1 PRINCIPAL ACTIVITIES, ORGANISATION AND BASIS OF PRESENTATION

Principal activities

China Petroleum & Chemical Corporation (the "Company") is an energy and chemical company that, through its subsidiaries (hereinafter collectively referred to as the "Group"), engages in fully integrated oil and gas and chemical operations in the People's Republic of China (the "PRC"). Oil and gas operations consist of exploring for, developing and producing crude oil and natural gas; transporting crude oil, natural gas and products by pipelines; refining crude oil into finished petroleum products; and marketing crude oil, natural gas and refined petroleum products. Chemical operations include the manufacture and marketing of a wide range of chemicals for industrial uses.

Organisation

The Company was established in the PRC on 25 February 2000 as a joint stock limited company as part of the reorganisation (the "Reorganisation") of China Petrochemical Corporation ("Sinopec Group Company"), the ultimate holding company of the Group and a ministry-level enterprise under the direct supervision of the State Council of the PRC. Prior to the incorporation of the Company, the oil and gas and chemical operations of the Group were carried on by oil administration bureaux, petrochemical and refining production enterprises and sales and marketing companies of Sinopec Group Company.

As part of the Reorganisation, certain of Sinopec Group Company's core oil and gas and chemical operations and businesses together with the related assets and liabilities were transferred to the Company. On 25 February 2000, in consideration for Sinopec Group Company transferring such oil and gas and chemical operations and businesses and the related assets and liabilities to the Company, the Company issued 68.8 billion domestic state-owned ordinary shares with a par value of RMB 1.00 each to Sinopec Group Company. The shares issued to Sinopec Group Company on 25 February 2000 represented the entire registered and issued share capital of the Company at that date. The oil and gas and chemical operations and businesses transferred to the Company related to (i) the exploration, development and production of crude oil and natural gas, (ii) the refining, transportation, storage and marketing of crude oil and petroleum products, and (iii) the production and sale of chemicals (collectively the "Predecessor Operations").

Basis of presentation

Pursuant to the resolution passed at the Directors' meeting on 10 October 2006, the Group acquired equity interests in Sinopec Hainan Refining and Chemical Company Limited ("Sinopec Hainan") for cash of RMB 2,990 million (hereinafter referred to as the "Acquisition of Sinopec Hainan"). Sinopec Hainan was previously wholly owned by Sinopec Group Company.

Pursuant to the resolution passed at the Directors' meeting on 6 December 2006, the Group acquired the equity interests in certain oil and gas production companies ("Oil Production Plants") from Sinopec Group Company, for a total consideration of RMB 3,500 million payable in 2007 (hereinafter referred to as the "Acquisition of Oil Production Plants").

As the Group, Sinopec Hainan and Oil Production Plants are under the common control of Sinopec Group Company, the Acquisitions of Sinopec Hainan and Oil Production Plants are considered as "combination of entities under common control" which are accounted in a manner similar to a pooling-of-interests ("as-if pooling-of-interests accounting"). Accordingly, the assets and liabilities acquired from Sinopec Hainan and Oil Production Plants have been accounted for at historical cost. In connection with these acquisitions, certain assets, primarily property, plant and equipment and construction in progress, were retained by Sinopec Group Company. The assets retained by Sinopec Group Company and the considerations paid by the Company for these acquisitions were treated as equity transactions.

The financial condition and results of operation previously reported by the Group as at and for the year ended 31 December 2005 have been restated to include the results of Sinopec Hainan and Oil Production Plants (collectively the "Acquired Group") as set out below.

	The Group without the Acquired Group RMB millions	The Acquired Group RMB millions	Combined RMB millions
Results of operation:			
Operating revenue	823,117	155	823,272
Profit attributable to the equity shareholders of the Company	40,920	535	41,455
Basic and diluted earnings per share (RMB)	0.47	0.01	0.48
Financial condition:			
Current assets	145,291	1,766	147,057
Total assets	537,321	11,719	549,040
Current liabilities	170,649	4,362	175,011
Total liabilities	284,325	9,735	294,060
Total equity attributable to equity shareholders of the Company	223,556	745	224,301

For the years presented, all significant balances and transactions between the Group and the Acquired Group have been eliminated.

The accompanying financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") promulgated by the International Accounting Standards Board ("IASB"). IFRS includes International Accounting Standards ("IAS") and related interpretations. These financial statements also comply with the disclosure requirements of the Hong Kong Companies Ordinance and the applicable disclosure provisions of the Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong Limited. A summary of the principal accounting policies adopted by the Group and the Company are set out in Note 2. These accounting policies have been consistently applied by the Group and the Company.

The accompanying financial statements are prepared on the historical cost basis as modified by the revaluation of certain property, plant and equipment (Note 18).

The preparation of the financial statements in accordance with IFRS requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the year. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results could differ from those estimates.

1 PRINCIPAL ACTIVITIES, ORGANISATION AND BASIS OF PRESENTATION *(Continued)*

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

Key assumptions and estimation made by management in the application of IFRS that have significant effect on the financial statements and have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities in the following financial year are disclosed in Note 41.

2 PRINCIPAL ACCOUNTING POLICIES

(a) Basis of consolidation

The consolidated financial statements comprise the Company and its subsidiaries, and the Group's interest in associates and jointly controlled entities.

(i) Subsidiaries

Subsidiaries are those entities controlled by the Group. Control exists when the Group has the power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

The financial statements of subsidiaries are included in the consolidated financial statements from the date that control effectively commences until the date that control effectively ceases.

Minority interests at the balance sheet date, being the portion of the net assets of subsidiaries attributable to equity interests that are not owned by the Company, whether directly or indirectly through subsidiaries, are presented in the consolidated balance sheet and statement of changes in equity within equity, separately from equity attributable to the equity shareholders of the Company. Minority interests in the results of the Group are presented on the face of the consolidated income statement as an allocation of the total profit or loss for the period between minority interests and the equity shareholders of the Company.

In the Company's balance sheet, investments in subsidiaries are stated at cost less impairment losses (Note 2(l)).

The particulars of the Group's principal subsidiaries are set out in Note 39.

(ii) Interest in associates

An associate is an entity, not being a subsidiary, in which the Group or the Company exercises significant influence over its management. Significant influence is the power to participate in the financial and operating policy decisions of the investee but is not control or joint control over those policies.

Investments in associates are accounted for in the consolidated financial statements using the equity method from the date that significant influence commences until the date that significant influence ceases.

In the Company's balance sheet, investments in associates are stated at cost less impairment losses (Note 2(l)).

(iii) Jointly controlled entities

A jointly controlled entity is an entity over which the Group or the Company can exercise joint control with other venturers. Joint control is the contractually agreed sharing of control over an economic activity.

Investments in jointly controlled entities are accounted for in the consolidated financial statements on a proportionate consolidation basis. Under this method, the Group combines its proportionate share of the jointly controlled entity's turnover and expenses with each major turnover and expense caption of the Group's income statement and combines its proportionate share of the jointly controlled entity's assets and liabilities with each major asset and liability caption of the Group's balance sheet, from the date that joint control commences until the date that joint control ceases.

In the Company's balance sheet, investments in jointly controlled entities are stated at cost less impairment losses (Note 2(l)).

(iv) Transactions eliminated on consolidation

Inter-company balances and transactions and any unrealised gains arising from inter-company transactions are eliminated on consolidation. Unrealised gains arising from transactions with associates and jointly controlled entities are eliminated to the extent of the Group's interest in the entity. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

(b) Translation of foreign currencies

The presentation currency of the Group is Renminbi. Foreign currency transactions during the year are translated into Renminbi at the applicable rates of exchange quoted by the People's Bank of China ("PBOC") prevailing on the transaction dates. Foreign currency monetary assets and liabilities are translated into Renminbi at the PBOC's rates at the balance sheet date.

Exchange differences, other than those capitalised as construction in progress, are recognised as income or expense in the income statement.

(c) Cash and cash equivalents

Cash equivalents consist of time deposits with financial institutions with an initial term of less than three months when purchased. Cash equivalents are stated at cost, which approximates fair value.

(d) Trade accounts and other receivables

Trade accounts and other receivables are initially recognised at fair value and thereafter stated at amortised cost less impairment losses for bad and doubtful debts (Note 2(l)).

2 PRINCIPAL ACCOUNTING POLICIES *(Continued)*

(e) 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 computed using the weighted average method and, in the case of work in progress and finished goods, direct labour and an appropriate proportion of production overheads. Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and the estimated costs necessary to make the sale.

Spare parts and consumables are stated at cost less any provision for obsolescence.

(f) Property, plant and equipment

An item of property, plant and equipment is initially recorded at cost, less accumulated depreciation and impairment losses (Note 2(l)). The cost of an asset comprises its purchase price, any directly attributable costs of bringing the asset to working condition and location for its intended use. Subsequent to the revaluation (Note 18), which was based on depreciated replacement costs, property, plant and equipment are carried at revalued amount, being the fair value at the date of the revaluation less any subsequent accumulated depreciation and impairment losses. Revaluations are performed periodically to ensure that the carrying amount does not differ materially from that which would be determined using fair value at the balance sheet date. The Group recognises in the carrying amount of an item of property, plant and equipment the cost of replacing part of such an item when that cost is incurred if it is probable that the future economic benefits embodied with the item will flow to the Group and the cost of the item can be measured reliably. All other expenditure is recognised as an expense in the income statement in the year in which it is incurred.

Gains or losses arising from the retirement or disposal of an item of property, plant and equipment, other than oil and gas properties, are determined as the difference between the net disposal proceeds and the carrying amount of the item and are recognised as income or expense in the income statement on the date of retirement or disposal. On disposal of a revalued asset, the related revaluation surplus is transferred from the revaluation reserve to retained earnings.

Depreciation is provided to write off the cost/revalued amount of items of property, plant and equipment, other than oil and gas properties, over its estimated useful life on a straight-line basis, after taking into account its estimated residual value, as follows:

Buildings	15 to 45 years
Plant, machinery, equipment, oil depots, storage tanks and others	4 to 18 years
Service stations	25 years

Where parts of an item of property, plant and equipment have different useful lives, the cost or valuation of the item is allocated on a reasonable basis between the parts and each part is depreciated separately. Both the useful life of an asset and its residual value, if any, are reassessed annually.

(g) Oil and gas properties

The Group uses the successful efforts method of accounting for its oil and gas producing activities. Under this method, 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. The impairment of exploratory well costs occurs upon the determination that the well has not found proved reserves. Exploratory wells that find oil and gas reserves in any area requiring major capital expenditure are expensed unless the well has found a sufficient quantity of reserves to justify its completion as a producing well if the required capital expenditure is made, and drilling of the additional exploratory wells is under way or firmly planned for the near future. 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, other dry hole costs and annual lease rentals, are expensed as incurred. Capitalised costs relating to proved properties are amortised at the field level on a unit-of-production method. The amortisation rates are determined based on oil and gas reserves estimated to be recoverable from existing facilities over the shorter of the economic lives of crude oil and natural gas reservoirs and the terms of the relevant production licenses.

Gains and losses on the disposal of proved oil and gas properties are not recognised unless the disposal encompasses an entire property. The proceeds on such disposals are credited to the carrying amounts of oil and gas properties.

(h) Lease prepayments

Lease prepayments represent land use rights paid to the relevant government authorities. Land use rights are carried at cost less accumulated amortisation and impairment losses (Note 2(l)). Amortisation is provided to write off the cost of lease prepayments on a straight-line basis over the respective periods of the rights.

(i) Construction in progress

Construction in progress represents buildings, oil and gas properties, various plant and equipment under construction and pending installation, and is stated at cost less impairment losses (Note 2(l)). Cost comprises direct costs of construction as well as interest charges, and foreign exchange differences on related borrowed funds to the extent that they are regarded as an adjustment to interest charges, during the periods of construction.

Construction in progress is transferred to property, plant and equipment when the asset is substantially ready for its intended use.

No depreciation is provided in respect of construction in progress.

(j) Goodwill

Goodwill represents amounts arising on acquisition of subsidiaries, associates or jointly controlled entities. Goodwill represents the difference between the cost of acquisition and the fair value of the net identifiable assets acquired.

Goodwill is stated at cost less accumulated impairment losses. Goodwill is allocated to cash-generating units and is tested annually for impairment (Note 2(l)). In respect of associates, the carrying amount of goodwill is included in the carrying amount of the interest in associates.

2 PRINCIPAL ACCOUNTING POLICIES *(Continued)*

(k) Investments

Investment in available-for-sale equity securities are carried at fair value with any change in fair value, other than impairment losses (Note2(l)), recognised directly in equity. When these investments are derecognised or impaired, the cumulative gain or loss previously recognised directly in equity is recognised in the income statement. Investments in equity securities, other than investments in associates, that do not have a quoted market price in an active market and whose fair value cannot be reliably measured are recognised in the balance sheet at cost less impairment losses (Note 2(l)).

(l) Impairment of assets

(i) Impairment of trade accounts receivable, other receivables and investment in equity securities other than investments in associates are accounted as follows:

Trade accounts receivable, other receivables and investment in equity securities other than investments in associates are reviewed at each balance sheet date to determine whether there is objective evidence of impairment. If any such evidence exists, an impairment loss is determined and recognised. The impairment loss is measured as the difference between the asset's carrying amount and the estimated future cash flows, discounted at the current market rate of return for a similar financial asset where the effect of discounting is material, and is recognised as an expense in the income statement. Impairment losses for trade and other receivables are reversed through the income statement if in a subsequent period the amount of the impairment losses decreases. Impairment losses for equity securities are not reversed.

(ii) Impairment of other long-lived assets is accounted as follows:

The carrying amounts of other long-lived assets, including property, plant and equipment, construction in progress, lease prepayment and investments in associates, are reviewed periodically in order to assess whether the recoverable amounts have declined below the carrying amounts. These 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. For goodwill, the recoverable amount is estimated at each balance sheet date.

The recoverable amount is the greater of the fair value less costs to sell and the value in use. In determining the value in use, expected future cash flows generated by the asset are discounted to their present value using a pre-tax discount rate that reflects current market assessments of time value of money and the risks specific to the asset. Where an asset does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the smallest group of assets that generates cash inflows independently (i.e. a cash-generating unit).

The amount of the reduction is recognised as an expense in the income statement unless the asset is carried at revalued amount for which an impairment loss is recognised directly against any related revaluation reserve to the extent that the impairment loss does not exceed the amount held in the revaluation reserve for that same asset. Impairment losses recognised in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to the cash-generating unit and then, to reduce the carrying amount of the other assets in the unit on a pro rata basis, except that the carrying value of an asset will not be reduced below its individual fair value less costs to sell, or value in use, if determinable.

The Group assesses at each balance sheet date whether there is any indication that an impairment loss recognised for an asset, except in the case of goodwill, in prior years may no longer exist. An impairment loss is reversed if there has been a favourable change in the estimates used to determine the recoverable amount. A subsequent increase in the recoverable amount of an asset, when the circumstances and events that led to the write-down or write-off cease to exist, is recognised as an income unless the asset is carried at revalued amount. Reversal of an impairment loss on a revalued asset is credited to the revaluation reserve except for impairment loss which was previously recognised as an expense in the income statement; a reversal of such impairment loss is recognised as an income. The reversal is reduced by the amount that would have been recognised as depreciation had the write-down or write-off not occurred. An impairment loss in respect of goodwill is not reversed.

(m)Trade accounts and other payables

Trade accounts and other payables are initially recognised at fair value and thereafter stated at amortised cost unless the effect of discounting would be immaterial, in which case they are stated at cost.

(n) Interest-bearing borrowings

Interest bearing borrowings are recognised initially at fair value less attributable transaction costs. Subsequent to initial recognition, interest-bearing borrowings are stated at amortised cost with any difference between cost and redemption value being recognised in income statement over the period of borrowings using the effective interest method.

(o) Provisions and contingent liability

A provision is recognised for liability of uncertain timing or amount when the Group has a legal or constructive obligation arising as a result of a past event, it is probable that an outflow of economic benefits will be required to settle the obligation and a reliable estimate can be made.

When it is not probable that an outflow of economic benefits will be required, or the amount cannot be estimated reliably, the obligation is disclosed as a contingent liability, unless the probability of outflow of economic benefits is remote. Possible obligations, whose existence will only be confirmed by the occurrence or non-occurrence of one or more future events are also disclosed as contingent liabilities unless the probability of outflow of economic benefits is remote.

2 PRINCIPAL ACCOUNTING POLICIES *(Continued)*

(p) Revenue recognition

Revenues associated with the sale of crude oil, natural gas, petroleum and chemical products and ancillary materials are recorded when the customer accepts the goods and the significant risks and rewards of ownership and title have been transferred to the buyer. Revenue from the rendering of services is recognised in the income statement upon performance of the services. 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.

Interest income is recognised on a time apportioned basis that takes into account the effective yield on the asset.

Government grants relating to the purchase of assets used for technology improvements are initially recorded as long-term liabilities when there is reasonable assurance that they will be received and thereafter offset against the cost of the related assets upon the transfer of these assets to property, plant and equipment. The grants are recognised as an income over the useful life of these property, plant and equipment by way of reduced depreciation.

A government grant that becomes receivable as compensation for expenses or losses already incurred with no future related costs is recognised as income in the period in which it becomes receivable.

(q) Borrowing costs

Borrowing costs are expensed in the income statement in the period in which they are incurred, except to the extent that they are capitalised as being attributable to the construction of an asset which necessarily takes a period of time to get ready for its intended use.

(r) Repairs and maintenance expenditure

Repairs and maintenance expenditure is expensed as incurred.

(s) Environmental expenditures

Environmental expenditures that relate to current ongoing operations or to conditions caused by past operations are expensed as incurred.

Liabilities related to future remediation costs are recorded when environmental assessments and/or cleanups are probable and the costs can be reasonably estimated. As facts concerning environmental contingencies become known to the Group, the Group reassesses its position both with respect to accrued liabilities and other potential exposures.

(t) Research and development costs

Research and development costs are recognised as expenses in the period in which they are incurred. Research and development costs amounted to RMB 2,902 million for the year ended 31 December 2006 (2005: RMB 2,244 million).

(u) Operating leases

Operating lease payments are charged to the income statement on a straight-line basis over the period of the respective leases.

(v) Retirement benefits

The contributions payable under the Group's retirement plans are recognised as expenses in the income statement as incurred and according to the contribution determined by the plans. Further information is set out in Note 37.

(w) Income tax

Income tax comprises current and deferred tax. Current tax is calculated on taxable income by applying the applicable tax rates. Deferred tax is provided using the balance sheet liability method on all temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is calculated on the basis of the enacted tax rates that are expected to apply in the period when the asset is realised or the liability is settled.

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 to the extent appropriate, and is not available for set-off against the taxable profit of another legal tax unit. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

(x) Dividends

Dividends are recognised as a liability in the period in which they are declared.

(y) Segmental reporting

A business segment is a distinguishable component of the Group that is engaged in providing products or services and is subject to risks and rewards that are different from those of other segments.

3 TURNOVER

Turnover represents revenue from the sales of crude oil, natural gas, petroleum and chemical products, net of value-added tax.

4 OTHER OPERATING REVENUES

	The Group	
	2006	2005
	RMB millions	RMB millions
Sale of materials, service and others	26,366	23,619
Rental income	384	394
	26,750	**24,013**

5 OTHER 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.

6 SELLING, GENERAL AND ADMINISTRATIVE EXPENSES

The following items are included in selling, general and administrative expenses:

	The Group	
	2006	2005
	RMB millions	RMB millions
Operating lease charges	6,128	5,516
Auditors' remuneration – audit services	84	76
Impairment losses:		
– trade accounts receivable	438	328
– other receivables	107	454

7 PERSONNEL EXPENSES

	The Group	
	2006	2005
	RMB millions	RMB millions
Wages and salaries	14,840	13,742
Staff welfare	1,927	1,808
Contributions to retirement schemes	2,270	2,273
Social security contributions	820	826
	19,857	**18,649**

8 EMPLOYEE REDUCTION EXPENSES

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

9 TAXES OTHER THAN INCOME TAX

	The Group	
	2006	2005
	RMB millions	RMB millions
Consumption tax	14,121	12,430
Special oil income levy	8,747	—
City construction tax	3,038	2,589
Education surcharge	1,615	1,311
Resources tax	854	642
Business tax	264	213
	28,639	**17,185**

Consumption tax is levied on producers of gasoline, diesel, naphtha, fuel oil, jet fuel, lubricant oil and solvent oil based on a tariff rate applied to the volume of sales. Effective 26 March 2006, a special oil income levy has been levied on oil exploration and production entities based on the progressive rates ranging from 20% to 40% on the portion of the monthly weighted average sales price of the crude oil produced in the PRC exceeding USD 40 per barrel. City construction tax is levied on an entity based on its total amount of value-added tax, consumption tax and business tax.

10 OTHER OPERATING EXPENSES, NET

	The Group	
	2006	2005
	RMB millions	RMB millions
Fines, penalties and compensations	65	155
Donations	98	203
Loss on disposal of property, plant and equipment, net	1,646	2,098
Impairment losses on long-lived assets (i)	825	1,851
Gain from debt extinguishment (ii)	(486)	—
Others	289	821
	2,437	**5,128**

Note:

(i) Impairment losses recognised on long-lived assets of the chemicals segment was RMB 250 million (2005: RMB 1,425 million) for the year ended 31 December 2006. These impairment losses relate to certain chemicals production facilities that are held for use. The carrying values of these facilities were written down to their recoverable amounts 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 impairment losses on long-lived assets 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.

Impairment losses recognised on long-lived assets of the marketing and distribution segment 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.

The factors resulting in the exploration and production ("E&P") segment impairment losses of RMB 552 million for the year ended 31 December 2006 (2005: RMB 60 million) were unsuccessful development drilling and high operating and development costs for certain small oil fields. The carrying values of these E&P properties were written down to a recoverable amount 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.

(ii) 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 totalling RMB 486 million.

11 INTEREST EXPENSE

	The Group	
	2006	2005
	RMB millions	RMB millions
Interest expense incurred	8,931	7,311
Less: Interest expense capitalised*	(1,494)	(1,385)
Interest expense	**7,437**	**5,926**
* Interest rates per annum at which borrowing costs were capitalised for construction in progress	**3.6% to 6.1%**	**3.3% to 6.6%**

Financial Statements (International)

12 TAXATION

Taxation in the consolidated income statement represents:

	The Group	
	2006	2005
	RMB millions	RMB millions
Current tax		
– Provision for the year	23,981	20,646
– Under-provision in prior years	260	477
Deferred taxation	(726)	(1,243)
	23,515	**19,880**

A reconciliation between actual tax expense and accounting profit at applicable tax rates is as follows:

	The Group	
	2006	2005
	RMB millions	RMB millions
Profit before taxation	78,923	64,656
Expected PRC income tax expense at a statutory tax rate of 33%	26,045	21,336
Tax effect of non-deductible expenses	516	461
Tax effect of non-taxable income	(648)	(567)
Tax effect of differential tax rate on subsidiaries' income (Note)	(2,867)	(2,010)
Tax effect of tax losses not recognised for deferred tax, net	258	391
Under-provision in prior years	260	477
Tax credit for domestic equipment purchases	(49)	(208)
Actual tax expense	**23,515**	**19,880**

Substantially all income before income tax and related tax expense is from PRC sources.

Note:

The provision for PRC current income tax is based on a statutory rate of 33% of the assessable income of the Group as determined in accordance with the relevant income tax rules and regulations of the PRC, except for certain entities of the Group, which are taxed at a preferential rate of 15%.

13 DIRECTORS' AND SUPERVISORS' EMOLUMENTS

Directors' and supervisors' emoluments are as follows:

Name	Directors' fee RMB'000	Salaries, allowances and benefits in kind RMB'000	Discretionary bonuses RMB'000	Retirement scheme contributions RMB'000	2006 Total RMB'000
Executive directors					
Wang Tianpu	—	280	317	19	616
Zhang Jianhua	—	268	289	19	576
Wang Zhigang	—	268	289	19	576
Dai Houliang	—	230	200	16	446
Cao Yaofeng*	—	108	—	5	113
Wang Jiming*	—	141	—	8	149
Mou Suling*	—	109	—	6	115
Zhang Jiaren*	—	114	—	8	122
Cao Xianghong*	—	136	—	8	144
Non-executive directors					
Chen Tonghai	—	—	—	—	—
Zhou Yuan	—	—	—	—	—
Liu Genyuan*	—	—	—	—	—
Fan Yifei	35	—	—	—	35
Yao Zhongmin	35	—	—	—	35
Gao Jian*	—	—	—	—	—
Independent non-executive directors					
Shi Wanpeng	121	—	—	—	121
Liu Zhongli	109	—	—	—	109
Li Deshui	109	—	—	—	109
Chen Qingtai*	12	—	—	—	12
Zhang Youcai*	9	—	—	—	9
Ho Tsu Kwok Charles*	9	—	—	—	9
Supervisors					
Wang Zuoran	—	—	—	—	—
Zhang Chongqing*	—	—	—	—	—
Wang Peijun*	—	—	—	—	—
Wang Xianwen*	—	—	—	—	—
Zhang Baojian*	—	—	—	—	—
Kang Xianzhang	—	—	—	—	—
Su Wensheng	—	160	175	19	354
Cui Guoqi	—	147	163	19	329
Zhang Xianglin*	—	63	170	6	239
Zhang Jitian	—	90	—	12	102
Zou Huiping	—	90	—	12	102
Li Zhonghua	—	86	—	8	94
Independent supervisors					
Cui Jianmin*	9	—	—	—	9
Li Yonggui	121	—	—	—	121
Zhang Youcai	109	—	—	—	109
Total	**678**	**2,290**	**1,603**	**184**	**4,755**

* These directors and supervisors were resigned on 24 May 2006.

13 DIRECTORS' AND SUPERVISORS' EMOLUMENTS *(Continued)*

Name	Directors' fee RMB'000	Salaries, allowances and benefits in kind RMB'000	Discretionary bonuses RMB'000	Retirement scheme contributions RMB'000	2005 Total RMB'000
Executive directors					
Wang Jiming	—	239	225	16	480
Mou Shuling	—	219	212	11	442
Zhang Jiaren	—	227	212	16	455
Cao Xianghong	—	227	212	16	455
Cao Yaofeng	—	133	134	12	279
Non-executive directors					
Chen Tonghai	—	—	—	—	—
Liu Genyuan	—	—	—	—	—
Gao Jian	—	—	—	—	—
Fan Yifei	—	—	—	—	—
Independent non-executive directors					
Chen Qingtai	27	—	—	—	27
Ho Tsu Kwok Charles	21	—	—	—	21
Shi Wanpeng	24	—	—	—	24
Zhang Youcai	21	—	—	—	21
Supervisors					
Wang Zuoran	—	—	—	—	—
Zhang Chongqing	—	—	—	—	—
Wang Peijun	—	—	—	—	—
Wang Xianwen	—	—	—	—	—
Zhang Baojian	—	—	—	—	—
Kang Xianzhang	—	—	—	—	—
Su Wensheng	—	164	22	16	202
Cui Guoqi	—	105	42	7	154
Zhang Xianglin	—	82	88	11	181
Zhang Haichao	—	89	95	10	194
Independent supervisors					
Cui Jianming	24	—	—	—	24
Li Yonggui	24	—	—	—	24
Total	**141**	**1,485**	**1,242**	**115**	**2,983**

14 SENIOR MANAGEMENT'S EMOLUMENTS

For the year ended 31 December 2006, of the five highest paid individuals, four (2005: four) are directors whose emoluments are disclosed in Note 13. The aggregate of the emoluments in respect of the five highest paid individuals are as follows:

	2006 RMB'000	2005 RMB'000
Salaries and other emoluments	2,640	2,269
Retirement scheme contributions	92	77
	2,732	**2,346**

An analysis of emoluments paid to the five highest paid individuals by number of individuals and emolument range is as follows:

	2006 Number	2005 Number
Nil to HK$ 1,000,000	**5**	**5**

15 PROFIT ATTRIBUTABLE TO EQUITY SHAREHOLDERS OF THE COMPANY

The consolidated profit attributable to equity shareholders of the Company includes a profit of RMB 55,140 million (2005: RMB 26,668 million) which has been dealt with in the financial statements of the Company.

16 DIVIDENDS

Dividends payable to equity shareholders of the Company attributable to the year represent:

	2006 RMB millions	2005 RMB millions
Dividends declared and paid during the year of RMB 0.04 per share (2005: RMB 0.04 per share)	3,468	3,468
Dividends declared after the balance sheet date of RMB 0.11 per share (2005: RMB 0.09 per share)	9,537	7,803
	13,005	**11,271**

Pursuant to the Company's Articles of Association and a resolution passed at the Directors' meeting on 25 August 2006, the directors authorised to declare an interim dividends for the year ended 31 December 2006 of RMB 0.04 (2005: RMB 0.04) per share totalling RMB 3,468 million (2005: RMB 3,468 million), which was paid on 28 September 2006 (2005: 30 September 2005).

16 DIVIDENDS *(Continued)*

Pursuant to a resolution passed at the Directors' meeting on 6 April 2007, a final dividend in respect of the year ended 31 December 2006 of RMB 0.11 (2005: RMB 0.09) per share totalling RMB 9,537 million (2005: RMB 7,803 million) was proposed for shareholders' approval at the Annual General Meeting. Final dividend of RMB 9,537 million (2005: RMB 7,803 million) proposed after the balance sheet date has not been recognised as a liability at the balance sheet date.

Dividends payable to equity shareholders of the Company attributable to the previous financial year, approved and paid during the period represent:

	2006 RMB millions	2005 RMB millions
Final dividends in respect of the previous financial year, approved and paid during the year of RMB 0.09 per share (2005: RMB 0.08 per share)	**7,803**	**6,936**

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.

17 BASIC AND DILUTED EARNINGS PER SHARE

The calculations of basic and diluted earnings per share for the year ended 31 December 2006 are based on the profit attributable to equity shareholders of the Company of RMB 53,912 million (2005: RMB 41,455 million) and the weighted average number of shares of 86,702,439,000 (2005: 86,702,439,000) during the year.

18 PROPERTY, PLANT AND EQUIPMENT

The Group - by segment

	Exploration and production RMB millions	Refining RMB millions	Marketing and distribution RMB millions	Chemicals RMB millions	Corporate and others RMB millions	Total RMB millions
Cost/valuation:						
Balance at 1 January 2005	194,466	116,923	65,345	163,222	4,092	544,048
Additions	412	129	382	271	150	1,344
Transferred from construction in progress	23,451	8,121	14,017	18,457	381	64,427
Proportionate share of a jointly controlled entity	—	—	—	1,028	—	1,028
Reclassification	(157)	(432)	204	289	96	—
Disposals	(3,131)	(2,859)	(2,927)	(3,164)	(245)	(12,326)
Balance at 31 December 2005	**215,041**	**121,882**	**77,021**	**180,103**	**4,474**	**598,521**
Balance at 1 January 2006	215,041	121,882	77,021	180,103	4,474	598,521
Additions	1,175	145	1,280	280	456	3,336
Transferred from construction in progress	28,695	26,994	10,087	15,461	161	81,398
Acquisition of a subsidiary	2,071	—	—	—	—	2,071
Reclassification	(56)	(600)	—	725	(69)	—
Disposals	(5,562)	(1,522)	(2,280)	(4,302)	(153)	(13,819)
Balance at 31 December 2006	**241,364**	**146,899**	**86,108**	**192,267**	**4,869**	**671,507**
Accumulated depreciation:						
Balance at 1 January 2005	94,977	56,581	13,465	92,042	1,407	258,472
Depreciation charge for the year	11,090	6,974	3,013	9,392	282	30,751
Impairment losses for the year	60	—	366	1,425	—	1,851
Reclassification	(78)	(214)	78	160	54	—
Written back on disposals	(2,706)	(2,206)	(2,110)	(2,719)	(194)	(9,935)
Balance at 31 December 2005	**103,343**	**61,135**	**14,812**	**100,300**	**1,549**	**281,139**
Balance at 1 January 2006	103,343	61,135	14,812	100,300	1,549	281,139
Depreciation charge for the year	12,839	7,671	3,422	9,391	401	33,724
Acquisition of a subsidiary	592	—	—	—	—	592
Impairment losses for the year	552	—	23	250	—	825
Reclassification	(23)	(392)	—	420	(5)	—
Written back on disposals	(5,253)	(1,314)	(1,103)	(3,470)	(108)	(11,248)
Balance at 31 December 2006	**112,050**	**67,100**	**17,154**	**106,891**	**1,837**	**305,032**
Net book value:						
At 1 January 2005	99,489	60,342	51,880	71,180	2,685	285,576
Balance at 31 December 2005	**111,698**	**60,747**	**62,209**	**79,803**	**2,925**	**317,382**
Balance at 31 December 2006	**129,314**	**79,799**	**68,954**	**85,376**	**3,032**	**366,475**

18 PROPERTY, PLANT AND EQUIPMENT *(Continued)*

The Company - by segment

	Exploration and production RMB millions	Refining RMB millions	Marketing and distribution RMB millions	Chemicals RMB millions	Corporate and others RMB millions	Total RMB millions
Cost/valuation:						
Balance at 1 January 2005	69,584	88,066	61,983	59,859	3,070	282,562
Additions	151	113	267	38	120	689
Transferred from construction in progress	13,213	5,772	9,363	2,069	371	30,788
Transferred to subsidiaries	—	—	(577)	—	—	(577)
Reclassification	(130)	(176)	276	(2)	32	—
Disposals	(1,415)	(1,546)	(2,864)	(978)	(213)	(7,016)
Balance at 31 December 2005	**81,403**	**92,229**	**68,448**	**60,986**	**3,380**	**306,446**
Balance at 1 January 2006	81,403	92,229	68,448	60,986	3,380	306,446
Additions	192	109	1,276	7	11	1,595
Transferred from construction in progress	25,317	15,049	8,115	11,357	52	59,890
Transferred from subsidiaries	109,581	2,702	—	15,866	—	128,149
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	**211,124**	**108,247**	**74,935**	**87,218**	**3,269**	**484,793**
Accumulated depreciation:						
Balance at 1 January 2005	32,119	42,789	12,892	35,694	1,057	124,551
Depreciation charge for the year	5,048	4,742	2,920	2,892	180	15,782
Transferred to subsidiaries	—	—	(66)	—	—	(66)
Impairment losses for the year	60	—	351	671	—	1,082
Reclassification	(65)	(49)	99	(1)	16	—
Written back on disposals	(1,371)	(1,183)	(2,061)	(814)	(185)	(5,614)
Balance at 31 December 2005	**35,791**	**46,299**	**14,135**	**38,442**	**1,068**	**135,735**
Balance at 1 January 2006	35,791	46,299	14,135	38,442	1,068	135,735
Depreciation charge for the year	11,569	5,757	3,082	3,835	235	24,478
Transferred from subsidiaries	50,994	1,472	—	9,382	—	61,848
Transferred to subsidiaries	—	—	(74)	—	—	(74)
Impairment losses for the year	533	—	23	200	—	756
Reclassification	(23)	(395)	—	423	(5)	—
Written back on disposals	(5,144)	(1,083)	(1,050)	(1,385)	(71)	(8,733)
Balance at 31 December 2006	**93,720**	**52,050**	**16,116**	**50,897**	**1,227**	**214,010**
Net book value:						
At 1 January 2005	37,465	45,277	49,091	24,165	2,013	158,011
Balance at 31 December 2005	**45,612**	**45,930**	**54,313**	**22,544**	**2,312**	**170,711**
Balance at 31 December 2006	**117,404**	**56,197**	**58,819**	**36,321**	**2,042**	**270,783**

18 PROPERTY, PLANT AND EQUIPMENT *(Continued)*

The Group - by asset class

	Buildings RMB millions	Oil and gas properties RMB millions	Oil depots, storage tanks and service stations RMB millions	Plant, machinery, equipment and others RMB millions	Total RMB millions
Cost/valuation:					
Balance at 1 January 2005	45,119	175,522	60,533	262,874	544,048
Additions	108	253	228	755	1,344
Transferred from construction in progress	2,535	22,235	13,851	25,806	64,427
Proportionate share of a jointly controlled entity	182	—	—	846	1,028
Reclassification	(406)	(802)	650	558	—
Disposals	(1,034)	(1,928)	(2,145)	(7,219)	(12,326)
Balance at 31 December 2005	**46,504**	**195,280**	**73,117**	**283,620**	**598,521**
Balance at 1 January 2006	46,504	195,280	73,117	283,620	598,521
Additions	748	777	1,071	740	3,336
Transferred from construction in progress	2,777	26,579	14,549	37,493	81,398
Acquisition of a subsidiary	519	1,313	—	239	2,071
Reclassification	(1,569)	10	3,170	(1,611)	—
Disposals	(749)	(5,266)	(1,658)	(6,146)	(13,819)
Balance at 31 December 2006	**48,230**	**218,693**	**90,249**	**314,335**	**671,507**
Accumulated depreciation:					
Balance at 1 January 2005	20,334	85,996	11,781	140,361	258,472
Depreciation charge for the year	1,724	10,431	2,914	15,682	30,751
Impairment losses for the year	79	60	261	1,451	1,851
Reclassification	(98)	(430)	153	375	—
Written back on disposals	(598)	(1,683)	(1,379)	(6,275)	(9,935)
Balance at 31 December 2005	**21,441**	**94,374**	**13,730**	**151,594**	**281,139**
Balance at 1 January 2006	21,441	94,374	13,730	151,594	281,139
Depreciation charge for the year	1,787	12,126	3,728	16,083	33,724
Acquisition of a subsidiary	49	468	—	75	592
Impairment losses for the year	118	532	23	152	825
Reclassification	(352)	(45)	1,221	(824)	—
Written back on disposals	(437)	(5,073)	(834)	(4,904)	(11,248)
Balance at 31 December 2006	**22,606**	**102,382**	**17,868**	**162,176**	**305,032**
Net book value:					
At 1 January 2005	24,785	89,526	48,752	122,513	285,576
Balance at 31 December 2005	**25,063**	**100,906**	**59,387**	**132,026**	**317,382**
Balance at 31 December 2006	**25,624**	**116,311**	**72,381**	**152,159**	**366,475**

18 PROPERTY, PLANT AND EQUIPMENT *(Continued)*

The Company - by asset class

	Buildings RMB millions	Oil and gas properties RMB millions	Oil depots, storage tanks and service stations RMB millions	Plant, machinery, equipment and others RMB millions	Total RMB millions
Cost/valuation:					
Balance at 1 January 2005	25,838	61,866	57,395	137,463	282,562
Additions	132	64	174	319	689
Transferred from construction in progress	989	12,266	9,363	8,170	30,788
Transferred to subsidiaries	(9)	—	(529)	(39)	(577)
Reclassification	(469)	(551)	651	369	—
Disposals	(552)	(578)	(2,097)	(3,789)	(7,016)
Balance at 31 December 2005	**25,929**	**73,067**	**64,957**	**142,493**	**306,446**
Balance at 1 January 2006	25,929	73,067	64,957	142,493	306,446
Additions	61	—	1,046	488	1,595
Transferred from construction in progress	1,339	23,683	12,213	22,655	59,890
Transferred from subsidiaries	3,288	102,919	—	21,942	128,149
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	**27,784**	**194,535**	**78,784**	**183,690**	**484,793**
Accumulated depreciation:					
Balance at 1 January 2005	10,537	29,934	11,403	72,677	124,551
Depreciation charge for the year	1,046	4,682	2,524	7,530	15,782
Transferred to subsidiaries	(3)	—	(41)	(22)	(66)
Impairment losses for the year	21	60	261	740	1,082
Reclassification	(111)	(309)	154	266	—
Written back on disposals	(326)	(565)	(1,349)	(3,374)	(5,614)
Balance at 31 December 2005	**11,164**	**33,802**	**12,952**	**77,817**	**135,735**
Balance at 1 January 2006	11,164	33,802	12,952	77,817	135,735
Depreciation charge for the year	927	11,071	3,146	9,334	24,478
Transferred from subsidiaries	1,056	45,609	—	15,183	61,848
Transferred to subsidiaries	—	—	(74)	—	(74)
Impairment losses for the year	118	532	23	83	756
Reclassification	(412)	(45)	1,209	(752)	—
Written back on disposals	(230)	(5,000)	(783)	(2,720)	(8,733)
Balance at 31 December 2006	**12,623**	**85,969**	**16,473**	**98,945**	**214,010**
Net book value:					
Balance at 1 January 2005	15,301	31,932	45,992	64,786	158,011
Balance at 31 December 2005	**14,765**	**39,265**	**52,005**	**64,676**	**170,711**
Balance at 31 December 2006	**15,161**	**108,566**	**62,311**	**84,745**	**270,783**

The Group's proportionate share of the jointly controlled entities' net book value of property, plant and equipment at 31 December 2006 in the exploration and production and the chemicals segments were RMB 388 million (2005: RMB 398 million) and RMB 13,871 million (2005: RMB 14,889 million), respectively.

As required by the relevant PRC regulations with respect to the Reorganisation, the property, plant and equipment of the Group at 30 September 1999 were valued for each asset class by China United Assets Appraisal Corporation, Beijing Zhong Zheng Appraisal Company, CIECC Assets Appraisal Corporation and Zhong Fa International Properties Valuation Corporation, independent valuers registered in the PRC, on a depreciated replacement cost basis. The value of property, plant and equipment was determined at RMB 159,788 million. The surplus on revaluation of RMB 32,320 million, net of amounts allocated to minority interests, was incorporated in the financial statements of the Group at 31 December 1999.

In connection with the acquisitions of certain entities and related operations from Sinopec Group Company in prior years, the related property, plant and equipment were revalued by independent valuers in accordance with relevant PRC rules and regulations. The surplus on these revaluations of RMB 1,409 million, net of amounts allocated to minority interests, was credited to revaluation reserve.

In connection with the Acquisition of Oil Production Plants, the property, plant and equipment of the Oil Production Plants were revalued at 30 June 2006, by a firm of independent valuers in accordance with the relevant PRC rules and regulations. The value of property, plant and equipment of the Oil Production Plants pursuant to the valuation, based on a depreciated replacement cost basis, was determined at RMB 2,303 million, which approximated the net historical carrying value of the assets.

In accordance with IAS 16, subsequent to these revaluations, which was based on depreciated replacement costs, property, plant and equipment are carried at revalued amount, being the fair value at the date of the revaluation less any subsequent accumulated depreciation and impairment losses. Revaluation is performed periodically to ensure that the carrying amount does not differ materially from that which would be determined using fair value at the balance sheet date. Based on a revaluation performed as of 31 December 2004, which was based on depreciated replacement costs, the carrying value of property, plant and equipment did not differ materially from their fair value.

19 CONSTRUCTION IN PROGRESS

The Group

	Exploration and production RMB millions	Refining RMB millions	Marketing and distribution RMB millions	Chemicals RMB millions	Corporate and others RMB millions	Total RMB millions
Balance at 1 January 2005	9,387	9,483	13,781	13,170	1,513	47,334
Additions	27,245	18,971	10,572	9,115	1,014	66,917
Additions by jointly controlled entities	814	—	—	1,830	—	2,644
Proportionate share of a jointly controlled entity	—	—	—	5,461	—	5,461
Dry hole costs written off	(2,992)	—	—	—	—	(2,992)
Transferred to property, plant and equipment and other assets	(23,451)	(8,121)	(14,017)	(19,014)	(381)	(64,984)
Balance at 31 December 2005	**11,003**	**20,333**	**10,336**	**10,562**	**2,146**	**54,380**
Balance at 1 January 2006	11,003	20,333	10,336	10,562	2,146	54,380
Additions	37,892	21,824	10,039	12,361	1,714	83,830
Additions by jointly controlled entities	91	—	—	148	—	239
Acquisition of a subsidiary	89	—	—	—	—	89
Dry hole costs written off	(3,960)	—	—	—	—	(3,960)
Transferred to property, plant and equipment	(28,695)	(26,994)	(10,087)	(15,461)	(161)	(81,398)
Balance at 31 December 2006	**16,420**	**15,163**	**10,288**	**7,610**	**3,699**	**53,180**

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 2,979 million (2005: RMB 2,888 million) and RMB 603 million (2005: RMB 504 million), respectively.

As at 31 December 2006, the amount of capitalised cost of exploratory wells included in the Group's construction in progress in the exploration and production segment was RMB 4,771 million (2005: RMB 3,573 million). The geological and geophysical costs paid during the year ended 31 December 2006 were RMB 3,878 million (2005: RMB 3,200 million).

The Company

	Exploration and production RMB millions	Refining RMB millions	Marketing and distribution RMB millions	Chemicals RMB millions	Corporate and others RMB millions	Total RMB millions
Balance at 1 January 2005	6,607	6,961	10,271	3,615	1,494	28,948
Additions	16,528	12,084	7,825	5,845	915	43,197
Dry hole costs written off	(2,271)	—	—	—	—	(2,271)
Transferred to property, plant and equipment	(13,213)	(5,772)	(9,363)	(2,069)	(371)	(30,788)
Balance at 31 December 2005	**7,651**	**13,273**	**8,733**	**7,391**	**2,038**	**39,086**
Balance at 1 January 2006	7,651	13,273	8,733	7,391	2,038	39,086
Additions	32,487	14,311	8,468	8,373	1,056	64,695
Transferred from subsidiaries	927	34	—	237	—	1,198
Dry hole costs written off	(3,950)	—	—	—	—	(3,950)
Transferred to property, plant and equipment	(25,317)	(15,049)	(8,115)	(11,357)	(52)	(59,890)
Balance at 31 December 2006	**11,798**	**12,569**	**9,086**	**4,644**	**3,042**	**41,139**

20 GOODWILL

	The Group	
	2006	2005
	RMB millions	RMB millions
Cost:		
Balance at 1 January	2,203	383
Additions	12,122	1,820
Balance at 31 December	**14,325**	**2,203**
Accumulated impairment losses:		
Balance at 1 January and 31 December	—	—
Net book value:		
Balance at 1 January	2,203	383
Balance at 31 December	**14,325**	**2,203**

Impairment tests for cash-generating units containing goodwill
Goodwill is allocated to the following Group's cash-generating units:

	2006	2005
	RMB millions	RMB millions
Sinopec Beijing Yanshan Branch ("Sinopec Yanshan")	1,157	1,157
Sinopec Zhenhai Refining and Chemical Company Limited ("Sinopec Zhenhai")	3,952	—
Sinopec Qilu Petrochemical Company Limited ("Sinopec Qilu")	2,159	—
Sinopec Yangzi Petrochemical Company Limited ("Sinopec Yangzi")	2,737	—
Sinopec Zhongyuan Petroleum Company Limited ("Sinopec Zhongyuan")	1,391	—
Shengli Oil Field Dynamic Company Limited ("Dynamic")	1,361	—
Multiple units without significant goodwill	1,568	1,046
	14,325	**2,203**

During the year ended 31 December 2005, the Group acquired the entire 1,012,000,000 H shares, representing approximately 29.99% of the issued share capital of Sinopec Beijing Yanshan Petrochemical Company Limited from minority interests shareholders at HK$ 3.80 per share. The total consideration paid by the Group was approximately RMB 4,088 million which was settled in cash. The excess of the cost of purchase over the fair value of the underlying assets and liabilities (on a proportionate share) was RMB 1,157 million.

During the year ended 31 December 2006, the Group acquired additional equity interests in Sinopec Zhenhai, Sinopec Qilu, Sinopec Yangzi, Sinopec Zhongyuan and Dynamic of 28.7%, 17.7%, 14.8%, 28.5% and 71.4%, respectively. The Company acquired these additional equity interests to reduce management layers and improve the efficiency of the production, management and sales of the Group as a whole. The total consideration paid by the Group was approximately RMB 21,971 million which was settled in cash. The excess of the cost of purchase over the fair value of the underlying assets and liabilities (on a proportionate share) in Sinopec Zhenhai, Sinopec Qilu, Sinopec Yangzi, Sinopec Zhongyuan and Dynamic were RMB 3,952 million, RMB 2,159 million, RMB 2,737 million, RMB 1,391 million and RMB 1,361 million, respectively.

The recoverable amounts of the Sinopec Yanshan, Sinopec Zhenhai, Sinopec Yangzi, Sinopec Qilu, Sinopec Zhongyuan and Dynamic are determined based on value in use calculations. These calculations use cash flow projections based on financial budgets approved by management covering a one-year period and pre-tax discount rates primarily ranging from 14.2% to 17.2%. Cash flows beyond the one-year period are maintained constant. Management believes any reasonably possible change in the key assumptions on which these entities' recoverable amounts are based would not cause these entities' carrying amounts to exceed their recoverable amounts.

Key assumptions used for the value in use calculations for these entities are the gross margin and sales volume. Management determined the budgeted gross margin based on the gross margin achieved in the period immediately before the budget period and its expectation for the development of international crude oil prices. The sales volume was based on the production capacity and the sales volume in the period immediately before the budget period.

21 INVESTMENTS IN SUBSIDIARIES

	The Company	
	2006	2005
	RMB millions	RMB millions
Investments in subsidiaries, at cost	**66,809**	**75,579**

Details of the Company's principal subsidiaries at 31 December 2006 are set out in Note 39.

22 INVESTMENTS

	The Group		The Company	
	2006	2005	**2006**	2005
	RMB millions	RMB millions	**RMB millions**	RMB millions
Available-for-sale securities	157	119	—	—
Other unlisted investments, at cost	2,741	3,359	1,083	1,140
	2,898	**3,478**	**1,083**	**1,140**
Less: Impairment losses	(316)	(327)	(112)	(103)
	2,582	**3,151**	**971**	**1,037**

Unlisted investments represent the Group's interests in PRC domiciled enterprises which are mainly engaged in non-oil and gas activities and operations. The Group has no significant investments in marketable securities.

The impairment losses relating to investments for the year ended 31 December 2006 amounted to RMB 48 million (2005: RMB 77 million).

23 INTEREST IN ASSOCIATES

	The Group		The Company	
	2006	2005	**2006**	2005
	RMB millions	RMB millions	**RMB millions**	RMB millions
Investments in associates, at cost	—	—	7,470	5,933
Share of net assets	11,617	9,267	—	—
	11,617	**9,267**	**7,470**	**5,933**

The Group's investments in associates are with companies primarily engaged in the oil and gas and chemical operations in the PRC. These investments are individually and in the aggregate not material to the Group's financial condition or results of operations for all periods presented. The share of associates' taxation for the year ended 31 December 2006 was RMB 439 million (2005: RMB 420 million). The principal investments in associates, all of which are incorporated in the PRC, are as follows:

Name of company	Form of business structure	Particulars of issued and paid up capital	Percentage of equity held by the Company %	Percentage of equity held by the Company's subsidiaries %	Principal activities
Sinopec Shandong Taishan Petroleum Company Limited	Incorporated	480,793,320 ordinary shares of RMB 1.00 each	38.68	—	Trading of petroleum products and decoration of service gas stations
Sinopec Finance Company Limited	Incorporated	Registered capital RMB 6,000,000,000	49.00	—	Provision of non-banking financial services
Shanghai Petroleum National Gas Corporation	Incorporated	Registered capital RMB 900,000,000	30.00	—	Exploration and production of crude oil and natural gas
Shanghai Chemical Industry Park Development Company Limited	Incorporated	Registered capital RMB 2,372,439,000	—	38.26	Planning, development and operation of the Chemical Industry Park in Shanghai, the PRC
China Shipping & Sinopec Suppliers Company Limited	Incorporated	Registered capital RMB 876,660,000	—	50.00	Transportation of petroleum products
China Aviation Oil Supply Company Limited	Incorporated	Registered capital RMB 3,800,000,000	—	29.00	Marketing and distribution of refined petroleum products

During the year ended 31 December 2006, the Group acquired 71.4% equity interests in Dynamic, which was previously an associate of the Group, and thereafter, Dynamic became a subsidiary of the Company (Notes 20 and 39).

24 INTEREST IN JOINTLY CONTROLLED ENTITIES

	The Company	
	2006	2005
	RMB millions	RMB millions
Investments in jointly controlled entities, at cost	**7,482**	**7,280**

The Group's principal interests in jointly controlled entities are primarily engaged in the oil and gas and chemical operations in the PRC as follows:

Name of company	Form of business structure	Particulars of issued and paid up capital	Percentage of equity held by the Company %	Percentage of equity held by the Company's subsidiaries %	Principal activities
Shanghai Secco Petrochemical Company Limited	Incorporated	Registered capital USD 901,440,964	30.00	20.00	Manufacturing and distribution of petrochemical products
BASF-YPC Company Limited	Incorporated	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	Incorporated	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	Unincorporated	—	—	43.00	Exploration and production of crude oil and natural gas

Included in the consolidated financial statements are the following items that represent the Group's proportionate share of the jointly controlled entities' results of operation, financial condition and cash flows.

	2006	2005
	RMB millions	RMB millions
Results of operation:		
Operating revenue	17,913	10,082
Expenses	(15,180)	(9,773)
Net profit	**2,733**	**309**
Financial condition:		
Current assets	4,966	2,631
Non-current assets, primarily property, plant and equipment and construction in progress with net book values of RMB 14,259 million (2005: RMB 15,287 million) and RMB 3,582 million (2005: RMB 3,392 million), respectively	18,635	19,522
Current liabilities	(2,736)	(2,543)
Non-current liabilities, primarily long-term bank loans, excluding current portion, of RMB 8,267 million (2005: RMB 10,006 million)	(8,643)	(10,177)
Net assets	**12,222**	**9,433**
Cash flows:		
Net cash generated from/(used in) operating activities	2,452	(1,434)
Net cash used in investing activities	(382)	(2,474)
Net cash (used in)/generated from financing activities	(939)	4,011

25 LONG-TERM PREPAYMENTS AND OTHER ASSETS

Long term prepayments and other assets primarily represent prepaid rental expenses over one year, computer software and catalysts.

26 TRADE ACCOUNTS AND BILLS RECEIVABLES

	The Group		The Company	
	2006	2005	**2006**	2005
	RMB millions	RMB millions	**RMB millions**	RMB millions
Amounts due from third parties	14,601	13,564	4,622	4,136
Amounts due from subsidiaries	—	—	5,570	6,252
Amounts due from Sinopec Group Company and fellow subsidiaries	3,396	3,145	923	518
Amounts due from associates	380	572	8	10
Amounts due from jointly controlled entities	547	505	377	229
	18,924	**17,786**	**11,500**	**11,145**
Less: Impairment losses for bad and doubtful debts	(3,334)	(3,140)	(2,668)	(2,319)
	15,590	**14,646**	**8,832**	**8,826**
Bills receivable	8,757	7,167	2,760	1,334
	24,347	**21,813**	**11,592**	**10,160**

The ageing analysis of trade accounts and bills receivables (net of impairment losses for bad and doubtful debts) is as follows:

	The Group		The Company	
	2006	2005	**2006**	2005
	RMB millions	RMB millions	**RMB millions**	RMB millions
Within one year	24,095	21,552	11,368	10,010
Between one and two years	169	178	158	112
Between two and three years	56	43	43	25
Over three years	27	40	23	13
	24,347	**21,813**	**11,592**	**10,160**

Sales are generally on a cash term. Credit is generally only available for major customers with well-established trading records. Amounts due from Sinopec Group Company and fellow subsidiaries are repayable under the same terms.

27 INVENTORIES

	The Group		The Company	
	2006	2005	**2006**	2005
	RMB millions	RMB millions	**RMB millions**	RMB millions
Crude oil and other raw materials	54,227	53,360	28,956	25,471
Work in progress	9,828	9,422	5,061	4,659
Finished goods	25,762	23,173	17,574	17,980
Spare parts and consumables	4,485	4,456	2,866	2,616
	94,302	**90,411**	**54,457**	**50,726**
Less: Allowance for diminution in value of inventories	(866)	(892)	(469)	(309)
	93,436	**89,519**	**53,988**	**50,417**

The cost of inventories recognised as an expense in the consolidated income statement amounted to RMB 895,290 million for the year ended 31 December 2006 (2005: RMB 682,288 million), including the write-down of inventories amounted to RMB 419 million (2005: RMB 262 million) and the reversal of write-down of inventories made in prior years amounted to RMB 445 million (2005: RMB 276 million) mainly arising from the sales of inventories.

28 PREPAID EXPENSES AND OTHER CURRENT ASSETS

	The Group		The Company	
	2006	2005	**2006**	2005
	RMB millions	RMB millions	**RMB millions**	RMB millions
Advances to third parties	1,732	1,776	893	909
Amounts due from Sinopec Group Company and fellow subsidiaries	2,020	2,965	1,896	2,559
Amounts due from subsidiaries	—	—	4,491	2,964
Other receivables	2,298	1,977	1,166	742
Purchase deposits	3,106	2,496	2,222	1,106
Prepayments in connection with construction work and equipment purchases	4,658	6,613	1,753	4,584
Prepaid value-added tax and customs duty	4,815	4,288	2,496	2,184
Amounts due from associates	332	539	308	508
	18,961	**20,654**	**15,225**	**15,556**

29 DEFERRED TAX ASSETS AND LIABILITIES

Deferred tax assets and deferred tax liabilities are attributable to the items detailed in the table below:

The Group

	Assets		Liabilities		Net balance	
	2006	2005	**2006**	2005	**2006**	2005
	RMB millions	RMB millions	**RMB millions**	RMB millions	**RMB millions**	RMB millions
Current						
Receivables and inventories	3,531	3,448	—	—	3,531	3,448
Accruals	865	456	—	—	865	456
Non-current						
Property, plant and equipment	2,295	1,642	(1,678)	(1,619)	617	23
Accelerated depreciation	—	—	(4,657)	(4,290)	(4,657)	(4,290)
Tax value of losses carried forward, net of valuation allowances	53	128	—	—	53	128
Lease prepayments	351	359	—	—	351	359
Others	63	39	(4)	(66)	59	(27)
Deferred tax assets/(liabilities)	**7,158**	**6,072**	**(6,339)**	**(5,975)**	**819**	**97**

The Company

	Assets		Liabilities		Net balance	
	2006	2005	**2006**	2005	**2006**	2005
	RMB millions	RMB millions	**RMB millions**	RMB millions	**RMB millions**	RMB millions
Current						
Receivables and inventories	3,339	1,226	—	—	3,339	1,226
Accruals	814	409	—	—	814	409
Non-current						
Property, plant and equipment	1,749	1,553	(1,634)	(1,083)	115	470
Accelerated depreciation	—	—	(4,540)	(1,066)	(4,540)	(1,066)
Lease prepayments	17	17	—	—	17	17
Others	17	15	—	(67)	17	(52)
Deferred tax assets/(liabilities)	**5,936**	**3,220**	**(6,174)**	**(2,216)**	**(238)**	**1,004**

As at 31 December 2006, certain subsidiaries of the Company provided valuation allowance against tax value of losses carried forward for PRC income tax purpose of RMB 4,382 million which are available to offset their future PRC taxable income, if any. The tax value of these losses carried forward of RMB 215 million, RMB 341 million, RMB 720 million, RMB 1,185 million and RMB 1,921 million will expire in 2007, 2008, 2009, 2010 and 2011, respectively.

A valuation allowance on deferred tax assets is recorded if it is probable that some portion or all of the deferred tax assets will not be realised through the recovery of taxes previously paid and/or future taxable income. The allowance is subject to ongoing adjustments based on changes in circumstances that affect the Group's assessment on the realisability of the deferred tax assets. The Group has reviewed its deferred tax assets at the balance sheet date. Based on this review, net valuation allowances of RMB 258 million (2005: RMB 391 million) were provided for the year ended 31 December 2006. The Group determined the valuation allowance based on management's assessment of the probability that taxable profit will be available over the period which the deferred tax assets can be realised or utilised. In assessing the probability, both positive and negative evidence was considered, including whether it is probable that the operations will have future taxable profits over the periods which the deferred tax assets are deductible or utilised and whether the tax losses result from identifiable causes which are unlikely to recur. Based on this assessment, a valuation allowance was provided to reduce the deferred tax asset to the amount that is probable to be realised.

29 DEFERRED TAX ASSETS AND LIABILITIES *(Continued)*

Movements in the deferred tax assets and liabilities are as follows:

The Group

	Balance at 1 January 2005 RMB millions	Recognised in consolidated income statement RMB millions	Recognised in other reserve RMB millions	Balance at 31 December 2005 RMB millions
Current				
Receivables and inventories	2,260	1,188	—	3,448
Accruals	268	188	—	456
Non-current				
Property, plant and equipment	(138)	161	—	23
Accelerated depreciation	(4,000)	(290)	—	(4,290)
Tax value of losses carried forward, net of valuation allowance	66	62	—	128
Lease prepayments	366	(7)	—	359
Others	32	(59)	—	(27)
Net deferred tax (liabilities)/assets	**(1,146)**	**1,243**	**—**	**97**

	Balance at 1 January 2006 RMB millions	Recognised in consolidated income statement RMB millions	Recognised in other reserve RMB millions	Balance at 31 December 2006 RMB millions
Current				
Receivables and inventories	3,448	83	—	3,531
Accruals	456	409	—	865
Non-current				
Property, plant and equipment	23	594	—	617
Accelerated depreciation	(4,290)	(367)	—	(4,657)
Tax value of losses carried forward, net of valuation allowance	128	(75)	—	53
Lease prepayments	359	(8)	—	351
Others (Note)	(27)	90	(4)	59
Net deferred tax assets/(liabilities)	**97**	**726**	**(4)**	**819**

Note:

The amount recognised in equity represents the tax effect of change in fair value of available-for-sale securities, which was recognised directly in equity.

The Company

	Balance at 1 January 2005 RMB millions	Transferred from subsidiaries RMB millions	Recognised in income statement RMB millions	Balance at 31 December 2005 RMB millions
Current				
Receivables and inventories	1,999	—	(773)	1,226
Accruals	246	—	163	409
Non-current				
Property, plant and equipment	474	—	(4)	470
Accelerated depreciation	(1,042)	—	(24)	(1,066)
Lease prepayments	16	—	1	17
Others	6	—	(58)	(52)
Net deferred tax assets/(liabilities)	**1,699**	**—**	**(695)**	**1,004**

	Balance at 1 January 2006 RMB millions	Transferred from subsidiaries RMB millions	Recognised in income statement RMB millions	Balance at 31 December 2006 RMB millions
Current				
Receivables and inventories	1,226	2,066	47	3,339
Accruals	409	—	405	814
Non-current				
Property, plant and equipment	470	(494)	139	115
Accelerated depreciation	(1,066)	(3,102)	(372)	(4,540)
Lease prepayments	17	—	—	17
Others	(52)	—	69	17
Net deferred tax assets/(liabilities)	**1,004**	**(1,530)**	**288**	**(238)**

30 SHORT-TERM AND LONG-TERM DEBTS AND LOANS FROM SINOPEC GROUP COMPANY AND FELLOW SUBSIDIARIES

Short-term debts represent:

	The Group		The Company	
	2006	2005	**2006**	2005
	RMB millions	RMB millions	**RMB millions**	RMB millions
Third parties' debts				
Short-term bank loans	**25,666**	**15,392**	**15,045**	**3,094**
Current portion of long-term bank loans	15,291	14,879	13,308	12,043
Current portion of long-term other loans	27	26	3	1
Current portion of long-term bank loans of jointly controlled entities	490	193	—	—
	15,808	**15,098**	**13,311**	**12,044**
Corporate bonds (a)	**11,885**	**9,921**	**9,885**	**9,921**
	53,359	**40,411**	**38,241**	**25,059**
Loans from Sinopec Group Company and fellow subsidiaries				
Short-term loans	4,849	2,705	806	3,846
Current portion of long-term loans	552	100	552	100
	5,401	**2,805**	**1,358**	**3,946**
	58,760	**43,216**	**39,599**	**29,005**

The Group's and the Company's weighted average interest rate on short-term loans were 5.2% (2005: 4.0%) and 4.7 % (2005: 3.2%) at 31 December 2006, respectively.

Long-term debts comprise:

	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 denominated	Interest rates ranging from interest free to 6.9 % per annum at 31 December 2006 with maturities through 2016	65,484	65,069	55,457	54,792
Japanese Yen denominated	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 denominated	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 denominated	Fixed interest rate at 6.7% per annum at 31 December 2006 with maturities through 2010	101	117	101	117
Hong Kong Dollar denominated	Floating rate at Hong Kong Prime Rate plus 0.8% to 1.1% per annum at 31 December 2005 with maturities through 2007; Paid off as at 31 December 2006	—	94	—	—
		70,379	**73,730**	**59,463**	**61,874**
Long-term other loans					
Renminbi denominated	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 denominated	Interest rates ranging from interest free to 2.0% per annum at 31 December 2006 with maturities through 2015	44	51	30	34
		3,142	**221**	**3,037**	**71**
Corporate bonds					
Renminbi denominated	Fixed interest rate at 4.61% per annum at 31 December 2006 with maturity in February 2014 (b)	**3,500**	**3,500**	**3,500**	**3,500**
		77,021	**77,451**	**66,000**	**65,445**

30 SHORT-TERM AND LONG-TERM DEBTS AND LOANS FROM SINOPEC GROUP COMPANY AND FELLOW SUBSIDIARIES *(Continued)*

		The Group		The Company	
	Interest rate and final maturity	**2006**	2005	**2006**	2005
		RMB millions	RMB millions	**RMB millions**	RMB millions
Long-term bank loans of jointly controlled entities					
Renminbi denominated	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 denominated	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	—	—
		8,757	**10,006**	**—**	**—**
Total third parties' long-term debts		**85,778**	**87,457**	**66,000**	**65,445**
Less: Current portion		(15,808)	(15,098)	(13,311)	(12,044)
		69,970	**72,359**	**52,689**	**53,401**
Long-term loans from Sinopec Group Company and fellow subsidiaries					
Renminbi denominated	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
Long-term loans of jointly controlled entities from Sinopec Group Company and fellow subsidiaries					
Renminbi denominated	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	—	—
Less: Current portion		(552)	(100)	(552)	(100)
		39,095	**39,933**	**38,840**	**39,212**
		109,065	**112,292**	**91,529**	**92,613**

(a) 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 of 2.54% per annum. The Company redeemed the corporate bonds 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, with an effective yield 3.83% per annum. The bonds mature in December 2007.

(b) The Company issued ten-year corporate bonds of RMB 3.5 billion to PRC citizens as well as PRC legal and non-legal persons on 24 February 2004 with a fixed interest rate at 4.61% per annum.

Third parties' loans of RMB 171 million of the Group at 31 December 2006 (2005: RMB 35 million) were secured by certain of the Group's property, plant and equipment. The net book value of property, plant and equipment of the Group pledged as security amounted to RMB 288 million at 31 December 2006 (2005: RMB 83 million).

Third parties' loans of RMB 46 million of the Company at 31 December 2006 (2005: RMB 13 million) were secured by certain of the Company's property, plant and equipment. The net book value of property, plant and equipment of the Company pledged as security amounted to RMB 75 million at 31 December 2006 (2005: RMB 10 million).

The aggregate maturities of long-term debts and loans from Sinopec Group Company and fellow subsidiaries are as follows:

	The Group		The Company	
	2006	2005	**2006**	2005
	RMB millions	RMB millions	**RMB millions**	RMB millions
Within one year	16,360	15,198	13,863	12,144
Between one and two years	26,529	19,787	24,590	16,420
Between two and five years	36,205	43,442	26,147	34,771
After five years	46,331	49,063	40,792	41,422
	125,425	**127,490**	**105,392**	**104,757**

30 SHORT-TERM AND LONG-TERM DEBTS AND LOANS FROM SINOPEC GROUP COMPANY AND FELLOW SUBSIDIARIES *(Continued)*

Included in short-term and long-term debts and loans from Sinopec Group Company and fellow subsidiaries of the Group are the following amounts denominated in a currency other than the functional currency of the entity to which they relate:

	2006 millions	2005 millions
US Dollars	USD985	USD2,158
Japanese Yen	JPY41,350	JPY50,507
Euro	EUR10	EUR12
Hong Kong Dollars	HKD7,789	HKD128

31 TRADE ACCOUNTS AND BILLS PAYABLES

	The Group		The Company	
	2006 RMB millions	2005 RMB millions	**2006 RMB millions**	2005 RMB millions
Amounts due to third parties	49,177	50,353	17,213	12,032
Amounts due to subsidiaries	—	—	19,775	15,805
Amounts due to Sinopec Group Company and fellow subsidiaries	2,194	2,763	1,049	996
Amounts due to jointly controlled entities	750	650	—	—
Amounts due to associates	4	51	4	—
	52,125	**53,817**	**38,041**	**28,833**
Bills payable	21,685	23,243	16,265	19,077
	73,810	**77,060**	**54,306**	**47,910**

Amounts due to Sinopec Group Company and fellow subsidiaries are repayable in accordance with normal commercial terms.

The maturities of trade accounts and bills payables are as follows:

	The Group		The Company	
	2006 RMB millions	2005 RMB millions	**2006 RMB millions**	2005 RMB millions
Due within 1 month or on demand	44,303	45,044	32,295	23,251
Due after 1 month but within 6 months	29,386	31,704	21,937	24,353
Due after 6 months	121	312	74	306
	73,810	**77,060**	**54,306**	**47,910**

32 ACCRUED EXPENSES AND OTHER PAYABLES

	The Group		The Company	
	2006 RMB millions	2005 RMB millions	**2006 RMB millions**	2005 RMB millions
Amounts due to Sinopec Group Company and fellow subsidiaries	12,670	8,133	9,757	4,538
Amounts due to subsidiaries	—	—	16,191	7,032
Accrued expenditures	23,266	19,660	18,384	13,984
Taxes other than income tax	6,313	3,092	5,048	1,415
Receipts in advance	18,513	12,375	15,473	9,133
Advances from third parties	1,356	1,226	1,305	1,100
Others	6,938	5,037	6,155	3,357
	69,056	**49,523**	**72,313**	**40,559**

33 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 domestic state-owned shares with a par value of RMB 1.00 each. Such shares were issued to Sinopec Group Company in consideration for the assets and liabilities of the Predecessor Operations transferred to the Company (Note 1).

Pursuant to the resolutions passed at an Extraordinary General Meeting held on 25 July 2000 and approvals from relevant government authorities, the Company is authorised to increase its share capital to a maximum of 88.3 billion shares with a par value of RMB 1.00 each and offer not more than 19.5 billion shares with a par value of RMB 1.00 each to investors outside the PRC. Sinopec Group Company is authorised to offer not more than 3.5 billion shares of its shareholdings in the Company to investors outside the PRC. The shares sold by Sinopec Group Company to investors outside the PRC would be converted into H shares.

In October 2000, the Company issued 15,102,439,000 H shares with a par value of RMB 1.00 each, representing 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 per H share and US$ 20.645 per ADS, respectively, by way of a global initial public offering to Hong Kong and overseas investors. As part of the global initial public offering, 1,678,049,000 domestic state-owned ordinary shares of RMB 1.00 each owned by Sinopec Group Company were converted into H shares and sold to Hong Kong and overseas investors.

In July 2001, the Company issued 2.8 billion domestic listed A shares with a par value of RMB 1.00 each at RMB 4.22 by way of a public offering to natural persons and institutional investors in the PRC.

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 they held, in exchange for the approval for the listing of all state-owned A shares. The 784,000,000 stated-owned A shares paid to the shareholders of listed A shares were tradable on 10 October 2006. The 66,337,551,000 domestic stated-owned A shares have been granted trading right upon settlement of the above consideration.

All A shares and H shares rank pari passu in all material aspects.

34 RESERVES

	The Group		The Company	
	2006	2005	**2006**	2005
	RMB millions	RMB millions	**RMB millions**	RMB millions
Capital reserve				
Balance at 1 January	(19,217)	(19,217)	13,672	13,672
Transfer from capital reserve to other reserves	(2,373)	—	(1,628)	—
Balance at 31 December	**(21,590)**	**(19,217)**	**12,044**	**13,672**
Share premium				
Balance at 1 January/31 December	**18,072**	**18,072**	**18,072**	**18,072**
Revaluation reserve				
Balance at 1 January	26,342	27,998	—	—
Revaluation surplus realised	(1,590)	(1,656)	—	—
Balance at 31 December	**24,752**	**26,342**	**—**	**—**
Statutory surplus reserve				
Balance at 1 January	13,514	9,558	13,514	9,558
Appropriation	5,066	3,956	5,066	3,956
Statutory public welfare fund transferred to statutory surplus reserve	13,514	—	13,514	—
Balance at 31 December	**32,094**	**13,514**	**32,094**	**13,514**
Statutory public welfare fund				
Balance at 1 January	13,514	9,558	13,514	9,558
Appropriation	—	3,956	—	3,956
Statutory public welfare fund transferred to statutory surplus reserve	(13,514)	—	(13,514)	—
Balance at 31 December	**—**	**13,514**	**—**	**13,514**
Discretionary surplus reserve				
Balance at 1 January	7,000	7,000	7,000	7,000
Appropriation	20,000	—	20,000	—
Balance at 31 December	**27,000**	**7,000**	**27,000**	**7,000**
Other reserves				
Balance at 1 January, as adjusted	987	547	242	247
Change in fair value of available-for-sale securities, net of deferred tax	34	—	—	—
Realisation of deferred tax on land use rights	(7)	(5)	(7)	(5)
Transfer from retained earnings to other reserves	1,013	535	—	—
Transfer from capital reserve to other reserves	2,373	—	1,628	—
Distribution to Sinopec Group Company	(631)	(90)	(1,628)	—
Consideration for Acquisition of Oil Production Plants (Note 1)	(3,500)	—	—	—
Balance at 31 December	**269**	**987**	**235**	**242**
Retained earnings				
Balance at 1 January	77,387	53,122	20,591	(4,211)
Profit for the year attributable to equity shareholders of the Company	53,912	41,455	57,895	43,113
Final dividend for 2004 (Note 16)	—	(6,936)	—	—
Interim dividend for 2005 (Note 16)	—	(3,468)	—	—
Final dividend for 2005 (Note 16)	(7,803)	—	(7,803)	(6,936)
Interim dividend for 2006 (Note 16)	(3,468)	—	(3,468)	(3,468)
Appropriation	(25,066)	(7,912)	(25,066)	(7,912)
Revaluation surplus realised	1,590	1,656	—	—
Realisation of deferred tax on land use rights	7	5	7	5
Transfer from retained earnings to other reserves	(1,013)	(535)	—	—
Balance at 31 December	**95,546**	**77,387**	**42,156**	**20,591**
	176,143	**137,599**	**131,601**	**86,605**

35 COMMITMENTS AND CONTINGENT LIABILITIES

Operating lease commitments

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

	The Group		The Company	
	2006	2005	**2006**	2005
	RMB millions	RMB millions	**RMB millions**	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
Thereafter	122,406	95,176	120,638	93,601
	145,171	**112,309**	**142,554**	**110,289**

35 COMMITMENTS AND CONTINGENT LIABILITIES *(Continued)*

Capital commitments
At 31 December 2006 and 31 December 2005, capital commitments are as follows:

	2006 RMB millions	2005 RMB millions
The Group		
Authorised and contracted for	113,192	75,069
Authorised but not contracted for	165,967	85,575
	279,159	**160,644**
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 investments and interest in associates.

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 is given by the State Council. The maximum term of production licenses issued to the Group is 55 years as a special dispensation was given to the Group 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 RMB millions	2005 RMB millions	**2006 RMB millions**	2005 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
Thereafter	226	239	226	108
	663	**640**	**663**	**419**

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 and 2005, guarantees given to banks in respect of banking facilities granted to the parties below were as follows:

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

The Group monitors the conditions that are subject to the guarantees to identify whether it is probable that a loss has occurred, and recognise any such losses under guarantees when those losses are estimable. At 31 December 2006 and 2005, it is not probable that the Group will be required to make payments under the guarantees. Thus no liability has been accrued for a loss related to the Group's obligation under these guarantee arrangements.

35 COMMITMENTS AND CONTINGENT LIABILITIES *(Continued)*

Environmental contingencies

To date, the Group has not incurred any significant expenditures 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 fees 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 believes that any resulting liabilities will not have a material adverse effect on the financial position or operating results of the Group.

36 RELATED PARTY TRANSACTIONS

Parties are considered to be related to the Group if the Group has the ability, directly or indirectly, to control or jointly control the party or exercise significant influence over the party in making financial and operating decisions, or vice versa, or where the Group and the party are subject to common control or common significant influence. Related parties may be individuals (being members of key management personnel, significant shareholders and/or their close family members) or other entities and include entities which are under the significant influence of related parties of the Group where those parties are individuals, and post-employment benefit plans which are for the benefit of employees of the Group or of any entity that is a related party of the Group.

(a) Transactions with Sinopec Group Company and fellow subsidiaries, associates and jointly controlled entities

The Group is part of a larger group of companies under Sinopec Group Company, which is owned by the PRC government, and has significant transactions and relationships with Sinopec Group Company and fellow subsidiaries. Because of these relationships, it is possible that the terms of these transactions are not the same as those that would result from transactions among wholly unrelated parties.

The principal related party transactions with Sinopec Group Company and fellow subsidiaries, associates and jointly controlled entities, which were carried out in the ordinary course of business, are as follows:

	Note	**2006 RMB millions**	2005 RMB millions
Sales of goods	(i)	129,221	95,043
Purchases	(ii)	56,703	45,923
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	1,036
Net deposits withdrawn from related parties	(xii)	(3,910)	(67)
Net loans obtained from/(repaid to) related parties	(xiii)	1,758	(4,714)

The amounts set out in the table above in respect of the year ended 31 December 2006 and 2005 represent the relevant costs to the Group 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. Guarantees given to banks by the Group in respect of banking facilities to associates and jointly controlled entities are disclosed in Note 35.

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 materials 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.

36 RELATED PARTY TRANSACTIONS *(Continued)*

(a) Transactions with Sinopec Group Company and fellow subsidiaries, associates and jointly controlled entities *(Continued)*

(iv) Exploration and development services comprise direct costs incurred in the exploration and development 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 equipment.

(viii) Agency commission income represents commission earned for acting as an agent in respect of sales of products and purchase of materials for 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. The balance of deposits at 31 December 2006 was RMB 689 million (2005: RMB 4,599 million).

(xi) Interest paid represents interest charges on the loans and advances obtained from Sinopec Group Company and Sinopec Finance Company Limited.

(xii) Deposits withdrawn from related parties represent net deposits withdrawn from Sinopec Finance Company Limited.

(xiii) The Group obtained loans from/repaid loans to Sinopec Group Company and Sinopec Finance Company Limited.

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. The terms of these agreements are summarised as follows:

(a) The Company has entered into a non-exclusive Agreement for Mutual Provision of Products and Ancillary Services ("Mutual Provision Agreement") with Sinopec Group Company effective from 1 January 2000 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 has agreed 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 a non-exclusive 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 series 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, however such amount cannot 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 stations franchise agreement with Sinopec Group Company effective from 1 January 2000 under which its service stations and retail stores would exclusively sell the refined products supplied by the Group.

As discussed in Note 1, pursuant to the resolution passed at the Directors' meeting on 10 October 2006, the Group acquired equity interests in Sinopec Hainan for cash of RMB 2,990 million. Sinopec Hainan was previously wholly owned by Sinopec Group Company.

As discussed in Note 1, pursuant to the resolution passed at the Directors' meeting on 6 December 2006, the Group acquired the equity interests of Oil Production Plants from Sinopec Group Company, for a total consideration of RMB 3,500 million payable in 2007.

36 RELATED PARTY TRANSACTIONS *(Continued)*

(a) Transactions with Sinopec Group Company and fellow subsidiaries, associates and jointly controlled entities *(Continued)*

Amounts due from/to Sinopec Group Company and fellow subsidiaries, associates and jointly controlled entities included in the following accounts captions are summarised as follows:

	2006 RMB millions	2005 RMB millions
Trade accounts receivable	4,323	4,222
Prepaid expenses and other current assets	2,352	3,504
Total amounts due from Sinopec Group Company and fellow subsidiaries, associates and jointly controlled entities	**6,675**	**7,726**
Trade accounts payable	2,948	3,464
Accrued expenses and other payables	12,670	8,133
Short-term loans and current portion of long-term loans from Sinopec Group Company and fellow subsidiaries	5,401	2,805
Long-term loans excluding current portion from Sinopec Group Company and fellow subsidiaries	39,095	39,933
Total amounts due to Sinopec Group Company and fellow subsidiaries, associates and jointly controlled entities	**60,114**	**54,335**

Amounts due from/to Sinopec Group Company and fellow subsidiaries, associates and jointly controlled entities, other than short-term loans and long-term loans, bear no interest, are unsecured and are repayable in accordance with normal commercial terms. The terms and conditions associated with short-term loans and long-term loans payable to Sinopec Group Company and fellow subsidiaries are set out in Note 30.

As at and for the year ended 31 December 2006 and 2005, no impairment losses for bad and doubtful debts were recorded in respect of amounts due from Sinopec Group Company and fellow subsidiaries, associates and jointly controlled entities.

(b) Key management personnel emoluments

Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the Group, directly or indirectly, including directors and supervisors of the Group. The key management personnel compensations are as follows:

	2006 RMB'000	2005 RMB'000
Short-term employee benefits	4,571	2,868
Retirement scheme contributions	184	115
	4,755	**2,983**

Total emoluments are included in "personnel expenses" as disclosed in Note 7.

(c) Contributions to defined contribution retirement plans

The Group participates in various defined contribution retirement plans organised by municipal and provincial governments for its staff. The details of the Group's employee benefits plan are disclosed in Note 37. As at 31 December 2006 and 2005, there was no material outstanding contribution to post-employment benefit plans.

(d) Transactions with other state-controlled entities in the PRC

The Group is a state-controlled energy and chemical enterprise and operates in an economic regime currently dominated by entities directly or indirectly controlled by the PRC government through its government authorities, agencies, affiliations and other organisations (collectively referred as "state-controlled entities").

Apart from transactions with Sinopec Group Company and fellow subsidiaries, the Group has transactions with other state-controlled entities include but not limited to the following:

- sales and purchase of goods and ancillary materials;
- rendering and receiving services;
- lease of assets;
- depositing and borrowing money; and
- use of public utilities.

These transactions are conducted in the ordinary course of the Group's business on terms comparable to those with other entities that are not state-controlled. The Group has established its procurement policies, pricing strategy and approval process for purchases and sales of products and services which do not depend on whether the counterparties are state-controlled entities or not.

Having considered the transactions potentially affected by related party relationships, the entity's pricing strategy, procurement policies and approval processes, and the information that would be necessary for an understanding of the potential effect of the related party relationship on the financial statements, the directors are of the opinion that the following related party transactions require disclosure of numeric details:

36 RELATED PARTY TRANSACTIONS *(Continued)*

(d) Transactions with other state-controlled entities in the PRC *(Continued)*

(i) Transactions with other state-controlled energy and chemical companies

The Group's major domestic suppliers of crude oil and refined petroleum products are China National Petroleum Corporation and its subsidiaries ("CNPC Group") and China National Offshore Oil Corporation and its subsidiaries ("CNOOC Group"), which are state-controlled entities.

During the year ended 31 December 2006, the aggregate amount of crude oil purchased by refining segment from CNPC and CNOOC Group and refined petroleum purchased by marketing and distribution segment from CNPC Group was RMB 60,863 million (2005: RMB 58,957 million).

The aggregate amounts due from/to CNPC Group and CNOOC Group are summarised as follows:

	2006 RMB millions	2005 RMB millions
Trade accounts receivable	111	213
Prepaid expenses and other current assets	115	120
Total amounts due from CNPC Group and CNOOC Group	**226**	**333**
Trade accounts payable	1,231	1,237
Accrued expenses and other payables	7	127
Total amounts due to CNPC Group and CNOOC Group	**1,238**	**1,364**

(ii) Transactions with state-controlled banks

The Group deposits its cash with several state-controlled banks in the PRC. The Group also obtains short-term and long-term loans from these banks in the ordinary course of business. The interest rates of the bank deposits and loans are regulated by the PBOC. The Group's interest income from and interest expense to these state-controlled banks in the PRC are as follows:

	2006 RMB millions	2005 RMB millions
Interest income	458	323
Interest expense	6,001	4,878

The amounts of cash deposited at and loans from state-controlled banks in the PRC are summarised as follows:

	2006 RMB millions	2005 RMB millions
Cash and cash equivalents	7,366	9,418
Time deposits with financial institutions	615	964
Total deposits at state-controlled banks in the PRC	**7,981**	**10,382**
Short-term loans and current portion of long-term loans	34,803	27,891
Long-term loans excluding current portion of long-term loans	62,346	67,641
Total loans from state-controlled banks in the PRC	**97,149**	**95,532**

37 EMPLOYEE BENEFITS PLAN

As stipulated by the regulations of the PRC, the Group participates in various defined contribution retirement plans organised by municipal and provincial governments for its staff. The Group is required to make contributions to the retirement plans at rates ranging from 17.0% to 30.0% of the salaries, bonuses and certain allowances of its staff. A member of the plan is entitled to a pension equal to a fixed proportion of the salary prevailing at his or her retirement date. The Group has no other material obligation for the payment of pension benefits associated with these plans beyond the annual contributions described above. The Group's contributions for the year ended 31 December 2006 were RMB 2,270 million (2005: RMB 2,273 million).

38 SEGMENTAL REPORTING

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, that is sourced from the exploration and production segment of the Group and external suppliers, and manufactures and sells petroleum products to the chemicals and marketing and distribution segments of the Group and external customers.

(iii) Marketing and distribution, which owns and operates oil depots and service stations in the PRC, and distributes and sells refined petroleum products (mainly gasoline and diesel) in the PRC through wholesale and retail sales networks.

(iv) Chemicals, which manufactures and sells petrochemical products, derivative petrochemical products and other chemical products mainly to external customers.

(v) Corporate and 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 corporate 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.

38 SEGMENTAL REPORTING *(Continued)*

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

	2006 RMB millions	2005 RMB millions
Turnover		
Exploration and production		
External sales	23,355	20,006
Inter-segment sales	105,656	84,423
	129,011	**104,429**
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 sale	12,299	12,199
	221,432	**172,982**
Corporate and 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)
Turnover	**1,044,652**	**799,259**
Other operating revenues		
Exploration and production	14,155	10,756
Refining	4,590	5,421
Marketing and distribution	687	1,358
Chemicals	6,661	5,841
Corporate and others	657	637
Other operating revenues	**26,750**	**24,013**
Other income		
Refining	5,000	9,415
Total other income	**5,000**	**9,415**
Turnover, other operating revenues and other income	**1,076,402**	**832,687**

	2006 RMB millions	2005 RMB millions
Result		
Operating profit		
By segment		
– Exploration and production	63,182	48,334
– Refining	(25,298)	(3,536)
– Marketing and distribution	30,234	10,350
– Chemicals	17,234	14,296
– Corporate and others	(1,532)	(1,198)
Total operating profit	**83,820**	**68,246**
Share of profits less losses from associates		
– Exploration and production	233	326
– Refining	58	23
– Marketing and distribution	404	241
– Chemicals	20	1
– Corporate and others	232	266
Aggregate share of profits less losses from associates	**947**	**857**
Finance costs		
Interest expense	(7,437)	(5,926)
Interest income	555	384
Foreign exchange losses	(153)	(79)
Foreign exchange gains	935	996
Net finance costs	**(6,100)**	**(4,625)**
Investment income	256	178
Profit before taxation	**78,923**	**64,656**
Taxation	(23,515)	(19,880)
Profit for the year	**55,408**	**44,776**

38 SEGMENTAL REPORTING *(Continued)*

Assets and liabilities dedicated to a particular segment's operations are included in that segment's total assets and liabilities. Assets which benefit more than one segment or are considered to be corporate assets are not allocated. "Unallocated assets" consists primarily of cash and cash equivalents, time deposits with financial institutions, investments and deferred tax assets. "Unallocated liabilities" consists primarily of short-term and long-term debts, loans from Sinopec Group Company and fellow subsidiaries, income tax payable, deferred tax liabilities and other liabilities.

Interests in and share of profits from associates are included in the segments in which the associates operate. Information on associates is included in Note 23. Additions to long-lived assets by operating segment are included in Notes 18 and 19.

	2006 RMB millions	2005 RMB millions
Assets		
Segment assets		
— Exploration and production	155,043	127,471
— Refining	163,898	142,776
— Marketing and distribution	108,053	102,935
— Chemicals	125,051	115,942
— Corporate and others	22,641	20,570
Total segment assets	**574,686**	**509,694**
Interest in associates		
— Exploration and production	1,063	1,494
— Refining	1,117	571
— Marketing and distribution	4,692	4,298
— Chemicals	1,245	1,092
— Corporate and others	3,500	1,812
Aggregate interest in associates	**11,617**	**9,267**
Unallocated assets	**25,487**	**30,079**
Total assets	**611,790**	**549,040**
Liabilities		
Segment liabilities		
— Exploration and production	30,082	20,262
— Refining	30,162	27,311
— Marketing and distribution	27,090	23,713
— Chemicals	19,619	19,442
— Corporate and others	35,913	35,855
Total segment liabilities	**142,866**	**126,583**
Unallocated liabilities	**184,135**	**167,477**
Total liabilities	**327,001**	**294,060**

Segment capital expenditure is the total cost incurred during the year to acquire segment assets that are expected to be used for more than one year.

	2006 RMB millions	2005 RMB millions
Capital expenditure		
Exploration and production	31,734	23,095
Refining	21,969	19,100
Marketing and distribution	11,319	10,954
Chemicals	12,629	9,386
Corporate and others	2,170	1,164
	79,821	**63,699**
Capital expenditure of Oil Production Plants		
Exploration and production	**3,362**	**1,612**
Capital expenditure of jointly controlled entities		
Exploration and production	102	772
Chemicals	160	1,830
	262	**2,602**
Depreciation, depletion and amortisation		
Exploration and production	12,945	11,118
Refining	7,733	7,055
Marketing and distribution	3,452	3,026
Chemicals	9,697	9,697
Corporate and others	408	722
	34,235	**31,618**
Impairment losses on long-lived assets		
Exploration and production	552	60
Marketing and distribution	23	366
Chemicals	250	1,425
	825	**1,851**

39 PRINCIPAL SUBSIDIARIES

At 31 December 2006, the following list contains the particulars of subsidiaries which principally affected the results or assets of the Group.

Name of company	Particulars of issued capital (millions)	Type of legal entity	Percentage of equity held by the Company %	Percentage of equity held by the Company's subsidiary %	Principal activities
China Petrochemical International Company Limited	RMB 1,663	Limited company	100.00	—	Trading of petrochemical products
Sinopec Sales Company Limited	RMB 1,700	Limited company	100.00	—	Marketing and distribution of refined petroleum products
Sinopec Zhenhai Refining and Chemical Company Limited (Note 20)	RMB 2,524	Limited company	100.00	—	Manufacturing of intermediate petrochemical products and petroleum products
Sinopec Qilu Petrochemical Company Limited (Note 20)	RMB 1,950	Limited company	99.76	—	Manufacturing of intermediate petrochemical products and petroleum products
Sinopec Yangzi Petrochemical Company Limited (Note 20)	RMB 2,330	Limited company	99.81	—	Manufacturing of intermediate petrochemical products and petroleum products
Sinopec Zhongyuan Petroleum Company Limited (Note 20)	RMB 875	Limited company	99.35	—	Exploration and production of crude oil and natural gas
Sinopec Shengli Oil Field Dynamic Company Limited (Note 20)	RMB 364	Limited company	97.71	—	Exploration and production of crude oil and distribution of petrochemical products
Sinopec Fujian Petrochemical Company Limited (i)	RMB 2,253	Limited company	50.00	—	Manufacturing of plastics, intermediate petrochemical products and petroleum products
Sinopec Shanghai Petrochemical Company Limited	RMB 7,200	Limited company	55.56	—	Manufacturing of synthetic fibres, resin and plastics, intermediate petrochemical products and petroleum products
Sinopec Shijiazhuang Refining Chemical Company Limited	RMB 1,154	Limited company	79.73	—	Manufacturing of intermediate petrochemical products and petroleum products
Sinopec Kantons Holdings Limited	HK$ 104	Limited company	—	72.40	Trading of crude oil and petroleum products
Sinopec Wuhan Petroleum Group Company Limited (i)	RMB 147	Limited company	46.25	—	Marketing and distribution of refined petroleum products
Sinopec Yizheng Chemical Fibre Company Limited (i)	RMB 4,000	Limited company	42.00	—	Production and sale of polyester chips and polyester fibres
Sinopec Zhongyuan Petrochemical Company Limited	RMB 2,400	Limited company	93.51	—	Manufacturing of chemical products
Sinopec Shell (Jiangsu) Petroleum Marketing Company Limited	RMB 830	Limited company	60.00	—	Marketing and distribution of refined petroleum products
BP Sinopec (Zhejiang) Petroleum Company Limited	RMB 800	Limited company	60.00	—	Marketing and distribution of refined petroleum products
Sinopec Qingdao Refining and Chemical Company Limited	RMB 800	Limited company	85.00	—	Manufacturing of intermediate petrochemical products and petroleum products
China International United Petroleum and Chemical Company Limited	RMB 223	Limited company	100.00	—	Trading of crude oil and petrochemical products
Sinopec Hainan Refining and Chemical Company Limited	RMB 3,986	Limited company	75.00	—	Manufacturing of intermediate petrochemical products and petroleum products

Except for Sinopec Kantons Holdings Limited, which is incorporated in Bermuda, all of the above principal subsidiaries are incorporated in the PRC.

(i) The Group consolidated the results of the entity because the Group controlled the board of this entity and had the power to govern its financial and operating policies.

(ii) During the year ended 31 December 2006, the Company disposed the 211,423,651 A shares, representing approximately 40.72% of the issued share capital, in Sinopec Wuhan Phoenix Company Limited pursuant to an agreement entered into with a third party. No significant disposal gain or loss was recorded from this transaction.

40 FINANCIAL INSTRUMENTS

Financial assets of the Group include cash and cash equivalents, time deposits with financial institutions, investments, trade accounts receivable, bills receivable, amounts due from Sinopec Group Company and fellow subsidiaries, advances to third parties, amounts due from associates, and other receivables. Financial liabilities of the Group include bank and other loans, loans from Sinopec Group Company and fellow subsidiaries, trade accounts payable, bills payable, amounts due to Sinopec Group Company and fellow subsidiaries, receipts in advance, and advances from third parties. The Group has no derivative instruments that are designated and qualified as hedging instruments at 31 December 2006 and 2005.

Credit risk

The carrying amounts of cash and cash equivalents, time deposits with financial institutions, trade accounts and bills receivables, and other current assets, except for prepayments and deposits, represent the Group's maximum exposure to credit risk in relation to financial assets.

The majority of the Group's trade accounts receivable relate to sales of petroleum and chemical products to related parties and third parties operating in the petroleum and chemical industries. The Group performs ongoing credit evaluations of its customers' financial condition and generally does not require collateral on trade accounts receivable. The Group maintains an impairment loss for doubtful accounts and actual losses have been within management's expectations. No single customer accounted for greater than 10% of total revenues.

No other financial assets carry a significant exposure to credit risk.

Currency risk

Substantially all of the revenue-generating operations of the Group are transacted in Renminbi, which is not fully convertible into foreign currencies. On 1 January 1994, the PRC government abolished the dual rate system and introduced a single rate of exchange as quoted by the PBOC. However, the unification of the exchange rate does not imply convertibility of Renminbi into United States dollars or other foreign currencies. All foreign exchange transactions continue to take place either through the PBOC or other banks authorised to buy and sell foreign currencies at the exchange rates quoted by the PBOC. Approval of foreign currency payments by the PBOC or other institutions requires submitting a payment application form together with suppliers' invoices, shipping documents and signed contracts.

With the authorisation from the PRC government, the PBOC announced that the PRC government reformed the exchange rate regime by moving into a managed floating exchange rate regime based on market supply and demand with reference to a basket of currencies on 21 July 2005.

Other than the amounts as disclosed in Note 30, the amounts of other financial assets and liabilities of the Group are substantially denominated in the functional currency of respective entity of the Group.

Interest rate risk

The interest rates and terms of repayment of short-term and long-term debts of the Group are disclosed in Note 30.

Fair values

The disclosures of the fair value estimates, methods and assumptions, set forth below for the Group's financial instruments, are made to comply with the requirements of IAS 32 and IAS 39 and should be read in conjunction with the Group's consolidated financial statements and related notes. The estimated fair value amounts have been determined by the Group using market information and valuation methodologies considered appropriate. However, considerable judgement is required to interpret market data to develop the estimates of fair value. Accordingly, the estimates presented herein are not necessarily indicative of the amounts the Group could realise in a current market exchange. The use of different market assumptions and/or estimation methodologies may have a material effect on the estimated fair value amounts.

The following table presents the carrying amount and fair value of the Group's long-term indebtedness other than loans from Sinopec Group Company and fellow subsidiaries at 31 December 2006 and 31 December 2005:

	2006 RMB millions	2005 RMB millions
Carrying amount	85,778	87,457
Fair value	85,376	87,461

The fair value of long-term indebtedness is estimated by discounting future cash flows thereon using current market interest rates offered to the Group for debts with substantially the same characteristics and maturities.

Unquoted equity securities are individually and in the aggregate not material to the Group's financial condition or results of operations. There are no listed market prices for such interests in the PRC and, accordingly, a reasonable estimate of fair value could not be made without incurring excessive costs.

The fair values of all other financial instruments approximate their carrying amounts due to the nature or short-term maturity of these instruments.

41 ACCOUNTING ESTIMATES AND JUDGEMENTS

The Group's financial condition and results of operations are sensitive to accounting methods, assumptions and estimates that underlie the preparation of the financial statements. The Group bases the assumptions and estimates on historical experience and on various other assumptions that the Group believes to be reasonable and which form the basis for making judgements about matters that are not readily apparent from other sources. On an on-going basis, management evaluates its estimates. Actual results may differ from those estimates as facts, circumstances and conditions change.

The selection of critical accounting policies, the judgements and other uncertainties affecting application of those policies and the sensitivity of reported results to changes in conditions and assumptions are factors to be considered when reviewing the financial statements. The principal accounting policies are set forth in Note 2. The Group believes the following critical accounting policies involve the most significant judgements and estimates used in the preparation of the financial statements.

Oil and gas properties and reserves

The accounting for the exploration and production's oil and gas activities is subject to accounting rules that are unique to the oil and gas business. There are two methods to account for oil and gas business activities, the successful efforts method and the full cost method. The Group has elected to use the successful efforts method. The successful efforts method reflects the volatility that is inherent in exploring for mineral resources in that costs of unsuccessful exploratory efforts are charged to expense as they are incurred. These costs primarily include dry hole costs, seismic costs and other exploratory costs. Under the full cost method, these costs are capitalised and written-off or depreciated over time.

Engineering estimates of the Group's oil and gas reserves are inherently imprecise and represent only approximate amounts because of the subjective judgements involved in developing such information. There are authoritative guidelines regarding the engineering criteria that have to be met before estimated oil and gas reserves can be designated as "proved". Proved and proved developed reserves estimates are updated at least annually and take into account recent production and technical information about each field. In addition, as prices and cost levels change from year to year, the estimate of proved and proved developed reserves also changes. This change is considered a change in estimate for accounting purposes and is reflected on a prospective basis in related depreciation rates.

Despite the inherent imprecision in these engineering estimates, these estimates are used in determining depreciation expense and impairment expense. Depreciation rates are determined based on estimated proved developed reserve quantities (the denominator) and capitalised costs of producing properties (the numerator). Producing properties' capitalised costs are amortised based on the units of oil or gas produced.

Impairment for long lived assets

If circumstances indicate that the net book value of a long-lived asset may not be recoverable, the asset may be considered "impaired", and an impairment loss may be recognised in accordance with IAS 36 "Impairment of Assets". The carrying amounts of long-lived assets are reviewed periodically in order to assess whether the recoverable amounts have declined below the carrying amounts. These 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 recoverable amount. For goodwill, the recoverable amount is estimated annually. The recoverable amount is the greater of the net selling price and the value in use. It is difficult to precisely estimate selling price because quoted market prices for the Group's assets or cash-generating units are not readily available. In determining the value in use, expected cash flows generated by the asset or the cash-generating unit are discounted to their present value, which requires significant judgement relating to level of sale volume, selling price and amount of operating costs. The Group uses all readily available information in determining an amount that is a reasonable approximation of recoverable amount, including estimates based on reasonable and supportable assumptions and projections of sale volume, selling price and amount of operating costs.

Depreciation

Property, plant and equipment, other than oil and gas properties, are depreciated on a straight-line basis over the estimated useful lives of the assets, after taking into account the estimated residual value. The Group reviews the estimated useful lives of the assets regularly in order to determine the amount of depreciation expense to be recorded during any reporting period. The useful lives are based on the Group's historical experience with similar assets and taking into account anticipated technological changes. The depreciation expense for future periods is adjusted if there are significant changes from previous estimates.

Impairment for bad and doubtful debts

The Group estimates impairment losses for bad and doubtful debts resulting from the inability of the customers to make the required payments. The Group bases the estimates on the aging of the accounts receivable balance, customer credit-worthiness, and historical write-off experience. If the financial condition of the customers were to deteriorate, actual write-offs would be higher than estimated.

42 POSSIBLE IMPACT OF AMENDMENTS, NEW STANDARDS AND INTERPRETATIONS ISSUED BUT NOT YET EFFECTIVE FOR THE ANNUAL ACCOUNTING PERIOD ENDING 31 DECEMBER 2006

Up to the date of issue of these financial statements, the IASB has issued the following amendments, new standards and interpretations which are not yet effective for the annual accounting period ending 31 December 2006 and which have not been adopted in these financial statements:

	Effective for accounting period beginning on or after
IFRS 7, Financial instruments: disclosures	1 January 2007
IFRS 8, Operating Segments	1 January 2009
IFRIC 7, Applying the restatement approach under IAS 29, Financial reporting in hyperinflationary economies	1 March 2006
IFRIC 8, Scope of IFRS 2	1 May 2006
IFRIC 9, Reassessment of Embedded Derivatives	1 June 2006
IFRIC 10, Interim financial reporting and impairment	1 November 2006
IFRIC 11, IFRS2- Group and treasury share transaction	1 March 2007
IFRIC 12, Service concession arrangements	1 January 2008
Amendment to IAS 1, Presentation of financial statements: capital disclosures	1 January 2007

The Group is in the process of making an assessment of what the impact of these amendments, new standards and new interpretations is expected to be in the period of initial application. Up to the date of issuance of these financial statements, the Group believes that the adoption of IFRIC 7, IFRIC 8, IFRIC 9, IFRIC 10, IFRIC 11, IFRIC 12 and the amendment to IAS 1 are not applicable to any of the Group's operations and that the adoption of the remainder of the above new standards and new interpretations is unlikely to have a significant impact on the Group's results of operations and financial position.

43 POST BALANCE SHEET EVENT

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.

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.

44 PARENT AND ULTIMATE HOLDING COMPANY

The directors consider the parent and ultimate holding company of the Group as at 31 December 2006 is Sinopec Group Company, a state-owned enterprise established in the PRC. This entity does not produce financial statements available for public use.