Notes to Financial Statements

December 31, 2003

1. GROUP REORGANISATION AND BASIS OF PRESENTATION OF FINANCIAL STATEMENTS

China Oilfield Services Limited (the "Company") was established on December 25, 2001 by China National Offshore Oil Corporation ("CNOOC"), a State-owned enterprise in the People's Republic of China (the "PRC"), in Tianjin, the PRC, as a limited liability company under the Company Laws of the PRC. As part of the reorganisation (the "Reorganisation") of CNOOC in preparation for the listing of the Company's shares on The Stock Exchange of Hong Kong Limited (the "HKSE") and pursuant to an approval document obtained from the relevant government authority dated September 26, 2002, the Company was restructured into a joint stock limited liability company. Pursuant to the Reorganisation which was effective on April 30, 2002, the Company acquired from the wholly-owned subsidiaries of CNOOC:

(1) the assets, liabilities and undertakings which principally relate to the business of the provision of oilfield services including drilling services, well services, marine support and transportation services and geophysical services offshore China (the "Relevant Businesses"), with the exclusion of certain cash and cash equivalents of RMB688 million and a payable to CNOOC of RMB688 million; and

(2) the interests in certain joint ventures which principally carry on the business of the provision of oilfield services including well services and geophysical services offshore China (the "Relevant Companies").

In consideration of the above acquisition, the Company in total issued 2,600 million State legal person shares of par value of RMB1.00 each to CNOOC, and the Company's registered and paid-up capital became RMB2,600 million accordingly.

The prior year comparative figures included in the Group's financial statements are presented using the following bases:

i) The Reorganisation involved companies under common control. The Relevant Businesses and the Relevant Companies are regarded as a continuing group. Accordingly, for information purposes, the pro forma combined profit and loss accounts, and the pro forma cash flow statement for the year ended December 31, 2002 have been prepared which include the operating results of the Relevant Businesses and the Relevant Companies as if the current Group structure had been in existence throughout the year ended December 31, 2002.

ii) The Company did not acquire the Relevant Businesses and the Relevant Companies until April 30, 2002. As such, there were no results of operations prior to April 30, 2002. The consolidated profit and loss account, the consolidated statement of changes in equity and the consolidated cash flow statement for the period from December 25, 2001 (date of establishment of the Company) to December 31, 2002 include the activities of the Group for the period from May 1, 2002 to 31 December, 2002.

2. CORPORATE INFORMATION

The registered office of China Oilfield Services Limited is located at 3-1516 Hebei Road, Haiyang New and Hi-Tech Development Zone, Tanggu, Tianjin 300451, China.

The principal activities of the Group consisted of the provision of oilfield services including drilling services, well services, marine support and transportation services, and geophysical services offshore China.

In the opinion of the directors, the Company's ultimate holding company is CNOOC.

3. IMPACT OF NEW AND REVISED STATEMENTS OF STANDARD ACCOUNTING PRACTICE ("SSAPs")

The SSAP12 (revised) "Income tax" is effective for the first time for the current year's financial statements. The revised SSAP12 prescribes the accounting for income taxes payable or recoverable, arising from the taxable profit or loss for the current period (current tax); and income taxes payable or recoverable in future periods, principally arising from taxable and deductible temporary differences and the carry forward of unused tax losses (deferred tax).

The SSAP has had no significant impact for these financial statements on the amounts recorded for income taxes. However, the related note disclosures are now more extensive than previously required. These are detailed in notes 12 and 26 to the financial statements and include a reconciliation between the accounting profit and the tax expense for the year.

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICES

Basis of preparation

These financial statements have been prepared in accordance with Hong Kong Statements of Standard Accounting Practice, accounting principles generally accepted in Hong Kong and the disclosure requirements of Hong Kong Companies Ordinance. They have been prepared under the historical cost convention, except for the periodic remeasurement of short term investments as further explained below.

Basis of consolidation

The consolidated financial statements include the financial statements of the Company and its subsidiaries. The results of the subsidiaries acquired or disposed of during the year are consolidated from or to its effective date of acquisition or disposal, respectively. All significant intercompany transactions and balances within the Group are eliminated on consolidation.

Subsidiaries

A subsidiary is a company whose financial and operating policies the Company controls, directly or indirectly, so as to obtain benefits from its activities.

The results of subsidiaries are included in the Company's profit and loss account to the extent of dividends received and receivable. The Company's investments in subsidiaries are stated at cost less any impairment losses.

Jointly-controlled entities

A jointly-controlled entity is a joint venture company which is subject to joint control, resulting in none of the participating parties having unilateral control over the economic activity of the jointly-controlled entity.

The Group's share of the post-acquisition results and reserves of jointly-controlled entities is included in the consolidated profit and loss account and consolidated reserves, respectively. The Group's interests in jointly-controlled entities are stated in the consolidated balance sheet at the Group's share of net assets under the equity method of accounting, less any impairment losses.

The results of jointly-controlled entities are included in the Company's profit and loss account to the extent of dividends received and receivable. The Company's investments in jointly-controlled entities are treated as long term assets and are stated at cost less any impairment losses.

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICES continued

Related parties

Parties are considered to be related if one party has the ability, directly or indirectly, to control the other party or exercise significant influence over the other party in making financial and operating decisions. Parties are also considered to be related if they are subject to common control or common significant influence. Related parties may be individuals or corporate entities.

Impairment of assets

An assessment is made at each balance sheet date of whether there is any indication of impairment of any asset, or whether there is any indication that an impairment loss previously recognised for an asset in prior years may no longer exist or may have decreased. If any such indication exists, the asset's recoverable amount is estimated. An asset's recoverable amount is calculated at the higher of the asset's value in use or its net selling price.

An impairment loss is recognised only if the carrying amount of an asset exceeds its recoverable amount. An impairment loss is charged to the profit and loss account in the period in which it arises, unless the asset is carried at a revalued amount, when the impairment loss is accounted for in accordance with the relevant accounting policy for that revalued asset.

A previously recognised impairment loss is reversed only if there has been a change in the estimates used to determine the recoverable amount of an asset, however not to an amount higher than the carrying amount that would have been determined (net of any depreciation/amortisation), had no impairment loss been recognised for the asset in prior years. A reversal of an impairment loss is credited to the profit and loss account in the period in which it arises, unless the asset is carried at a revalued amount, when the reversal of the impairment loss is accounted for in accordance with the relevant accounting policy for that revalued asset.

Property, plant and equipment, and depreciation

Property, plant and equipment, other than investment properties and construction in progress, are stated at cost less accumulated depreciation and any impairment losses. The cost of an asset comprises its purchase price and any directly attributable costs of bringing the asset to its working condition and location for its intended use. Expenditure incurred after fixed assets have been put into operation, such as repairs and maintenance, is normally charged to the profit and loss account in the period in which it is incurred. In situations where it can be clearly demonstrated that the expenditure has resulted in an increase in the future economic benefits expected to be obtained from the use of the fixed asset, the expenditure is capitalised as an additional cost of that asset.

Depreciation is calculated on the straight-line basis to write off the cost less residual value of each asset over its estimated useful life. The estimated useful lives of property, plant and equipment are as follows:

Vessels	10-15 years
Tankers	20 years
Drilling equipment	25 years
Machinery and equipment	5-10 years
Motor vehicles	5 years

The gain or loss on disposal or retirement of property, plant and equipment recognised in the profit and loss account is the difference between the net sales proceeds and the carrying amount of the relevant asset.

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICES continued

Construction in progress

Construction in progress represents vessels and equipment under construction, which is stated at cost less any impairment losses, and is not depreciated. Cost comprises the direct costs of construction and capitalised borrowing costs on related borrowed funds during the period of construction.

Construction in progress is reclassified to the appropriate category of property, plant and equipment when completed and ready for use.

Short term investments

Short term investments held for investment purpose are stated at their fair value on the basis of their quoted market prices at the balance sheet date on an individual investment basis. The gains or loses arising from changes in the fair value of debt securities are credited or changed to the profit and loss account in the period in which they arise.

Inventories

Inventories primarily consist of materials and supplies used for repairs and maintenance of plant and equipment and daily operations. Inventories are stated at the lower of cost and net realisable value after allowances for obsolete or slow-moving items. Cost is determined on the weighted average basis. Materials and supplies are capitalised to plant and equipment when used for renewals or betterments of plant and equipment or recognised as expenses when used for daily operations.

Cash and cash equivalents

For the purpose of the consolidated cash flow statement, cash and cash equivalents comprise cash on hand and demand deposits, and short term highly liquid investments which are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value, and have a short maturity of generally within three months when acquired, less bank overdrafts which are repayable on demand and form an integral part of the Group's cash management.

For the purpose of the balance sheet, cash and cash equivalents comprise cash on hand and at banks, including term deposits which are not restricted as to use.

Provisions

A provision is recognised when a present obligation (legal or constructive) has arisen as a result of a past event and it is probable that a future outflow of resources will be required to settle the obligation, provided that a reliable estimate can be made of the amount of the obligation.

When the effect of discounting is material, the amount recognised for a provision is the present value at the balance sheet date of the future expenditures expected to be required to settle the obligation. The increase in the discounted present value amount arising from the passage of time is included in finance costs in the profit and loss account.

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICES continued

Income tax

Income tax comprises current and deferred tax. Income tax is recognised in the profit and loss account or in equity if it relates to items that are recognised in the same or a different period, directly in equity.

Deferred tax is provided, using the liability method, on all temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred tax liabilities are recognised for all taxable temporary differences:

- except where the deferred tax liability arises from goodwill or the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and

- in respect of taxable temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, except where the timing of the reversal of the temporary difference can be controlled and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred tax assets are recognised for all deductible temporary differences, carryforward of unused tax assets and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carryforward of unused tax assets and unused tax losses can be utilized:

- except where the deferred tax asset relating to the deductible temporary differences arises from negative goodwill or the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and

- in respect of deductible temporary differences associated with investments in subsidiaries, associates and interest in joint ventures, deferred tax assets are only recognised to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary difference can be utilised.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised. Conversely, previously unrecognized deferred tax assets are recognised to the extent that it is probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilized.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the period when the asset is realized or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the balance sheet date.

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICES continued

Revenue recognition

Revenue is recognised when it is probable that the economic benefits will flow to the Group and when the revenue can be measured reliably, on the following bases:

(a) income from day rate contracts is recognised as and when services are performed;

(b) income from turnkey contracts is recognised to the extent of costs incurred until the specific turnkey depth and other contract requirements are met. When the turnkey depth and contract requirements are met, revenue on turnkey contracts is recognized based on the percentage of completion. Provisions for future losses on turnkey contracts are recognised when it becomes apparent that expenses to be incurred on a specific contract will exceed the revenue from that contract;

(c) interest income, on a time proportion basis taking into account the principal outstanding and the effective interest rate applicable; and

(d) dividends, when the shareholders' right to receive payment has been established.

Research and development costs

All research costs are charged to the profit and loss account as incurred.

Expenditure incurred on projects to develop new products is capitalised and deferred only when the projects are clearly defined; the expenditure is separately identifiable and can be measured reliably; there is reasonable certainty that the projects are technically feasible; and the products have commercial value. Product development expenditure which does not meet these criteria is expensed when incurred.

Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, i.e. assets that necessarily take a substantial period of time to get ready for their intended use or sale, are capitalised as part of the cost of those assets. The capitalisation of such borrowing costs ceases when the assets are substantially ready for their intended use or sale. Investment income earned on the temporary investment of specific borrowings pending their expenditure on qualifying assets is deducted from the borrowing costs capitalised.

Retirement benefits costs

The Company's employees in the PRC are required to participate in a central pension scheme administered by local municipal governments. The Company is required to contribute 19%-22% of its payroll costs of the central pension scheme.

Dividends

Final and interim dividends proposed by the directors are classified as a separate allocation of retained earnings within capital and reserves in the balance sheet, until they have been approved by the shareholders in a general meeting. When these dividends have been approved by the shareholders and declared, they are recognised as a liability.

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICES continued

Foreign currencies

Foreign currency transactions are recorded at the applicable exchange rates ruling at the transaction dates. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated at the applicable exchange rates ruling at that date. Exchange differences are dealt with in the profit and loss account.

During the year, substantially all the transactions were denominated in Renminbi. Accordingly, exchange differences recorded during the period were minimal.

On consolidation, the balance sheet of overseas subsidiaries, joint-controlled entities and associates are translated into Renminbi at the applicable exchange rates ruling at the balance sheet date whereas the profit and loss account of overseas subsidiaries, jointly-controlled entities and associates are translated into Renminbi at the weighted average exchange rates for the year. The resulting translation differences are included in the exchange fluctuation reserves.

Operating leases

Leases where substantially all the rewards and risks of ownership of assets remain with the lessor are accounted for as operating leases. Rentals applicable to such operating leases are charged to the profit and loss account on the straight-line basis over the lease terms.

5. SEGMENT INFORMATION

The Group is engaged in a broad range of petroleum related activities through its four major business segments: drilling services, well services, marine support and transportation services, and geophysical services.

The Group's operating businesses are structured and managed separately, according to the nature of their operations and the services they provide. Each of the Group's business segments represents a strategic business unit that provides services which are subject to risks and returns that are different from those of other business segments. Summary details of the business segments are as follows:

(a) the drilling services segment is engaged in the provision of oilfield drilling services and well workovers;

(b) the well services segment is engaged in the provision of logging and downhole services, such as drilling fluids, directional drilling, cementing and well completion;

(c) the marine support and transportation segment is engaged in the transportation of materials, supplies and personnel to offshore facilities, moving and positioning drilling structures and the transportation of crude oil and refined products; and

(d) the geophysical segment is engaged in the provision of offshore seismic data collection, marine surveying and data processing services.

No further analysis of geographical segment information is presented as almost all of the Group's assets, operations and customers are located in the PRC, which is considered as one geographic location in an economic environment with similar risks and returns.

5. SEGMENT INFORMATION continued

The following table presents revenue, profit and certain asset, liability and expenditure information for the Group's business segments for the year ended December 31, 2003:

	Drilling RMB'000	Well services RMB'000	Marine support and transportation RMB'000	Geophysical RMB'000	Total RMB'000
TURNOVER					
Sales (including intersegment)	1,381,807	705,641	666,769	498,773	3,252,990
Less: Intersegment sales	99,309	33,119	34,797	23,510	190,735
Total sales to external customers	1,282,498	672,522	631,972	475,263	3,062,255
PROFIT FROM OPERATIONS					
Segment results	279,148	110,530	79,238	80,859	549,775
Exchange losses, net					(716)
Interest expenses					—
Interest income					32,175
Share of profits of jointly-controlled entities					48,932
Profit before tax					630,166
Tax					(164,260)
Net profit					465,906
ASSETS					
Segment assets	2,268,247	845,927	2,160,158	435,750	5,710,082
Interests in jointly-controlled entities	—	137,171	—	11,736	148,907
Unallocated assets					2,372,066
Total assets					8,231,055
LIABILITIES					
Segment liabilities	93,220	28,355	33,000	15,582	170,157
Unallocated liabilities					1,515,762
					1,685,919
OTHER INFORMATION					
Capital expenditure	200,065	365,912	509,949	38,266	1,114,192
Depreciation of property, plant and equipment	243,238	87,506	205,427	57,832	594,003
Provision for doubtful debts	26,058	333	333	270	26,994
Write back of inventories	(151)	(78)	(75)	(55)	(359)

5. SEGMENT INFORMATION continued

The following table presents pro forma combined revenue, profit and certain asset, liability and expenditure information for the Group's business segments for the year ended December 31, 2002:

	Drilling RMB'000	Well services RMB'000	Marine Support and transportation RMB'000	Geophysical RMB'000	Total RMB'000
	(note 1)	(note 1)	(note 1)	(note 1)	(note 1)
TURNOVER					
Sales (including intersegment)	1,084,242	671,612	602,710	387,046	2,745,610
Less: Intersegment sales	19,828	—	—	—	19,828
Total sales to external customers	1,064,414	671,612	602,710	387,046	2,725,782
PROFIT FROM OPERATIONS					
Segment results	266,834	92,376	111,679	12,133	483,022
Exchange losses, net					(973)
Interest expenses					(5,289)
Interest income					11,216
Share of profits of jointly-controlled entities					42,600
Profit before tax					530,576
Tax					(176,190)
Net profit					354,386
ASSETS					
Segment assets	2,276,915	466,014	1,868,210	441,228	5,052,367
Interests in jointly-controlled entities	—	130,752	—	10,411	141,163
Unallocated assets					2,764,002
Total assets					7,957,532
LIABILITIES					
Segment liabilities	623,358	88,716	192,651	51,709	956,434
Unallocated liabilities					820,503
					1,776,937
OTHER INFORMATION					
Capital expenditure	134,609	120,563	465,064	43,256	763,492
Depreciation of property, plant and equipment	205,409	112,100	162,837	72,177	552,523
Write back of doubtful debts	(665)	(104)	(146)	(125)	(1,040)
Write back of inventories	(510)	(319)	(64)	(18)	(911)

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5. SEGMENT INFORMATION continued

The following table presents consolidated revenue, profit and certain asset, liability and expenditure information for the Group's business segments for the period from December 25, 2001 (date of establishment of the Company) to December 31, 2002:

	Drilling RMB'000	Well services RMB'000	Marine support and transportation RMB'000	Geophysical RMB'000	Total RMB'000
TURNOVER					
Sales (including intersegment)	760,573	465,995	409,411	316,558	1,952,537
Less: Intersegment sales	17,358	—	—	—	17,358
Total sales to external customers	743,215	465,995	409,411	316,558	1,935,179
PROFIT FROM OPERATIONS					
Segment results	165,118	31,100	44,945	34,716	275,879
Exchange losses, net					(869)
Interest expenses					(3,545)
Interest income					7,847
Share of profits of jointly-controlled entities					33,524
Profit before tax					312,836
Tax					(103,371)
Net profit					209,465
ASSETS					
Segment assets	2,276,915	466,014	1,868,210	441,228	5,052,367
Interests in jointly-controlled entities	—	130,752	—	10,411	141,163
Unallocated assets					2,764,002
Total assets					7,957,532
LIABILITIES					
Segment liabilities	623,358	88,716	192,651	51,709	956,434
Unallocated liabilities					820,503
					1,776,937
OTHER INFORMATION					
Capital expenditure	124,464	98,316	383,095	15,410	621,285
Depreciation of property, plant and equipment	143,058	94,206	129,236	39,543	406,043
Write back of doubtful debts	(1,515)	(736)	(532)	(706)	(3,489)
Provision for/(write back) of inventories	405	(176)	(71)	(12)	146

6. TURNOVER AND OTHER REVENUES

Turnover represents the net invoiced value of offshore oilfield services rendered, net of sales surtaxes. All significant intragroup transactions have been eliminated on consolidation/combination.

Other revenues comprise the following:

	Consolidated for the year ended December 31, 2003 RMB'000	Pro forma combined for the year ended December 31, 2002 RMB'000	Consolidated for the period from December 25, 2001 (date of establishment) to December 31, 2002 RMB'000
		(note 1)	(note 1)
Other revenues:			
Gain on disposal of scrap materials	**106**	2	2
Others	**11,614**	4,598	3,834
	11,720	4,600	3,836

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7. PROFIT FROM OPERATING ACTIVITIES

The Group's profit from operating activities is arrived at after charging/(crediting):

	Consolidated for the year ended December 31, 2003 RMB'000	Pro forma combined for the year ended December 31, 2002 RMB'000	Consolidated for the period from December 25, 2001 (date of establishment) to December 31, 2002 RMB'000
		(note 1)	(note 1)
Auditors' remuneration	**2,900**	3,071	2,800
Employee compensation costs:			
Wages, salaries and bonuses	**369,998**	325,109	224,869
Social security costs	**110,409**	105,265	60,695
Retirement benefits contributions (note11)	**32,691**	31,919	18,087
	513,098	462,293	303,651
Depreciation of property, plant and equipment	**594,003**	552,523	406,043
Loss on disposal of property, plant and equipment, net	**2,469**	2,236	2,062
Minimum lease payment under operating leases in respect of land and buildings, berths and equipment	**121,526**	61,522	54,135
Provision for/(write back) of doubtful debts	**26,994**	(1,040)	(3,489)
Provision for/(write back) of inventories	**(359)**	(911)	146
Repair and maintenance costs	**172,139**	152,693	138,749
Research and development costs included in:			
Depreciation of property, plant and equipment	**7,214**	8,671	8,052
Employee compensation costs	**8,273**	8,533	7,844
Repair and maintenance costs	**442**	608	607
Consumption of supplies, materials, fuel, services and others	**10,101**	7,900	7,691
Other operating expenses	**7,064**	5,491	3,363
	33,094	31,203	27,557

8. INTEREST EXPENSES

	Group		
	Consolidated for the year ended December 31, 2003 RMB'000	Pro forma combined for the year ended December 31, 2002 RMB'000	Consolidated for the period from December 25, 2001 (date of establishment) to December 31, 2002 RMB'000
		(note 1)	(note 1)
Interest on bank loans and other loans wholly repayable within five years	**—**	5,444	3,595
Less: Interest capitalised	**—**	155	50
	—	5,289	3,545

9. DIRECTORS' AND SUPERVISORS' REMUNERATION

Directors' and supervisors' remuneration for the year, disclosed pursuant to the Listing Rules and Section 161 of the Hong Kong Companies Ordinance is as follows:

	Group		
	Consolidated for the year ended December 31, 2003 RMB'000	Pro forma combined for the year ended December 31, 2002 RMB'000	Consolidated for the period from December 25, 2001 (date of establishment) to December 31, 2002 RMB'000
		(note 1)	(note 1)
Fees	**429**	133	133
Basic salaries, housing, benefits, other allowances and benefits in kind	**304**	386	295
Bonuses	**762**	389	328
Pension scheme contributions	**34**	135	109
	1,529	1,043	865

Fees are payable to the independent non-executive directors (2002: RMB130,000). There were no other emoluments payable to the independent non-executive directors during the year (2002: Nil).

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9. DIRECTORS' AND SUPERVISORS' REMUNERATION continued

The remunerations of each of the directors and supervisors during the year and 2002 fell within the band of nil to RMB1,000,000.

There was no arrangement under which a director or a supervisor waived or agreed to waive any remuneration during the year.

There was no emolument paid by the Group to the directors or supervisors as an inducement to join or upon joining the Group or as compensation for loss of office during the year.

10. FIVE HIGHEST PAID EMPLOYEES

The five highest paid employees during the year included one director (2002: one), details of whose remuneration are set out in note 9 above. Details of the remuneration of the remaining four (2002: four) non-director, non-supervisor, highest paid employees for the year are as follows:

	Group		
	Consolidated for the year ended December 31, 2003 RMB'000	Pro forma combined for the year ended December 31, 2002 RMB'000	Consolidated for the period from December 25, 2001 (date of establishment) to December 31, 2002 RMB'000
		(note 1)	(note 1)
Basic salaries, housing benefits, other allowances and benefits in kind	**492**	637	429
Bonuses	**1,240**	685	554
Pension scheme contributions	**58**	233	173
	1,790	1,555	1,156

The remunerations of each of the non-director, non-supervisor, highest paid employees during the year and 2002 fell within the band of nil to RMB1,000,000.

There was no emolument paid by the Group to the employees as an inducement to join or upon joining the Group or as compensation for loss of office during the year.

11. RETIREMENT BENEFITS

All the Group's full-time employees in the PRC are covered by a government-regulated pension, and are entitled to an annual pension determined by their basic salaries upon their retirement. The PRC government is responsible for the pension liabilities to these retired employees. The Group is required to make annual contributions to the government-regulated pension at rates ranging from 19% to 22% of the employees' basic salaries. The related pension costs are expensed as incurred.

As part of the CNOOC group, the employees of the Group were entitled to supplementary pension benefits (the "Supplementary Pension Benefits") provided by CNOOC in addition to the benefits under the government-regulated pension fund described above. The Supplementary Pension Benefits were calculated based on factors including number of years of services and salary level on the date of retirement of the employees. Following the Reorganisation, CNOOC agreed with the Group that the Supplementary Pension Benefits of the Group's current employees attributed to the period prior to the Company's public listing in Hong Kong and the Supplementary Pension Benefits of the Group's retired employees will continue to be assumed by CNOOC. As the obligations under the Supplementary Pension Benefits have been fully assumed by CNOOC, the costs of such supplemental pension have not been recorded in the Group's financial statements for the year ended December 31, 2003 (2002: Nil).

In 1999, the CNOOC group implemented an early retirement plan for certain employees, and as part of the CNOOC group, the pension benefits payable to the early retired employees of the Group prior to their joining the government-regulated pension scheme described above were assumed by CNOOC. Upon reaching the normal retirement age, the employees that took early retirement are entitled to both the government-regulated pension scheme and the Supplementary Pension Benefits. Following the Reorganisation, the employees of the Group that took early retirement were all transferred to CNOOC and CNOOC has agreed to continue to assume the pension benefits obligations payable to such former employees until they reach their respective normal retirement ages when they can join the government-regulated pension scheme and are entitled to the Supplementary Pension Benefits. As the Group was not liable to any pension benefit obligations payable to the employees that took early retirement, the pension costs of these individuals have not been recorded in the Group's financial statements for the year ended December 31, 2003 (2002: Nil).

The expenses attributed to the PRC government-regulated pension are as follows:

	Group		
	Consolidated for the year ended December 31, 2003 RMB'000	Pro forma combined for the year ended December 31, 2002 RMB'000	Consolidated for the period from December 25, 2001 (date of establishment) to December 31, 2002 RMB'000
		(note 1)	(note 1)
Contributions to PRC government-regulated pension scheme *(note 7)*	**32,691**	31,919	18,087

At December 31, 2003, the Group had no forfeited contributions available to reduce its contributions to the pension scheme in future years (2002: Nil).

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12. TAX

The Group is subject to income tax on an entity basis on profit arising in or derived from the tax jurisdictions in which members of the Group are domiciled and operate. The Group is not liable for income tax in Hong Kong as it does not have assessable income currently sourced from Hong Kong.

Prior to the Reorganisation on April 30, 2002, the filing of tax returns of the Company was handled by CNOOC on a group basis. The share of the Company's income tax liability was determined based on the applicable tax rate on the Company's profits determined in accordance with PRC accounting principles applicable to state-owned enterprises. Such tax was payable to CNOOC which in turn would settle the tax liability with the relevant tax bureau. Following the Reorganisation, the Company became subject to enterprise income tax at the rate of 33% and the Company now settles its tax liability by itself with the respective tax authorities.

During the year, the application by the Company as an advanced technology enterprise for tax purposes was approved and the Company's enterprise income tax rate for the period from October 1, to December 31, 2002 (being the period after the restructuring of the Company into a joint stock limited liability company on September 26, 2002) was reduced from 33% to 15%. As a result, a tax refund of RMB45.5 million relating to the period from October 1, to December 31, 2002 has been recorded by the Company. The eligibility for such tax rate reduction in the future is conditional upon the fulfillment of certain conditions on an annual basis as stipulated in the relevant tax rules, which include a minimum proportion of sales of advanced technology services to total sales and a minimum proportion of research and development expenses to each of total expenses and total revenues under the PRC accounting principles.

As a reduction in the enterprise income tax rate from 33% to 15% for the year ended December 31, 2003 cannot the ascertained at the date of this report, management considers it appropriate to use 33% to accrue for the income tax liability of the Company for the year ended December 31, 2003.

The Company's newly incorporated subsidiary in Malaysia, COSL (Labuan) Company Limited, is subject to income tax and branch profit tax at an aggregate rate of 6.6% for its gross services income generated from drilling activities in Indonesia.

The determination of current and deferred income tax was based on enacted tax rates.

12. TAX continued

An analysis of the Group's provision for tax is as follows:

	Group		
	Consolidated for the year ended December 31, 2003 RMB'000	Pro forma combined for the year ended December 31, 2002 RMB'000	Consolidated for the period from December 25, 2001 (date of establishment) to December 31, 2002 RMB'000
		(note 1)	
Hong Kong profits tax:	**—**	—	—
Overseas income taxes:			
Current income taxes	**89**	271	226
Deferred income taxes	**—**	—	—
PRC corporate income tax:			
Current income taxes	**225,766**	295,704	183,950
Tax refund	**(45,532)**	—	—
Deferred income taxes *(note 26)*	**(26,332)**	(134,001)	(94,001)
Share of tax attributable to:			
Jointly-controlled entities	**10,269**	14,216	13,196
Total tax charge for the year	**164,260**	176,190	103,371

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December 31, 2003

12. TAX continued

A reconciliation of the tax expense applicable to profit before tax using the statutory rate for the Mainland China in which the Company and its jointly calculated entities are domiciled to the tax expense at the effective tax rate and a reconciliation of the applicable rate (i.e., the statutory tax rate) to the effective tax rate is as follows:

	Consolidated for the year ended December 31, 2003		Pro forma combined for the year ended December 31, 2002		Consolidated for the period from December 25, 2001 (date of establishment) to December 31, 2002	
	RMB'000	**%**	RMB'000	%	RMB'000	%
Profit before tax	**630,166**		530,576		312,836	
Tax at the statutory tax rate of 33% (2002: 33%)	**207,955**	**33.0**	175,090	33.0	103,236	33.0
Lower tax rates for special provinces or local authority	**(7,060)**	**(1.1)**	—	—	—	—
Tax refund	**(45,532)**	**(7.2)**	—	—	—	—
Expenses not deductible for tax	**8,897**	**1.4**	1,100	0.2	135	—
Total tax charge at the Group's effective rate	**164,260**	**26.1**	176,190	33.2	103,371	33.0

13. NET PROFIT FROM ORDINARY ACTIVITIES ATTRIBUTABLE TO SHAREHOLDERS

The net profit from ordinary activities attributable to shareholders for the year ended December 31, 2003 dealt with in the financial statements of the Company is RMB438,241,000 (2002: RMB207,558,000).

14. DIVIDENDS/PROFIT DISTRIBUTIONS

	Consolidate for the year ended December 31, 2003 RMB'000	Pro forma combined for the year ended December 31, 2002 RMB'000	Consolidated for the period from December 25, 2001 (date of establishment) to December 31, 2002 RMB'000
		(note 1)	(note 1)
Profit distributions	—	344,921	—
Special interim dividend-RMB1.23 cents (2002: Nil) per ordinary share	49,026	—	—
Proposed final dividend - RMB2.27cents (2002: 1.31cents) per ordinary share	90,694	52,339	52,339
	139,720	397,260	52,339

The proposed final dividend for the year is subject to the approval of the Company's shareholders at the forthcoming annual general meeting.

Cash dividends to shareholders in Hong Kong will be paid in Hong Kong dollars.

In connection with the Reorganization and in preparation for the listing of the Company shares on HKSE on November 20, 2002, the Company declared a special distributions of RMB 344.9 million for the four months ended April 30, 2002.

Following the establishment of the Company, under the PRC Company Law and the Company's articles of association, net profit after tax as reported in the PRC statutory financial statements can only be distributed as dividends after allowance has been made for the following:

(i) making up prior years' cumulative losses, if any;

(ii) allocations to the statutory common reserve fund of at least 10% of after-tax profit, until the fund aggregates 50% of the Company's registered capital. For the purpose of calculating the transfer to reserves, the profit after tax shall be the amount determined under PRC accounting principles. The transfer to this reserve must be made before any distribution of dividends to shareholders.

The statutory common reserve can be used to offset previous years' losses, if any, and part of the statutory common reserve can be capitalised as the Company's share capital provided that the amount of such reserve remaining after the capitalisation shall not be less than 25% of the registered capital of the Company;

Notes to Financial Statements

December 31, 2003

14. DIVIDENDS/PROFIT DISTRIBUTIONS continued

(iii) allocations of 5% to 10% of after-tax profit, as determined under PRC accounting principles and regulations, to the Company's statutory public welfare fund, which will be established for the purpose of providing with the Company's employees collective welfare benefits such as the construction of dormitories, canteens and other staff welfare facilities. The fund forms part of the shareholders' equity as only individual employees can use these facilities, while the title of such facilities is held by the Company. The transfer to this fund must be made before any distribution of dividends to shareholders; and

(iv) allocations to the discretionary common reserve if approved by the shareholders. Discretionary common reserve can be used to offset prior years' losses, if any, and capitalised as the Company's share capital.

In accordance with the articles of association of the Company, the net profit after tax of the Company for the purpose of profit distribution will be deemed to be the lesser of (i) the net profit determined in accordance with the PRC accounting principles and financial regulations and (ii) the net profit determined in accordance with Hong Kong accounting standards.

15. EARNINGS PER SHARE

The calculation of basic earnings per share is based on the net profit from ordinary activities attributable to shareholders for the year ended December 31, 2003 of RMB465,906,000 (2002: RMB209,465,000) and the weighted average of 3,995,320,000 (2002: 1,972,321,075) shares in issue during the year.

The weighted average number of shares used to calculate the basic earnings per share for the period from December 25, 2001 (date of establishment) to December 31, 2002 includes 300 million shares (the Company had registered capital of RMB300 million upon establishment on December 25, 2001 and pursuant to the Reorganisation, the entire registered capital was converted to share capital) deemed to have been in issue from the date of establishment of the Company to the Reorganisation date on April 30, 2002 and the issued share capital of 2,600 million shares issued immediately after Reorganisation but prior to the new issue of shares by way of placing and public offering as further described in note 29 to the financial statements. The weighted average number of shares used in the calculation of basic earnings per share for the period from December 25, 2001 (date of establishment) to December 31, 2002 also includes the 1,395,320,000 new shares issued by way of placing and public offering in connection with the public listing of the Company's shares on November 20, 2002.

The calculation of pro forma basic earnings per share is based on the pro forma net profit from ordinary activities attributable to shareholders for the year ended December 31, 2002 of RMB354,386,000 and the pro forma weighted average number of shares in issue of approximately 2,760,557,370 deemed to have been in issue during the year.

Diluted earnings per share for the years ended December 31, 2003 and 2002 have not been calculated because no diluting events existed during these years.

16. PROPERTY, PLANT AND EQUIPMENT

Group

	Tankers and vessels RMB'000	Drilling equipment RMB'000	Machine and equipment RMB'000	Motor vehicles RMB'000	Construction in progress RMB'000	Total RMB'000
Cost:						
At beginning of the year	3,952,496	5,211,122	1,006,135	47,032	556,287	10,773,072
Additions	—	—	148,487	76	965,629	1,114,192
Disposals/write offs	(29,491)	—	(3,999)	(7,557)	—	(41,047)
Transfers from construction in progress	377,460	10,807	284,949	1,049	(674,265)	—
At December 31, 2003	**4,300,465**	**5,221,929**	**1,435,572**	**40,600**	**847,651**	**11,846,217**
Accumulated depreciation:						
At beginning of the year	2,322,792	3,447,853	662,433	23,287	—	6,456,365
Depreciation provided During the year	240,626	208,889	138,672	5,816	—	594,003
Disposals/write offs	(26,289)	—	(3,243)	(1,442)	—	(30,974)
At December 31, 2003	**2,537,129**	**3,656,742**	**797,862**	**27,661**	**—**	**7,019,394**
Net book value:						
At December 31, 2003	**1,763,336**	**1,565,187**	**637,710**	**12,939**	**847,651**	**4,826,823**
At December 31, 2002	1,629,704	1,763,269	343,702	23,745	556,287	4,316,707

As part of the Reorganisation and pursuant to relevant PRC regulations, the property, plant and equipment acquired by the Company upon Reorganisation as at April 30, 2002 was revalued by China Consultant of Accounting and Financial Management Company Limited using the depreciated replacement cost approach and the revaluation increase in cost of RMB2,426 million and accumulated depreciation and impairment of RMB1,223 million was considered as part of the acquisition cost of property, plant and equipment upon Reorganisation and recorded in the Company's balance sheet as at April 30, 2002.

The additional depreciation arising from the revaluation surplus at April 30, 2002 upon Reorganisation is not tax deductible under the latest applicable tax regulations in the PRC, and the deferred tax liability of RMB357.3 million arising from the difference between the tax base and accounting base of the property, plant and equipment under revaluation has been recorded in the balance sheet of the Company as at the Reorganisation date. Thereafter, part of deferred tax liability of RMB45.5 million has been credited to the profit and loss account and the balance of deferred tax on revaluation surplus carried to December 31, 2003 was reduced to RMB311.8 million (2002: RMB333.5 million).

16. PROPERTY, PLANT AND EQUIPMENT continued

As of the date of these financial statements, drilling rigs, tankers and vessels with an aggregate cost amount and net book value of RMB438 million (2002: RMB5,034 million) and RMB124 million (2002: RMB1,761 million), respectively, have yet to be completed the title re-registration procedures after Reorganisation. The Company is in the process of re-registration with relevant government authorities of the title of these rigs, tankers and vessels under its name.

Company

	Tankers and vessels RMB'000	Drilling equipment RMB'000	Machine and equipment RMB'000	Motor vehicles RMB'000	Construction in progress RMB'000	Total RMB'000
Cost:						
At beginning of the year	3,952,496	5,211,122	1,004,199	47,032	556,287	10,771,136
Additions	—	—	148,001	73	965,629	1,113,703
Disposals/write offs	(29,491)	—	(3,999)	(7,557)	—	(41,047)
Transfers from construction in progress	377,460	10,807	284,949	1,049	(674,265)	—
At December 31, 2003	**4,300,465**	**5,221,929**	**1,433,150**	**40,597**	**847,651**	**11,843,792**
Accumulated depreciation:						
At beginning of the year	2,322,792	3,447,853	661,382	23,287	—	6,455,314
Depreciation provided during the year	240,626	208,889	138,566	5,816	—	593,897
Disposals/write offs	(26,289)	—	(3,243)	(1,442)	—	(30,974)
At December 31, 2003	**2,537,129**	**3,656,742**	**796,705**	**27,661**	**—**	**7,018,237**
Net book value:						
At December 31, 2003	**1,763,336**	**1,565,187**	**636,445**	**12,936**	**847,651**	**4,825,555**
At December 31, 2002	1,629,704	1,763,269	342,817	23,745	556,287	4,315,822

17. INVESTMENT IN SUBSIDIARIES

	2003 RMB'000	2002 RMB'000
Unlisted shares, at cost	**2,712**	2,712

Particulars of the principal subsidiaries are as follows:

Name of entity	Place of incorporation/ operation	Nominal value of issued and paid up capital	Percentage of equity directly attributable to the Group Direct	Indirect	Principal activities
Lico International Inc	United States of America	US$100,000	100%	—	Sales of logging equipment
China Oilfield Services (BVI) Limited	British Virgin Island	US$1	100%	—	Investment holding
COSL (Labuan) Company Limited	Malaysia	US$1	—	100%	Provision of drilling services in Indonesia
COSL Services Southeast Asia (BVI) Limited	British Virgin Island	US$1	—	100%	Investment holding

18. INTERESTS IN JOINTLY-CONTROLLED ENTITIES

	Group		Company	
	2003 RMB'000	2002 RMB'000	**2003 RMB'000**	2002 RMB'000
Unlisted investment, at cost	**—**	—	**129,583**	130,323
Share of net assets	**140,597**	131,438	**—**	—
Due from jointly-controlled entities	**13,988**	11,304	**13,988**	11,304
Due to jointly-controlled entities	**(5,678)**	(1,579)	**(5,678)**	(1,579)
	148,907	141,163	**137,893**	140,048

Pursuant to the Reorganisation effective on April 30, 2002, the Company acquired the interest of jointly-controlled entities from CNOOC as described in the note 1 to the financial statements.

Notes to Financial Statements

December 31, 2003

18. INTERESTS IN JOINTLY-CONTROLLED ENTITIES continued

As of the date of these financial statements, all equity interests in jointly-controlled entities has been completed the title re-registration procedures after Reorganisation.

The amounts with jointly-controlled entities are unsecured, interest-free and have no fixed terms of repayment.

Particulars of the jointly-controlled entities at December 31, 2003 are as follows:

			Percentage of			
Name	**Business structure**	**Place of incorporation and operations**	**Ownership interest**	**Voting power**	**Profit sharing**	**Principal activities**
China-France Bohai Geoservices Co., Ltd. ("China-France")	Corporate	Tianjin, PRC	50	50	50	Provision of logging services
China Nanhai-Magcobar Mud Corporation Ltd. ("Magcobar")	Corporate	Shenzhen, PRC	60*	60	60	Provision of drilling fluids services
CNOOC-OTIS Well Completion Services Ltd. ("CNOOC - OTIS")	Corporate	Tianjin, PRC	50	50	50	Provision of well completion services
China Petroleum Logging-Atlas Cooperation Service Company ("Logging - Atlas")	Corporate	Guangdong, PRC	50	50	50	Provision of logging services
China offshore Thales Geo Solutions (Tianjin) Company Ltd. ("China Offshore Thales")	Corporate	Tianjin, PRC	50	50	50	Provision of geophysical services
Tianjin Jinlong Petro-Chemical Company Ltd. ("Jinlong")	Corporate	Tianjin, PRC	50	50	50	Provision of drilling fluids services

* In the opinion of the directors, the Company does not have control over Magcobar's financial and operating decisions, and accordingly, the financial statements of Magcobar have not been incorporated into the Group's consolidated financial statements. The financial statements of Magcobar have been dealt with in the Group's consolidated financial statements under the equity accounting method.

19. INVENTORIES

Inventories consist of materials and supplies.

20. ACCOUNTS RECEIVABLE

An aged analysis of accounts receivable as at the balance sheet date is as follows:

	Group		Company	
	2003	2002	**2003**	2002
	RMB'000	RMB'000	**RMB'000**	RMB'000
Outstanding balances aged:				
Within one year	**533,586**	523,674	**527,714**	524,230
Within one to two years	**58,973**	1,689	**58,973**	1,689
Within two to three years	**1,919**	40	**1,919**	40
	594,478	525,403	**588,606**	525,959
Less: Provision for doubtful debts	**(26,928)**	(530)	**(26,928)**	(530)
	567,550	524,873	**561,678**	525,429

The general credit terms of the Group range from 30 to 90 days.

Included in the accounts receivable are the following amounts due from CNOOC Limited, its subsidiaries and associates (collectively known as "CNOOC Limited Group") and CNOOC, its subsidiaries and associates other than CNOOC Limited Group (collectively known as "CNOOC Group"), which are repayable on similar credit terms to those offered to independent third party customers:

	Group		Company	
	2003	2002	**2003**	2002
	RMB'000	RMB'000	**RMB'000**	RMB'000
Due from CNOOC Group and CNOOC Limited Group	**208,636**	156,818	**208,636**	156,818

Included in the Company's accounts receivable at December 31, 2003 was an amount due from subsidiaries of RMB82,346,000 (2002: RMB46,895,000) which was repayable on similar credit terms to those offered to the major customers of the Group.

21. DUE TO THE ULTIMATE HOLDING COMPANY

The amount due to CNOOC at December 31, 2003 under current liabilities of the Group is unsecured, interest-free, and has no fixed repayment terms.

22. BALANCES WITH OTHER CNOOC GROUP COMPANIES

The balances with other CNOOC group companies at December 31, 2003 are unsecured, interest-free and have no fixed terms of repayment.

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December 31, 2003

23. SHORT TERM INVESTMENTS

	Group		Company	
	2003	2002	**2003**	2002
	RMB'000	RMB'000	**RMB'000**	RMB'000
Government debt securities purchased with an obligation to re-sell, market value	**180,427**	—	**180,427**	—

24. CASH AND CASH EQUIVALENTS AND PLEDGED DEPOSITS

	Group		Company	
	2003	2002	**2003**	2002
	RMB'000	RMB'000	**RMB'000**	RMB'000
Cash and bank balances:				
- Cash and balances with banks	**376,651**	2,558,045	**355,931**	2,553,371
- Deposit with CNOOC Finance Company Limited ("CNOOC Finance Company")	**152,552**	73,321	**152,552**	73,321
	529,203	2,631,366	**508,483**	2,626,692
Time deposits:				
- Banks	**1,572,402**	—	**1,572,402**	—
- CNOOC Finance Company	**100,000**	—	**100,000**	—
- CNOOC Trust and Investment Company Limited ("CNOOC Trust Company")	**—**	24,230	**—**	24,230
	1,672,402	24,230	**1,672,402**	24,230
Cash and balances with banks and financial institutions	**2,201,605**	2,655,596	**2,180,885**	2,650,922
Less: Pledged time deposits for letter of credit facilities	**(3,024)**	(23,440)	**(3,024)**	(23,440)
Cash and cash equivalents	**2,198,581**	2,632,156	**2,177,861**	2,627,482

At the balance sheet date, the cash and bank balances of the Group denominated in Renminbi ("RMB") amounted to RMB1,039,975,000. The RMB is not freely convertible into other currencies, however, under Mainland China's Foreign Exchange Control Regulation and Administration of Settlement, Sale and Payment of Foreign Exchange Regulations, the Group is permitted to exchange RMB for currencies through.

25. TRADE PAYABLES AND OTHER PAYABLES

An aged analysis of trade and other payables as at the balance sheet date is as follows:

	Group		Company	
	2003	2002	**2003**	2002
	RMB'000	RMB'000	**RMB'000**	RMB'000
Outstanding balances aged:				
Within one year	**277,244**	254,662	**269,860**	253,328
Within one to two years	**5,851**	20,034	**5,851**	20,034
Within two to three years	**2,301**	45	**2,301**	45
	285,396	274,741	**278,012**	273,407

26. DEFERRED TAX

The principal components of the provision for deferred tax are as follows:

	Group		
	Consolidated for the year ended December 31, 2003	Pro forma combined for the year ended December 31, 2002	Consolidated for Consolidated for the period from December 25, 2001 (date of establishment) to December 31, 2002
	RMB'000	RMB'000	RMB'000
		(note 1)	(note 1)
Deferred tax movement:			
Balance at beginning of the year	**567,299**	344,000	—
Acquisition pursuant to the Reorganisation	**—**	—	304,000
Deferred tax on revaluation upon Reorganisation	**—**	357,300	357,300
Credit for the year *(note 12)*	**(26,332)**	(134,001)	(94,001)
	540,967	567,299	567,299

26. DEFERRED TAX continued

	Group		Company	
	2003	2002	**2003**	2002
	RMB'000	RMB'000	**RMB'000**	RMB'000
Deferred tax asset:				
Provision for staff bonus	**(25,867)**	(37,781)	**(25,867)**	(37,781)
Deferred tax liabilities:				
Accelerated depreciation	**255,001**	271,600	**255,001**	271,600
Revaluation surplus on Reorganisation	**311,833**	333,480	**311,833**	333,480
Net deferred tax liabilities	**540,967**	567,299	**540,967**	567,299

27. LONG TERM PAYABLE TO THE ULTIMATE HOLDING COMPANY

The long term payable to CNOOC is unsecured, interest-free and repayable over three years on an annual equal instalment basis with repayments commencing from May 1, 2005.

28. DISTRIBUTABLE RESERVES

As at December 31, 2003, in accordance with the PRC Company Law, an amount of approximately RMB1,976 million (2002: RMB1,976 million) standing to the credit of the Company's capital reserve account and an amount of approximately RMB101 million (2002: RMB31 million) standing to the credit of the Company's statutory reserve funds (details of which are set forth in note 30 to the financial statements), as determined under the PRC accounting standards and regulations, were available for distribution by way of future capitalisation issue. In addition, the Company had retained profits of approximately RMB352 million (2002: RMB124 million) available for distribution as dividend. Save as aforesaid, the Company did not have any reserves available for distribution to its shareholders at December 31, 2003.

29. ISSUED SHARE CAPITAL

	2003	2002
	RMB'000	RMB'000
Registered, issued and fully paid:		
2,460,468,000 State legal person shares of RMB1.00 each	**2,460,468**	2,460,468
1,534,852,000 H shares of RMB1.00 each	**1,534,852**	1,534,852
	3,995,320	3,995,320

The Company was established on December 25, 2001 with registered capital of RMB300,000,000, which was contributed in cash by CNOOC.

The Company does not have any share option scheme.

29. ISSUED SHARE CAPITAL continued

During the period from December 25, 2001 (date of incorporation) to December 31, 2002, the following movements in share capital were recorded:

(a) As part of the Reorganisation of CNOOC in preparation for the listing of the Company's shares on the HKSE, the Company obtained an approval document dated September 26, 2002 and was restructured into a joint stock limited liability company. Pursuant to the Reorganisation which was effective on April 30, 2002, the Company acquired the Relevant Businesses and the Relevant Companies (note 1). In consideration of the above acquisition, the Company issued 2,600 million State legal person shares at par value of RMB1.00 each to CNOOC, and the Company's registered and paid-up capital became RMB2,600 million accordingly.

(b) The Company's shares were listed on the HKSE on November 20, 2002 and 1,534,852,000 H shares, consisting of 1,395,320,000 new shares and 139,532,000 State legal person shares, respectively, with a par value of RMB1.00 each were issued to the public by way of placement and offer at HK$1.68 (equivalent to approximately RMB1.78) each.

A summary of the transactions from December 25, 2001 to December 31, 2002 with reference to the above movements of the Company's ordinary share capital is as follows:

	Number of shares in issue		Share Capital			
	State legal person shares	H shares	State legal person shares RMB'000	H shares RMB'000	Total RMB'000	Registered capital RMB'000
December 25, 2001 (date of establishment) and at December 31, 2001	—	—	—	—	—	300,000
Reorganisation (a)	2,600,000,000	—	2,600,000	—	2,600,000	(300,000)
Sales of State legal person shares by CNOOC and conversion into H shares (b)	(139,532,000)	139,532,000	(139,532)	139,532	—	—
Issue of H shares upon listing (b)	—	1,395,320,000	—	1,395,320	1,395,320	—
At December 31, 2002 and December 31, 2003	2,460,468,000	1,534,852,000	2,460,468	1,534,852	3,995,320	—

There was no movement in issued share capital for the year ended December 31, 2003.

30. RESERVES

(a) The amounts of the Group's reserves and the movements herein for the current year are presented in the consolidated statement of changes in equity on page 52 of the financial statements.

(b) Company

	Capital reserve RMB'000	Statutory reserve funds RMB'000	Retained profits RMB'000	Total RMB'000
	(iii)			
Issue of shares upon Reorganisation	999,354	—	—	999,354
Profit for the period from December 25, 2001 (date of establishment) to December 31, 2002 *(note (i))*	—	—	207,558	207,558
Transfer to statutory reserve funds *(note (ii))*	—	31,420	(31,420)	—
Issue of H shares upon listing	1,092,165	—	—	1,092,165
Share issuing expenses	(115,709)	—	—	(115,709)
Proposed final 2002 dividend	—	—	(52,339)	(52,339)
At December 31, 2002 and January 1, 2003	1,975,810	31,420	123,799	2,131,029
Net profit for the year	—	—	438,241	438,241
Interim 2003 dividend	—	—	(49,026)	(49,026)
Proposal final 2003 dividend	—	—	(90,694)	(90,694)
Transfer to statutory reserve funds	—	69,886	(69,886)	—
At December 31, 2003	**1,975,810**	**101,306**	**352,434**	**2,429,550**

Notes:

(i) The Company did not acquire the Relevant Businesses and the Relevant Companies as set out in note 1 to the financial statements until April 30, 2002. As such, there were no results of operations prior to April 30, 2002.

(ii) As detailed in note 14 to the financial statements, the Company is required to transfer a minimum percentage of after-tax profit, if any, to statutory common reserve fund and statutory public welfare fund. The Company transferred 10% and 5% of after-tax profit to the statutory common reserve fund and statutory public welfare fund, respectively, in 2003.

(iii) Capital reserve account can only be used to increase share capital.

31. NOTES TO CONSOLIDATED CASH FLOW STATEMENT

Net assets acquired upon Reorganisation

	Consolidated for the year ended December 31, 2003 RMB'000	Pro forma combined for the year ended December 31, 2002 RMB'000	Consolidated for the period from 25 December 2001 (date of establishment) to December 31, 2002 RMB'000
		(note 1)	(note 1)
Net assets acquired:			
Property, plant and equipment, net	**—**	—	4,132,739
Interests in jointly-controlled entities	**—**	—	148,869
Inventories	**—**	—	159,403
Prepayments, deposits and other receivables	**—**	—	161,893
Accounts receivable	**—**	—	604,541
Due from other CNOOC group companies	**—**	—	9,284
Cash and bank balances	**—**	—	6,880
Due to the ultimate holding company	**—**	—	(22,547)
Trade payables and other payables	**—**	—	(384,662)
Salary and bonus payables	**—**	—	(115,227)
Due to other CNOOC group companies	**—**	—	(10,519)
Bank loans	**—**	—	(130,000)
Deferred tax liabilities	**—**	—	(661,300)
Long term payable to the ultimate holding company	**—**	—	(600,000)
	—	—	3,299,354
Satisfied by:			
Issue of State legal person shares	—	—	2,300,000
Capital Reserve	—	—	999,354
	—	—	3,299,354
Cash and bank balances acquired and net cash inflow in respect of the net assets acquired upon Reorganisation	—	—	6,880

Notes to the Financial Statements

December 31, 2003

32. OPERATING LEASE ARRANGEMENTS

The Group and the Company lease certain of its office properties and operating equipment under operating lease arrangements. Leases for properties and equipment are negotiated for terms ranging from one to seven years.

At December 31, 2003, the Group had following minimum lease payments under non-cancellable operating leases:

	Group		Company	
	2003	2002	**2003**	2002
	RMB'000	RMB'000	**RMB'000**	RMB'000
Within one year	**48,701**	12,773	**48,701**	12,773
In the second to fifth years, inclusive	**239,484**	4,493	**239,484**	4,493
After five years	**245,073**	—	**245,073**	—
	533,258	17,266	**533,258**	17,266

33. CAPITAL COMMITMENTS

The Group and the Company had the following capital commitments, principally for fixed assets construction and purchases:

	Group		Company	
	2003	2002	**2003**	2002
	RMB'000	RMB'000	**RMB'000**	RMB'000
Contracted, but not provided for	**50,889**	679,159	**50,889**	679,159
Authorised, but not contracted for	**3,330,953**	395,402	**3,330,953**	395,402
	3,381,842	1,074,561	**3,381,842**	1,074,561

34. CONTINGENT LIABILITIES

At the balance sheet date, neither the Group, nor the Company had any significant contingent liabilities.

35. RELATED PARTY TRANSACTIONS

The Group is part of a larger group of companies under CNOOC and has extensive transactions and relationships with members of CNOOC. As such, it is possible that the terms of these transactions are not the same as those that would result from transactions among wholly unrelated parties. Related parties refer to corporations in which CNOOC is a shareholder and is able to exercise control and joint control or significant influence. The transactions were made on terms agreed between the parties.

In addition to the transactions and balances detailed elsewhere in these financial statements, the following is a summary of significant transactions carried out between the Group and (i) CNOOC Limited Group; (ii) CNOOC Group; and (iii) its jointly-controlled entities and associate:

	Consolidated for the year ended December 31, 2003 RMB'000	Pro forma combined for the year ended December 31, 2002 RMB'000 (note 1)	Consolidated for the period from December 25, 2001 (date of establishment) to December 31, 2002 RMB'000 (note 1)
A. Included in revenue			
Gross revenue earned from provision of services to the following related parties:			
a. CNOOC Limited Group			
Provision of drilling services	**639,199**	480,744	311,263
Provision of well services	**463,312**	332,658	254,526
Provision of marine support and transportation services	**334,924**	299,736	233,295
Provision of geophysical services	**237,471**	153,136	131,775
	1,674,906	1,266,274	930,859
b. CNOOC Limited Group as operator under production sharing contracts			
Provision of drilling services	**49,556**	62,136	49,498
Provision of well services	**10,376**	194,649	107,476
Provision of marine support and transportation services	**48,630**	57,983	13,244
Provision of geophysical services	**6,325**	16,980	16,980
	114,887	331,748	187,198

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December 31, 2003

35. RELATED PARTY TRANSACTIONS continued

	Consolidated for the year ended December 31, 2003 RMB'000	Pro forma combined for the year ended December 31, 2002 RMB'000	Consolidated for the period from December 25, 2001 (date of establishment) to December 31, 2002 RMB'000
		(note 1)	(note 1)
c. CNOOC Group			
Provision of drilling services	**29,181**	5,828	5,828
Provision of well services	**13,154**	30,991	30,991
Provision of marine support and transportation service	**69,361**	91,711	57,885
Provision of geophysical services	**35,067**	10,092	10,092
	146,763	138,622	104,796
d. Jointly-controlled entities and associate			
Provision of drilling services	**1,309**	2,449	2,449
Provision of well services	**30,254**	22,845	22,845
	31,563	25,294	25,294
B. Included in operating expenses			
Services provided by the CNOOC Group:			
Labour services	**14,901**	50,278	33,459
Materials, utilities and other ancillary	**58,794**	66,670	50,876
Transportation services	**3,095**	9,500	6,315
Lease of office, warehouse, berths	**16,652**	7,796	6,658
Lease of equipment	**—**	1,420	1,061
Repair and maintenance services	**2,361**	27,724	22,871
Management services	**15,789**	4,375	4,262
	111,592	167,763	125,502
C. Included in interest income/expenses:			
Interest income earned from the CNOOC Group	**2,369**	1,861	836
Interest expenses paid to the CNOOC Group	**—**	4,520	2,776

35. RELATED PARTY TRANSACTIONS continued

	Consolidated for the year ended December 31, 2003 RMB'000	Pro forma combined for the year ended December 31, 2002 RMB'000	Consolidated for the period from December 25, 2001 (date of establishment) to December 31, 2002 RMB'000
		(note 1)	(note 1)
D. Transfer of property, plant and equipment and business:			
Purchases of property, plant and equipment from the CNOOC Group	—	2,392	2,392
Sale of property, plant and equipment to CNOOC Group	—	98,553	14,000

		December 31, 2003 RMB'000	2002 RMB'000
E. Deposits and loans:			
Deposits placed with CNOOC Trust Company	—	**24,230**	24,230
Deposits placed with CNOOC Finance Company	**252,552**	**73,321**	73,321

In addition to the above, (i) during the year, accounts receivable amounting to approximately RMB58 million were settled through CNOOC Finance Company at an early settlement discount of approximately RMB200,000 with recourse; and (ii) CNOOC made an advance of RMB238 million to the Company during 2002 which was repaid prior to December 31, 2002. No such advance was noted for the year.

The Company and the above related parties are within the CNOOC Group and are under common control by the same ultimate holding company.

In connection with the Reorganisation, the Company entered into several agreements with the CNOOC Group which govern employee benefits arrangements, the provision of materials, utilities and ancillary services, the provision of technical services, the lease of properties and various other commercial arrangements.

During the year, all pension payments relating to the supplementary pension benefits of approximately RMB28 million (2002: RMB49 million) were borne by CNOOC (note 11).

35. RELATED PARTY TRANSACTIONS continued

Prior to the Reorganisation, the Group occupied certain properties owned by CNOOC at no consideration. The Company signed various property lease agreements in September 2002 with CNOOC Group to lease the aforesaid properties together with other properties for a term of one year. Pursuant to these lease agreements, the Company is required to pay an aggregate annual rental of RMB7.6 million effective from 1 August 2002 to CNOOC Group.

The directors of the Company are of the opinion that the above transactions with related parties were conducted in the usual course of business.

36. APPROVAL OF THE FINANCIAL STATEMENTS

The financial statements were approved and authorised for issue by the board of directors on March 23, 2004.