3.2%) respectively at 31 December 2006. 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 2006 and 2005, 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			
	2006		2005	
	RMB millions	%	RMB millions	%
Within 3 months	35,580	68.3	40,932	77.3
Between 3 and 6 months	14,850	28.4	10,542	19.9
Over 6 months	1,695	3.3	1,493	2.8
Total	52,125	100.0	52,967	100.0

	The Company			
	2006		2005	
	RMB millions	%	RMB millions	%
Within 3 months	24,066	63.3	22,129	76.7
Between 3 and 6 months	12,485	32.8	5,792	20.1
Over 6 months	1,490	3.9	912	3.2
Total	38,041	100.0	28,833	100.0

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 2006 and 2005, the Group and the Company had no individually significant trade accounts payable aged over three years.

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 2006 and 2005, the Group and the Company had no individually significant receipts in advance aged over one year.

NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2006

21 TAXES PAYABLE

	The Group		The Company	
	2006	2005	2006	2005
	RMB millions	RMB millions	RMB millions	RMB millions
Value added tax	(859)	(2,240)	(591)	(1,796)
Consumption tax	1,744	1,348	1,362	1,031
Income tax	9,176	5,029	7,162	2,494
Business tax	88	45	81	25
Other taxes	1,199	1,080	757	321
Total	11,348	5,262	8,771	2,075

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 2006 and 2005, 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 2006 and 2005, the Group's and the Company's other payables primarily represented payables for special oil income levy, resources compensation fee and education surcharge.

23 OTHER CREDITORS

At 31 December 2006 and 2005, 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 2006 and 2005, the Group and the Company had no individually significant other creditors aged over three years.

24 ACCRUED EXPENSES

At 31 December 2006 and 2005, 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	
	2006	2005	2006	2005
	RMB millions	RMB millions	RMB millions	RMB millions
Long-term bank loans				
— Renminbi loans	13,909	11,952	12,443	9,694
— Japanese Yen loans	526	615	526	615
— US Dollar loans	831	2,206	314	1,710
— Euro loans	25	24	25	24
— Hong Kong Dollar loans	—	82	—	—
	15,291	14,879	13,308	12,043
Long-term bank loans of jointly controlled entities				
— Renminbi loans	183	82	—	—
— US Dollar loans	307	111	—	—
	490	193	—	—
Long-term other loans				
— Renminbi loans	22	22	—	—
— US Dollar loans	5	4	3	1
	27	26	3	1
Long-term loans from Sinopec Group Company and fellow subsidiaries				
— Renminbi loans	552	100	552	100
Total current portion of long-term loans	16,360	15,198	13,863	12,144

At 31 December 2006 and 2005, the Group and the Company had no significant overdue long-term loan.

NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2006

26 LONG-TERM LOANS

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

Interest rate and final maturity	The Group		The Company		
	2006	2005	2006	2005	
	RMB millions	RMB millions	RMB millions	RMB millions	
Third parties debts					
Long-term bank loans					
Renminbi loans	Interest rates ranging from interest free to 6.9% per annum at 31 December 2006 with maturities through 2016	65,484	59,769	55,457	54,792
Japanese Yen loans	Interest rates ranging from 2.6% to 5.8% per annum at 31 December 2006 with maturities through 2024	2,713	3,394	2,713	3,394
US Dollar loans	Interest rates ranging from interest free to 7.4% per annum at 31 December 2006 with maturities through 2031	2,081	5,056	1,192	3,571
Euro loans	Fixed rate at 6.7% per annum at 31 December 2006 with maturities through 2010	101	117	101	117
Hong Kong Dollar loans	Floating rate at Hong Kong Prime Rate plus 0.8% to 1.1% per annum at 31 December 2006 with maturities through 2007, paid off as at 31 December 2006	—	94	—	—
Less: Current portion		15,291	14,879	13,308	12,043
Long-term bank loans		55,088	53,551	46,155	49,831
Long-term bank loans of jointly controlled entities					
Renminbi loans	Floating rate at 90% of PBOC's base lending rate per annum at 31 December 2006 with maturities through 2021	5,019	5,710	—	—
US Dollar loans	Floating rate at London Interbank Offer Rate plus 0.4% to 0.7% per annum at 31 December 2006 with maturities through 2021	3,738	4,296	—	—
Less: Current portion		490	193	—	—
Long-term bank loans of jointly controlled entities		8,267	9,813	—	—
Other long-term loans					
Renminbi loans	Interest rates ranging from interest free to 5.2% per annum at 31 December 2006 with maturities through 2009	3,098	170	3,007	37
US Dollar loans	Interest rates ranging from interest free to 2.0% per annum at 31 December 2006 with maturities through 2015	44	51	30	34
Less: Current portion		27	26	3	1
Other long-term loans		3,115	195	3,034	70
Long-term loans from Sinopec Group Company and fellow subsidiaries					
Renminbi loans	Interest rates ranging from interest free to 5.7% per annum at 31 December 2006 with maturities through 2020	39,572	39,962	39,392	39,312
Less: Current portion		552	100	552	100
Long-term loans from Sinopec Group Company and fellow subsidiaries		39,020	39,862	38,840	39,212
Long-term loans of jointly controlled entities from Sinopec Group Company and fellow subsidiaries					
Renminbi loans	Floating rate at 90% of PBOC's base lending rate applicable to three-year tenor loan per annum at 31 December 2006 with maturities through 2021	75	71	—	—
Long-term loans of jointly controlled entities from Sinopec Group Company and fellow subsidiaries		75	71	—	—
Total		105,565	103,492	88,029	89,113

NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2006

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	
	2006	2005	2006	2005
	RMB millions	RMB millions	RMB millions	RMB millions
Between one and two years	26,529	18,787	24,590	16,420
Between two and five years	36,205	39,142	26,147	34,771
After five years	42,831	45,563	37,292	37,922
Total long-term loans	105,565	103,492	88,029	89,113

At 31 December 2006, the Group and the Company had secured loans from third parties amounting to RMB 171 million (2005: RMB 35 million) and RMB 46 million (2005: RMB 13 million) respectively. At 31 December 2006, the Group had loans secured by long-term investments from third parties amounting to RMB 3,590 million (2005: RMB 3,899 million). 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

	The Group		The Company	
	2006	2005	2006	2005
	RMB millions	RMB millions	RMB millions	RMB millions
Short-term corporate bonds (i)	11,885	9,921	9,885	9,921
Corporate bonds (ii)	3,500	3,500	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.

A subsidiary of the Company issued 270-day corporate bonds of face value at RMB 1 billion to corporate investors in PRC debenture market on 23 February 2006, at a discounted value of RMB 97.78 per RMB 100 par value with an effective yield of 3.07% per annum. The Company redeemed the corporate bonds in November 2006.

The Company issued 183-day corporate bonds of face value at RMB 10 billion to corporate investors in PRC debenture market on 16 May 2006, at a discounted value of RMB 98.68 per RMB 100 par value, with an effective yield of 2.67% per annum. The Company redeemed the corporate bonds in November 2006.

The Company issued 182-day corporate bonds of face value at RMB 10 billion to corporate investors in PRC debenture market on 13 November 2006, at a discounted value of RMB 98.43 per RMB 100 par value, with an effective yield of 3.20% per annum. The bonds mature in May 2007.

A subsidiary of the Company issued 365-day corporate bonds of face value at RMB 2 billion to corporate investors in the PRC debenture market on 11 December 2006 at par value of RMB 100, with an effective yield 3.83% per annum. The bonds mature in December 2007.

(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.

NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2006

29 SHARE CAPITAL

	The Group and the Company	
	2006	2005
	RMB millions	RMB millions
Registered, issued and fully paid:		
69,921,951,000 domestic listed A shares of RMB 1.00 each	69,922	—
16,780,488,000 overseas listed H shares of RMB 1.00 each	16,780	16,780
67,121,951,000 domestic state-owned A shares of RMB 1.00 each	—	67,122
2,800,000,000 domestic listed A shares of RMB 1.00 each	—	2,800
	86,702	86,702

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.

On 25 September 2006, the shareholders of listed A shares accepted the proposal offered by the shareholders of state-owned A shares whereby the shareholders of state-owned A shares agreed to transfer 2.8 state-owned A shares to shareholders of listed A shares for every 10 listed A shares held, in exchange for the approval for the listing of all state-owned A shares. The 784,000,000 state-owned A shares paid to the shareholders of listed A shares were tradable on 10 October 2006. The 66,337,551,000 domestic state-owned A shares have been granted trading right upon settlement of the above consideration.

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.

30 CAPITAL RESERVE

The movements in capital reserve are as follows:

	The Group		The Company	
	2006	2005	2006	2005
	RMB millions	RMB millions	RMB millions	RMB millions
Balance at 1 January	37,121	37,121	37,797	37,797
Gain from debt restructuring by a subsidiary (i)	486	—	486	—
Reserve for equity investment (ii)	—	—	200	—
Balance at 31 December	37,607	37,121	38,483	37,797

The capital reserve represents mainly: (a) the difference between the total amount of the par value of shares issued and the amount of the net assets transferred from Sinopec Group Company in connection with the Reorganisation; and (b) share premiums derived from issuances of H shares and A shares by the Company and excess of cash paid by investors over their proportionate shares in share capital.

- (i) During the year ended 31 December 2006, a subsidiary of the Group reached an agreement with a bank to waive loan principal balance and related interest payable. The gain in connection with the debt restructuring was reflected as an increase of capital reserve.
- (ii) During the year ended 31 December 2006, 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.

NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2006

31 SURPLUS RESERVES

Movements in surplus reserves are as follows:

	The Group and the Company			Total RMB millions
	Statutory surplus reserve RMB millions	Statutory public welfare fund RMB millions	Discretionary surplus reserve RMB millions	
Balance at 1 January 2005	9,558	9,558	7,000	26,116
Appropriation of net profit	3,956	3,956	—	7,912
Balance at 31 December 2005	13,514	13,514	7,000	34,028
Balance at 1 January 2006	13,514	13,514	7,000	34,028
Appropriation of net profit	5,066	—	20,000	25,066
Statutory public welfare fund transferred to statutory surplus reserve (Note)	13,514	(13,514)	—	—
Balance at 31 December 2006	32,094	—	27,000	59,094

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.

Note: According to No.167 of the PRC Company Law commencing from 1 January 2006, the Company is no longer required to make profit appropriation to the statutory public welfare fund. Pursuant to the "Notice on the Accounting Treatment of Business Enterprises In Relation to the Enactment of the Company Law" issued by the Ministry of Finance, the balance of this fund as at 31 December 2005 was transferred to the statutory surplus reserve.

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 2006, revenue from sales to top five customers amounted to RMB 88,354 million (2005: RMB 62,115 million) which accounted for 8% (2005: 8%) of income from principal operations of the Group.

33 SALES TAXES AND SURCHARGES

	The Group		The Company	
	2006 RMB millions	2005 RMB millions	2006 RMB millions	2005 RMB millions
Consumption tax	14,121	12,430	10,425	8,932
Special oil income levy	8,470	—	8,203	—
City construction tax	3,020	2,575	2,276	1,297
Education surcharge	1,604	1,305	1,206	658
Resources tax	818	634	789	201
Business tax	253	208	187	161
Total	28,286	17,152	23,086	11,249

34 FINANCIAL EXPENSES

	The Group		The Company	
	2006 RMB millions	2005 RMB millions	2006 RMB millions	2005 RMB millions
Interest expenses incurred	8,896	7,166	6,266	4,596
Less: Capitalised interest expenses	832	601	477	455
Net interest expenses	8,064	6,565	5,789	4,141
Interest income	(554)	(382)	(234)	(123)
Foreign exchange losses	153	79	111	17
Foreign exchange gains	(934)	(996)	(383)	(496)
Total	6,729	5,266	5,283	3,539

35 EXPLORATION EXPENSES

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

NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2006

36 INVESTMENT INCOME

	The Group		The Company	
	2006	2005	2006	2005
	RMB millions	RMB millions	RMB millions	RMB millions
Investment income accounted for under the cost method	302	255	29	76
Amortisation of equity investment differences	(1,158)	(200)	(1,162)	(201)
Impairment losses of investment	(48)	(77)	(20)	(14)
Investment income accounted for under the equity method	947	835	22,097	51,785
Total	43	813	20,944	51,646

37 SUBSIDY INCOME

The Group received a cash government grant from the Ministry of Finance of the PRC of RMB 5,000 million (2005: RMB 9,415 million) 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 2006. 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	
	2006	2005	2006	2005
	RMB millions	RMB millions	RMB millions	RMB millions
Loss on disposal of fixed assets	1,782	2,422	1,534	1,826
Impairment losses on fixed assets	600	1,851	531	1,082
Fines, penalties and compensation	68	160	62	149
Donations	95	203	75	144
Employee reduction expenses (Note)	236	369	80	119
Others	678	964	463	647
Total	3,459	5,969	2,745	3,967

Note: During the year ended 31 December 2006, in accordance with the Group's voluntary employee reduction plan, the Group recorded employee reduction expenses of RMB 236 million (2005: RMB 369 million) relating to the reduction of approximately 4,000 (2005: 7,000) employees.

39 INCOME TAX

	The Group		The Company	
	2006	2005	2006	2005
	RMB millions	RMB millions	RMB millions	RMB millions
Provision for PRC income tax for the year	23,198	20,159	22,740	17,137
Deferred taxation	(939)	(1,733)	(570)	489
Adjustment for provision for income tax in respect of proceeding year	260	477	240	512
Total	22,519	18,903	22,410	18,138

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 6 April 2007, a final dividend in respect of the year ended 31 December 2006 of RMB 0.11 per share totalling RMB 9,537 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 Board of Directors' meeting on 25 August 2006, an interim dividend for the year ending 31 December 2006 of RMB 0.04 (2005: RMB0.04) per share totalling RMB 3,468 million (2005: RMB3,468 million) was declared.

Pursuant to the shareholders' approval at the Annual General Meeting on 24 May 2006, a final dividend of RMB 0.09 per share totalling RMB 7,803 million in respect of the year ended 31 December 2005 was declared and paid on 30 June 2006.

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 27 June 2005.

NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2006

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 2006.

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

From 1 January 2006 to 26 September 2006	71.23%
From 27 September 2006 to 9 October 2006	76.74%
From 10 October 2006 to 31 December 2006	75.84%

(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
Sinopec Shengli Petroleum Administration Bureau
Sinopec Zhongyuan Petroleum Exploration Bureau
Guangdong Nanhua Petroleum Company Limited
Qingdao Petrochemical Company
Zhanjiang Dongxing Petroleum Corporation Company Limited
Baling Petrochemical Company Limited
Jinling Petrochemical Company Limited
Sinopec Assets Management Corporation

Associates of the Company:

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

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

NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2006

41 RELATED PARTIES AND RELATED PARTY TRANSACTIONS (Continued)

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

	Note	2006 RMB millions	2005 RMB millions
Sales of goods	(i)	129,425	95,123
Purchases	(ii)	60,821	48,454
Transportation and storage	(iii)	1,592	1,959
Exploration and development services	(iv)	22,060	17,001
Production related services	(v)	12,412	10,653
Ancillary and social services	(vi)	1,710	1,790
Operating lease charges	(vii)	3,826	3,213
Agency commission income	(viii)	60	48
Intellectual property license fee paid	(ix)	—	9
Interest received	(x)	52	52
Interest paid	(xi)	1,201	994
Net deposits withdrawn from related parties	(xii)	(3,900)	(82)
Net loans obtained from/(paid to) related parties	(xiii)	3,731	(4,714)

The amounts set out in the table above in respect of the years ended 31 December 2006 and 2005 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 2006 and 2005, 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) Net deposits withdrawn from related parties represent net 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 2006, which is based on monthly average balances, was RMB 47,593 million (2005: RMB 42,518 million).

NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2006

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 2006. 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 3,241 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 2006 and 2005 are as follows:

	The ultimate holding company		Other related companies	
	2006	2005	2006	2005
	RMB millions	RMB millions	RMB millions	RMB millions
Cash and cash equivalent	—	—	689	4,589
Trade accounts receivable	—	—	4,323	4,126
Advance payments and other receivables	806	1,507	1,546	1,986
Trade accounts payable	—	—	2,948	3,005
Receipts in advance	—	—	1,777	1,726
Other creditors	—	986	10,893	4,432
Short-term loans	—	—	4,849	732
Long-term loans (including current portion) (Note)	—	—	39,647	40,033

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.

As discussed in Note 1, pursuant to the resolution passed at the Directors’ meeting on 10 October 2006, the Company acquired equity interests in Sinopec Hainan by way of capital injection of RMB 2,990 million. Upon the completion of the capital increase, the Company will hold 75% of the equity interests in Sinopec Hainan.

As discussed in Note 1, pursuant to the resolution passed at the Directors’ meeting on 6 December 2006, the Company acquired the equity interests of Oil Production Plants from Sinopec Group Company, for a total consideration of RMB 3,500 million.

NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2006

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 2006. 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	1,663	100.00	Trading of petrochemical products
Sinopec Sales Company Limited	1,700	100.00	Marketing and distribution of refined petroleum products
Sinopec Zhenhai Refining and Chemical Company Limited ("Sinopec Zhenhai") (i)	2,524	100.00	Manufacturing of intermediate petrochemical products and petroleum products
Sinopec Qilu Petrochemical Company Limited ("Sinopec Qilu") (ii)	1,950	99.76	Manufacturing of intermediate petrochemical products and petroleum products
Sinopec Yangzi Petrochemical Company Limited ("Sinopec Yangzi") (ii)	2,330	99.81	Manufacturing of intermediate petrochemical products and petroleum products
Sinopec Zhongyuan Petroleum Company Limited ("Sinopec Zhongyuan") (ii)	875	99.35	Exploration and production of crude oil and natural gas
Sinopec Shengli Oil Field Dynamic Company Limited ("Dynamic") (ii)	364	97.71	Exploration and production of crude oil and distribution of petrochemical products
Sinopec Fujian Petrochemical Company Limited (iii)	2,253	50.00	Manufacturing of plastics, 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 (iii)	147	46.25	Marketing and distribution of refined petroleum products
Sinopec Yizheng Chemical Fibre Company Limited (iii)	4,000	42.00	Production and sale of polyester chips and polyester fibres
Sinopec Zhongyuan Petrochemical Company Limited	2,400	93.51	Manufacturing of chemical products
Sinopec Shell (Jiangsu) Petroleum Marketing Company Limited	830	60.00	Marketing and distribution of refined petroleum products
BP Sinopec (Zhejiang) Petroleum 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
China International United Petroleum and Chemical Company Limited	223	100.00	Trading of crude oil and petrochemical products
Sinopec Hainan Refining and Chemical Company Limited ("Sinopec Hainan") (Note 1)	3,986	75.00	Manufacturing of intermediate petrochemical products and petroleum products

(i) During the period, the Group acquired the entire 723,754,468 H shares, representing approximately 28.7% of the issued share capital of Sinopec Zhenhai at HK\$ 10.60 per share. The total consideration required to be paid by the Group is approximately RMB 7,930 million which will be settled in cash. The excess of the cost of purchase over the carrying value of the underlying assets and liabilities (on a proportionate share) was RMB 4,043 million, which was recorded as equity investment differences.

(ii) During the period, the Group acquired the shares not held by the Group in Sinopec Qilu, Sinopec Yangzi, Sinopec Zhongyuan and Dynamic of 17.71%, 14.83%, 28.50%, and 71.38%, respectively. The total consideration paid by the Group was approximately RMB 14,041 million which was settled in cash. The excess of the cost of purchase over the carrying value of the underlying assets and liabilities (on a proportionate share) was RMB 7,766 million, which was recorded as equity investment differences.

(iii) 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 2006

43 PRINCIPAL JOINTLY CONTROLLED ENTITIES

At 31 December 2006, 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 2006, the future minimum lease payments of the Group and the Company under operating leases are as follows:

	The Group		The Company	
	2006 RMB millions	2005 RMB millions	2006 RMB millions	2005 RMB millions
Within one year	4,711	3,593	4,457	3,424
Between one and two years	4,568	3,442	4,391	3,363
Between two and three years	4,531	3,388	4,359	3,319
Between three and four years	4,505	3,357	4,337	3,292
Between four and five years	4,450	3,353	4,372	3,290
After five years	122,406	95,176	120,638	93,601
Total	145,171	112,309	142,554	110,289

Capital commitments

At 31 December 2006, the capital commitments are as follows:

	2006 RMB millions	2005 RMB millions
The Group		
Authorised and contracted for	113,192	71,666
Authorised but not contracted for	165,967	84,213
	279,159	155,879
Jointly controlled entities		
Authorised and contracted for	1,878	2,160
Authorised but not contracted for	5	60
	1,883	2,220
The Company		
Authorised and contracted for	95,206	55,496
Authorised but not contracted for	97,699	45,938
	192,905	101,434

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 equity investments.

NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2006

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 236 million for the year ended 31 December 2006 (2005: RMB 208 million).

Estimated future annual payments are as follows:

	The Group		The Company	
	2006	2005	2006	2005
	RMB millions	RMB millions	RMB millions	RMB millions
Within one year	156	107	156	74
Between one and two years	147	112	147	81
Between two and three years	67	59	67	49
Between three and four years	57	67	57	58
Between four and five years	10	56	10	49
After five years	226	239	226	108
Total	663	640	663	419

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 2006, 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	
	2006	2005	2006	2005
	RMB millions	RMB millions	RMB millions	RMB millions
Subsidiaries	—	—	2,674	2,583
Associates and jointly controlled entities	160	79	11,863	11,986
Total	160	79	14,537	14,569

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 2006 and 2005, 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 1,637 million for the year ended 31 December 2006 (2005: RMB 493 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 2006

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, 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:

	2006	2005
	RMB millions	RMB millions
Income from principal operations		
Exploration and production		
External sales	23,282	19,862
Inter-segment sales	105,656	84,423
	128,938	104,285
Refining		
External sales	99,201	82,810
Inter-segment sales	471,571	386,456
	570,772	469,266
Marketing and distribution		
External sales	588,270	459,292
Inter-segment sales	4,601	3,172
	592,871	462,464
Chemicals		
External sales	209,133	160,783
Inter-segment sales	12,299	12,199
	221,432	172,982
Others		
External sales	124,693	76,368
Inter-segment sales	136,775	44,897
	261,468	121,265
Elimination of inter-segment sales	(730,902)	(531,147)
Income from principal operations	1,044,579	799,115
Cost of sales, sales taxes and surcharges		
Exploration and production	53,052	40,118
Refining	595,118	477,843
Marketing and distribution	536,381	427,308
Chemicals	196,274	149,431
Others	258,977	118,152
Elimination of inter-segment cost of sales	(731,487)	(527,451)
Cost of sales, sales taxes and surcharges	908,315	685,401
Profit from principal operations		
Exploration and production	76,022	59,732
Refining	(23,897)	(7,838)
Marketing and distribution	56,490	35,156
Chemicals	25,158	23,551
Others	2,491	3,113
Profit from principal operations	136,264	113,714

NOTES ON THE FINANCIAL STATEMENTS (CONTINUED)

for the year ended 31 December 2006

47 POST BALANCE SHEET EVENTS

On 15 February 2006, the Ministry of Finance (the “MOF”) issued the new Accounting Standards for Business Enterprises, with effect from 1 January 2007, which requires the Group no longer to adopt the current Accounting Standards for Business Enterprises and “Accounting Regulations for Business Enterprises”. As a result of the adoption of the new accounting standards, it may cause changes to the accounting policies and the accounting estimates, and have impact on the Group’s financial position and results of operations.

On 16 March 2007, the Fifth Plenary Session of the Tenth National People’s Congress passed the Corporate Income Tax Law of the People’s Republic of China (“new tax law”), which will take effect on 1 January 2008. According to the new tax law, the corporate income tax rate for entities other than certain high-tech enterprises and small-scale enterprises, as defined in the new tax law will be revised to 25%. In addition, entities that are currently taxed at preferential rates will be subject to a five-year transition period during which the tax rates will gradually be increased to the unified rate of 25% from 1 January 2008. As a result of the new tax law, it is expected that the income tax rate applicable to the Company and certain of its entities will be reduced from 33% to 25% from 1 January 2008. However, since the detailed implementation rules as to how the existing preferential rates will gradually be increased to the unified rate of 25% over the five-year transition period have not been formulated and promulgated, management is not yet in a position to estimate the impact of the new tax law on the deferred tax assets and liabilities of certain entities which are being taxed at preferential rates. The financial effect of the new tax law, if any, will be reflected in the Group’s 2007 financial statements. The enactment of the new tax law is not expected to have any financial effect on the amounts accrued in the balance sheet in respect of current tax payable.

On 6 December 2006, the Group announced its proposal to issue USD 1,500 million convertible bonds, which are convertible into H shares of the Company. This proposal was subsequently approved by the shareholders of the Company at the Extraordinary General Meeting held on 22 January 2007 and is subject to the approval from the relevant PRC governmental and regulatory bodies.

48 EXTRAORDINARY GAIN AND LOSS

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

	2006	2005
	RMB millions	RMB millions
Extraordinary gain and loss for the year:		
Loss on disposal of fixed assets	1,782	2,422
Employee reduction expenses	236	369
Donations	95	203
Gain on disposal of long-term equity investments	(25)	(25)
Other non-operating income and expenses, excluding impairment losses on long-lived assets	374	757
Written back of provisions for impairment losses in previous years	(583)	(1,115)
Subsidy income	(5,000)	(9,415)
Tax effect	1,030	2,245
Total	(2,091)	(4,559)

49 OTHER SIGNIFICANT EVENTS

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