

NOTES TO FINANCIAL STATEMENTS

31 December, 2004

1. CORPORATE INFORMATION

The registered office of China Oilfield Services Limited (the "Company", together with its subsidiaries, the "Group") 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 China National Offshore Oil Corporation ("CNOOC").

2. IMPACT OF RECENTLY ISSUED HONG KONG FINANCIAL REPORTING STANDARDS ("HKFRSs")

The Hong Kong Institute of Certified Public Accountants has issued a number of new Hong Kong Financial Reporting Standards and Hong Kong Accounting Standards, herein collectively referred to as the new HKFRSs, which are generally effective for accounting periods beginning on or after 1 January 2005. The Group has not early adopted these new HKFRSs in the financial statements for the year ended 31 December 2004. The Group has already commenced an assessment of the impact of these new HKFRSs but is not yet in a position to state whether these new HKFRSs would have a significant impact on its results of operations and financial position.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of preparation

These financial statements have been prepared in accordance with Hong Kong Financial Reporting Standards (which also include Statements of Standard Accounting Practice and Interpretations) issued by the Hong Kong Institute of Certified Public Accountants, 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.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued

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.

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 and 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.

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3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *continued*

Property, plant and equipment; depreciation

Property, plant and equipment 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.

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 losses arising from changes in the fair value of debt securities are credited or charged 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.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued

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.

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 utilised:

- 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

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3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued

Income tax continued

- 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.

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:

- income from day rate contracts is recognised as and when services are performed;
- 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;
- interest income, on a time proportion basis taking into account the principal outstanding and the effective interest rate applicable; and
- 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.

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.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued

Dividends

Final and interim dividends proposed by the directors are classified as a separate allocation of retained earnings within capital and reserves section of 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.

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.

On consolidation, the balance sheet of overseas subsidiaries and joint-controlled entities are translated into Renminbi at the applicable exchange rates ruling at the balance sheet date whereas the profit and loss account of overseas subsidiaries and jointly-controlled entities 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.

4. 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.

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4. SEGMENT INFORMATION continued

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.

The following table presents revenue, profit and certain asset, liability and expenditure information for the Group's business segments for the year ended 31 December, 2004:

	Drilling RMB'000	Well services RMB'000	Marine support and transportation RMB'000	Geophysical RMB'000	Total RMB'000
TURNOVER					
Sales (including intersegment)	1,881,630	891,730	802,966	500,307	4,076,633
Less: Intersegment sales	165,691	37,386	29,516	20,011	252,604
Total sales to external customers	1,715,939	854,344	773,450	480,296	3,824,029
PROFIT FROM OPERATIONS					
Segment results	374,322	127,942	105,246	84,658	692,168
Exchange gains, net					199
Interest income					34,300
Share of profits of jointly-controlled entities					99,196
Profit before tax					825,863
Tax					(124,136)
Net profit					701,727
ASSETS					
Segment assets	2,977,746	1,041,864	2,343,165	396,867	6,759,642
Interests in jointly-controlled entities	-	175,009	-	9,254	184,263
Unallocated assets					2,196,915
Total assets					9,140,820
LIABILITIES					
Segment liabilities	218,414	40,293	105,090	9,916	373,713
Unallocated liabilities					1,702,431
					2,076,144
OTHER INFORMATION					
Capital expenditure	855,892	193,938	450,183	111,835	1,611,848
Depreciation of property, plant and equipment	272,762	111,981	218,723	63,505	666,971
Provision for doubtful debts	35,054	(21)	(20)	(11)	35,002
Provision for inventories	400	398	398	398	1,594

4. 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 31 December, 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 gains, net					(716)
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)

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5. 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:

	2004 RMB'000	2003 RMB'000
Other revenues:		
Gain on disposal of scrap materials	-	106
Insurance claims received	22,352	7,284
Others	1,136	4,330
	23,488	11,720

6. PROFIT FROM OPERATIONS

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

	2004 RMB'000	2003 RMB'000
Auditors' remuneration	2,950	2,900
Employee compensation costs:		
Wages, salaries and bonuses	467,938	369,998
Social security costs	134,361	110,409
Retirement benefits contributions (note 9)	37,854	32,691
	640,153	513,098
Depreciation of property, plant and equipment	666,971	594,003
(Gain)/loss on disposal of property, plant and equipment, net	(236)	2,469
Minimum lease payments under operating leases in respect of land and buildings, berths and equipment	186,828	121,526
Provision for doubtful debts	35,002	26,994
Provision for/(write back of) inventories	1,594	(359)
Repair and maintenance costs	226,733	172,139

6. PROFIT FROM OPERATIONS continued

	2004 RMB'000	2003 RMB'000
Research and development costs included in:	10,029	7,214
Depreciation of property, plant and equipment	12,052	8,273
Employee compensation costs	40,104	10,101
Consumption of supplies, materials, fuel, services and others	31,107	7,506
Other operating expenses	93,292	33,094

7. 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 2004 RMB'000	2003 RMB'000
Fees	429	429
Basic salaries, housing, benefits, other allowances and benefits in kind	345	304
Bonuses	750	762
Pension scheme contributions	27	34
	1,551	1,529

Fees include RMB429,000 (2003: RMB429,000) payable to the independent non-executive directors. There were no other emoluments payable to the independent non-executive directors during the year (2003: Nil).

The remuneration of each of the directors and supervisors fell within the band of nil to RMB1,000,000 for 2004 and 2003.

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.

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8. FIVE HIGHEST PAID EMPLOYEES

The five highest paid employees during the year included one director (2003: one), details of whose remuneration are set out in note 7 above. Details of the remuneration of the remaining four (2003: four) non-director, non-supervisor, highest paid employees for the year are as follows:

	Group 2004 RMB'000	2003 RMB'000
Basic salaries, housing, benefits, other allowances and benefits in kind	565	492
Bonuses	1,392	1,240
Pension scheme contributions	70	58
	2,027	1,790

The remuneration of each of the non-director, non-supervisor, highest paid employees fell within the band of nil to RMB1,000,000 for 2004 and 2003.

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.

9. 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 service 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 31 December, 2004 (2003: Nil).

9. RETIREMENT BENEFITS *continued*

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 31 December, 2004 (2003: Nil).

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

	Group 2004 RMB'000	2003 RMB'000
Contributions to PRC government-regulated pension scheme (note 6)	37,854	32,691

At 31 December, 2004, the Group had no forfeited contributions available to reduce its contributions to the pension scheme in future years (2003: Nil).

10. 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.

In accordance with the relevant tax laws in the PRC, the Company is subject to enterprise income tax at the rate of 33%.

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 fiscal year 2003 was reduced from 33% to 15%. As a result, a tax refund of RMB129 million relating to fiscal year 2003 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.

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10. TAX continued

As a reduction in the enterprise income tax rate from 33% to 15% for the year ended 31 December, 2004 cannot be 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 31 December, 2004.

During the year, the application by the Company for a tax refund relating to the acquisition of domestic equipment has been approved by the tax authority. As a result, a tax refund of RMB23 million has been recorded by the Company.

The Company's incorporated subsidiary in Malaysia, COSL (Labuan) Company Limited, is subject to income tax and branch profit tax at an aggregate rate of 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.

	Group 2004 RMB'000	2003 RMB'000
Hong Kong profits tax:	-	-
Overseas income taxes:		
Current income taxes	271	89
Deferred income taxes	-	-
PRC corporate income tax:		
Current income taxes	363,434	225,766
Tax refund as an advanced technology enterprise	(128,907)	(45,532)
Tax refund from acquisition of domestic equipment	(22,704)	-
Deferred income taxes (note 24)	(107,709)	(26,332)
Share of tax attributable to: jointly-controlled entities	19,751	10,269
Total tax charge for the year	124,136	164,260

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-controlled 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:

10. TAX continued

	2004		2003	
	RMB'000	%	RMB'000	%
Profit before tax	825,863		630,166	
Tax at the statutory tax rate of 33% (2003: 33%)	272,535	33.0	207,955	33.0
Lower tax rates for special provinces or different tax categories	(14,101)	(1.7)	(7,060)	(1.1)
Tax refund as an advanced technology enterprise	(128,907)	(15.6)	(45,532)	(7.2)
Tax refund from acquisition of domestic equipment	(22,704)	(2.7)	-	-
Expenses not deductible for tax	17,313	2.0	8,897	1.4
Total tax charge at the Group's effective rate	124,136	15.0	164,260	26.1

11. NET PROFIT FROM ORDINARY ACTIVITIES ATTRIBUTABLE TO SHAREHOLDERS

The net profit from ordinary activities attributable to shareholders for the year ended 31 December, 2004 dealt with in the financial statements of the Company is RMB647,824,000 (2003: RMB438,241,000).

12. DIVIDENDS

	2004	2003
	RMB'000	RMB'000
Interim dividend-RMB2.29 FEN (2003: 1.23 FEN) per ordinary share	91,493	49,026
Proposed final dividend – RMB4.39 FEN (2003: 2.27 FEN) per ordinary share	175,395	90,694
	266,888	139,720

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.

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12. DIVIDENDS *continued*

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 and financial regulations. 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;

- (iii) allocations of 5% to 10% of after-tax profit, as determined under PRC accounting principles and financial 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 can be 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.

13. 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 31 December, 2004 of RMB701,727,000 (2003: RMB465,906,000) and 3,995,320,000 shares in issue during the year and 2003.

Diluted earnings per share for the years ended 31 December, 2004 and 2003 have not been calculated because no diluting events existed during these years.

14. PROPERTY, PLANT AND EQUIPMENT

Group

	Tankers and vessels RMB'000	Drilling equipment RMB'000	Machine and equipment RMB'000	Motor vehicles RMB'000	Land and building RMB'000	Construction in progress RMB'000	Total RMB'000
Cost:							
At beginning of the year	4,300,465	5,221,929	1,435,572	40,600	-	847,651	11,846,217
Additions	640	350,979	200,159	1,738	200	1,058,132	1,611,848
Disposals/write offs	-	-	(48,685)	(5,339)	-	-	(54,024)
Transfers from construction in progress	772,701	20,118	413,498	-	6,662	(1,212,979)	-
At 31 December, 2004	5,073,806	5,593,026	2,000,544	36,999	6,862	692,804	13,404,041
Accumulated depreciation:							
At beginning of the year	2,537,129	3,656,742	797,862	27,661	-	-	7,019,394
Depreciation provided during the year	250,023	209,261	203,143	4,271	273	-	666,971
Disposals/write offs	-	-	(40,902)	(4,846)	-	-	(45,748)
At 31 December, 2004	2,787,152	3,866,003	960,103	27,086	273	-	7,640,617
Net book value:							
At 31 December, 2004	2,286,654	1,727,023	1,040,441	9,913	6,589	692,804	5,763,424
At 31 December, 2003	1,763,336	1,565,187	637,710	12,939	-	847,651	4,826,823

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 the deferred tax liability of RMB45.5 million has been credited to the profit and loss account and the balance of deferred tax on the revaluation surplus carried to 31 December, 2004 was reduced to RMB283.2 million (2003: RMB311.8 million).

As of the date of these financial statements, drilling rigs, tankers and vessels with an aggregate cost and net book value of RMB438 million (2003: RMB438 million) and RMB105 million (2003: RMB124 million), respectively, have yet to complete the title re-registration procedures after Reorganisation. The Company is in the process of re-registering the title of these rigs, tankers and vessels under its name with the relevant government authorities.

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31 December, 2004

14. PROPERTY, PLANT AND EQUIPMENT *continued*

Company

	Tankers and vessels RMB'000	Drilling equipment RMB'000	Machine and equipment RMB'000	Motor vehicles RMB'000	Land and building RMB'000	Construction in progress RMB'000	Total RMB'000
Cost:							
At beginning of the year	4,300,465	5,221,929	1,433,150	40,597	-	847,651	11,843,792
Additions	640	350,979	199,762	1,741	200	1,058,132	1,611,454
Disposals/write offs	-	-	(48,052)	(5,339)	-	-	(53,391)
Transfers from construction in progress	772,701	20,118	413,498	-	6,662	(1,212,979)	-
At 31 December, 2004	5,073,806	5,593,026	1,998,358	36,999	6,862	692,804	13,401,855
Accumulated depreciation:							
At beginning of the year	2,537,129	3,656,742	796,705	27,661	-	-	7,018,237
Depreciation provided during the year	250,023	209,261	203,081	4,271	273	-	666,909
Disposals/write offs	-	-	(40,879)	(4,846)	-	-	(45,725)
At 31 December, 2004	2,787,152	3,866,003	958,907	27,086	273	-	7,639,421
Net book value:							
At 31 December, 2004	2,286,654	1,727,023	1,039,451	9,913	6,589	692,804	5,762,434
At 31 December, 2003	1,763,336	1,565,187	636,445	12,936	-	847,651	4,825,555

15. INVESTMENT IN SUBSIDIARIES

	2004 RMB'000	2003 RMB'000
Unlisted shares, at cost	2,712	2,712

15. INVESTMENT IN SUBSIDIARIES continued

Particulars of the 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		Principal activities
			Direct	Indirect	
COSL American Inc	United States of America	US\$100,000	100%	-	Sales of logging equipment
China Oilfield Services (BVI) Limited	British Virgin Islands	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 Islands	US\$1	-	100%	Investment holding

16. INTERESTS IN JOINTLY-CONTROLLED ENTITIES

	Group 2004 RMB'000	2003 RMB'000	Company 2004 RMB'000	2003 RMB'000
Unlisted investments, at cost	-	-	128,844	129,583
Share of net assets	184,305	140,597	-	-
Due from jointly-controlled entities	248	13,988	248	13,988
Due to jointly-controlled entities	(290)	(5,678)	(290)	(5,678)
	184,263	148,907	128,802	137,893

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

Particulars of the principal jointly-controlled entities at 31 December, 2004 are as follows:

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31 December, 2004

16. INTERESTS IN JOINTLY-CONTROLLED ENTITIES *continued*

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

17. INVENTORIES

	Group 2004 RMB'000	2003 RMB'000	Company 2004 RMB'000	2003 RMB'000
Gross inventory	221,836	205,148	221,836	204,609
Less: Provisions	(5,983)	(4,389)	(5,983)	(4,389)
	215,853	200,759	215,853	200,220

Inventories consist of materials and supplies.

18. ACCOUNTS RECEIVABLE

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

	Group 2004 RMB'000	2003 RMB'000	Company 2004 RMB'000	2003 RMB'000
Outstanding balances aged:				
Within one year	659,580	533,586	660,405	527,714
Within one to two years	10,294	58,973	10,294	58,973
Within two to three years	54,497	1,919	54,497	1,919
Over three years	641	-	641	-
	725,012	594,478	725,837	588,606
Less: Provision for doubtful debts	(62,464)	(26,928)	(62,464)	(26,928)
	662,548	567,550	663,373	561,678

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 2004 RMB'000	2003 RMB'000	Company 2004 RMB'000	2003 RMB'000
Due from CNOOC Group and CNOOC Limited Group	201,647	208,636	201,647	208,636

Included in the Company's accounts receivable at 31 December, 2004 was an amount due from subsidiaries of RMB151,605,000 (2003: RMB82,346,000) which was repayable on similar credit terms to those offered to the major customers of the Group.

19. DUE TO THE ULTIMATE HOLDING COMPANY

Except for the amount of RMB200 million repayable from May 1, 2005 (note 25), the amount due to CNOOC at 31 December, 2004 under current liabilities of the Group is unsecured, interest-free, and has no fixed repayment terms.

NOTES TO FINANCIAL STATEMENTS

31 December, 2004

20. BALANCES WITH OTHER CNOOC GROUP COMPANIES

The balances with other CNOOC group companies at 31 December, 2004 are unsecured, interest-free and have no fixed terms of repayment.

21. SHORT TERM INVESTMENTS

	Group and Company	
	2004	2003
	RMB'000	RMB'000
Government debt securities purchased with an obligation to re-sell, market value	20,003	180,427

22. CASH AND CASH EQUIVALENTS AND PLEDGED DEPOSITS

	Group		Company	
	2004	2003	2004	2003
	RMB'000	RMB'000	RMB'000	RMB'000
Cash and bank balances:				
- Cash and balances with banks	1,092,702	376,651	1,055,871	355,931
- Deposit with CNOOC Finance Company Limited ("CNOOC Finance Company")	411	152,552	411	152,552
	1,093,113	529,203	1,056,282	508,483
Time deposits:				
- Banks	1,073,424	1,572,402	1,073,424	1,572,402
- CNOOC Finance Company	-	100,000	-	100,000
	1,073,424	1,672,402	1,073,424	1,672,402
Cash and balances with banks and financial institutions	2,166,537	2,201,605	2,129,706	2,180,885
Less: Pledged time deposits for letter of credit facilities	(4,255)	(3,024)	(4,255)	(3,024)
Cash and cash equivalents	2,162,282	2,198,581	2,125,451	2,177,861

At the balance sheet date, the cash and bank balances of the Group denominated in Renminbi ("RMB") amounted to RMB1,292,887,000. The RMB is not freely convertible into other currencies. However, under China's Foreign Exchange Control Regulations and Administration of Settlement, Sale and Payment of Foreign Exchange Regulations, the Group is permitted to exchange RMB for foreign currencies through banks authorised to conduct foreign exchange business.

23. TRADE PAYABLES AND OTHER PAYABLES

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

	Group 2004 RMB'000	2003 RMB'000	Company 2004 RMB'000	2003 RMB'000
Outstanding balances aged:				
Within one year	551,974	277,244	532,694	269,860
Within one to two years	11,748	5,851	11,748	5,851
Within two to three years	5,851	2,301	5,851	2,301
Over three years	2,301	-	2,301	-
	571,874	285,396	552,594	278,012

24. DEFERRED TAX

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

	Group and Company	
	2004 RMB'000	2003 RMB'000
Deferred tax movement:		
Balance at beginning of the year	540,967	567,299
Credit for the year (note 10)	(107,709)	(26,332)
Balance at end of the year	433,258	540,967

	Group and Company	
	2004 RMB'000	2003 RMB'000
Deferred tax asset:		
Provision for staff bonus	(82,520)	(25,867)
Deferred tax liabilities:		
Accelerated depreciation	232,593	255,001
Revaluation surplus on Reorganisation	283,185	311,833
Net deferred tax liabilities	433,258	540,967

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31 December, 2004

25. LONG TERM PAYABLE TO THE ULTIMATE HOLDING COMPANY

	2004 RMB'000	2003 RMB'000
Amount payable:		
Within one year	200,000	-
In the second year	200,000	200,000
In the third year	200,000	400,000
	600,000	600,000
Portion classified as current liabilities (note 19)	(200,000)	-
Long term portion	400,000	600,000

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

26. ISSUED CAPITAL

	2004 RMB'000	2003 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 does not have any share option scheme.

There was no movement in issued share capital for the years ended 31 December, 2003 and 2004.

27. RESERVES

(a) Group

The amounts of the Group's reserves and the movements therein for the current year are presented in the consolidated statement of changes in equity on page 53 of the financial statements.

27. RESERVES continued

(b) Company

	Capital reserve RMB'000	Statutory reserve funds RMB'000	Retained profits RMB'000	Total RMB'000
Balance at 1 January, 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 31 December, 2003	1,975,810	101,306	352,434	2,429,550
Balance at 1 January, 2004	1,975,810	101,306	352,434	2,429,550
Net profit for the year	-	-	647,824	647,824
Interim 2004 dividend	-	-	(91,493)	(91,493)
Proposal final 2004 dividend	-	-	(175,395)	(175,395)
Transfer to statutory reserve funds (note (i))	-	104,259	(104,259)	-
At 31 December, 2004	1,975,810	205,565	629,111	2,810,486

Notes:

- (i) As detailed in note 12 to the financial statements, the Company is required to transfer a minimum percentage of after-tax profit, if any, to the statutory common reserve fund and the statutory public welfare fund. The Company transferred 10% and 5% of after-tax profit to the statutory common reserve fund and the statutory public welfare fund, respectively, in 2004.

As at 31 December, 2004, in accordance with the PRC Company Law, an amount of approximately RMB1,976 million (2003: RMB1,976 million) standing to the credit of the Company's capital reserve account and an amount of approximately RMB206 million (2003: RMB101 million) standing to the credit of the Company's statutory reserve funds, as determined under the PRC accounting principles and financial regulations, were available for distribution by way of future capitalisation issue. In addition, the Company had retained profits of approximately RMB629 million (2003: RMB352 million) available for distribution as dividend. Save as aforesaid, the Company did not have any reserves available for distribution to its shareholders at 31 December, 2004.

28. OPERATING LEASE ARRANGEMENTS

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

NOTES TO FINANCIAL STATEMENTS

31 December, 2004

28. OPERATING LEASE ARRANGEMENTS *continued*

At 31 December, 2004, the Group had following minimum lease payments under non-cancellable operating leases:

	Group and Company	
	2004	2003
	RMB'000	RMB'000
Within one year	65,212	48,701
In the second to fifth years, inclusive	250,281	239,484
After five years	119,926	245,073
	435,419	533,258

29. CAPITAL COMMITMENTS

At 31 December, 2004, the Group and Company had the following Capital commitments, principally for construction and purchases of fixed assets:

	Group and Company	
	2004	2003
	RMB'000	RMB'000
Contracted, but not provided for	531,172	50,889
Authorised, but not contracted for	1,893,374	3,330,953
	2,424,546	3,381,842

30. CONTINGENT LIABILITIES

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

31. 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, 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

31. RELATED PARTY TRANSACTIONS continued

	2004 RMB'000	2003 RMB'000
A. Included in revenue		
Gross revenue earned from provision of services to the following related parties:		
a. CNOOC Limited Group		
Provision of drilling services	832,246	639,199
Provision of well services	545,108	463,312
Provision of marine support and transportation services	405,560	334,924
Provision of geophysical services	349,354	237,471
	2,132,268	1,674,906
b. CNOOC Limited Group as operator under production sharing contracts		
Provision of drilling services	223,661	49,556
Provision of well services	58,876	10,376
Provision of marine support and transportation services	56,110	48,630
Provision of geophysical services	940	6,325
	339,587	114,887
c. CNOOC Group		
Provision of drilling services	67,967	29,181
Provision of well services	38,108	13,154
Provision of marine support and transportation service	102,371	69,361
Provision of geophysical services	3,461	35,067
	211,907	146,763
d. Jointly-controlled entities		
Provision of drilling services	3,207	1,309
Provision of well services	26,528	30,254
	29,735	31,563

NOTES TO FINANCIAL STATEMENTS

31 December, 2004

31. RELATED PARTY TRANSACTIONS *continued*

	2004 RMB'000	2003 RMB'000
B. Included in operating expenses		
Services provided by the CNOOC Group:		
Labour services	13,736	14,901
Materials, utilities and other ancillary	105,517	58,794
Transportation services	3,798	3,095
Lease of office, warehouse, berths	25,312	16,652
Lease of equipment	19,532	-
Repair and maintenance services	26,096	2,361
Management services	28,273	15,789
	222,264	111,592
C. Included in interest income:		
Interest income earned from the CNOOC Group	4,495	2,369
D. Deposits:		
Deposits placed with CNOOC Finance Company	411	252,552

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 (2003: RMB28 million) were borne by CNOOC (note 9).

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.

32. APPROVAL OF THE FINANCIAL STATEMENTS

The financial statements were approved and authorised for issue by the board of directors on 30 March, 2005.