

CORPORATE GOVERNANCE REPORT

The Company's corporate governance for the accounting period covered by this annual report has been in compliance with the relevant local and international laws and regulations, realizing fairness and transparency in practice and meeting the basic requirements of corporate governance and has been accepted by the capital market. The Company was chosen by Euro Money magazine as one of the 10 Most Accessible Management in Asia for the year 2003 and by Finance Asia magazine as one of the 10 Best Managed Companies for the year 2003.

During 2005, the Board of Directors reviewed the systems of the Company based on the Code on Corporate Governance Practices set out in Appendix 14 of the Rules of the Stock Exchange of Hong Kong Limited (hereinafter referred to as "the Code") and took a step forward in perfecting the structure of governance so as to ensure high standards in corporate governance. Details of actions are as follows:

I. Overview of Corporate Governance

Regarding the Code as the criterion for deciding on the standard of corporate governance, the Board of Directors consider the code an important reference standard for measurement of corporate governance, they have stepped up their efforts in organizing training for directors to familiarize them with the Code. The Secretary to the Board was assigned to make a comparison between the Code and the existing practice of the Company. To perfect the relevant practices, the Board of Directors adopted higher standards for governance and have formulated and implemented various practices so as to comply with provisions of the Code. The Company considered the Code of Best Practice together with its actual situation and incorporated some of the practices into the system of the Company and some others used in operation. For instance, it is stated in clause A.3.2 of the Code that the number of independent non-executive directors should represent at least one third of the members of the Board of Directors, this has been consistently abided by the Company since its listing in 2002. At present, the number of independent non-executive directors exceeds one third of the Board of the Company. Apart from that, the Company observed clause A.4.4 of the Code and established a Nomination Committee in 2005

with the majority of members being independent non-executive directors. The Company also adopted the recommended best practices of the Code in respect of directors' liability insurance and for better communication between independent non-executive directors and the Chairman.

Regarding compliance with clause E1.2 of the Code during the period under review, the Board considered it necessary to explain the following to shareholders. The Company held its 2004 annual general meeting on 25 May 2005. In accordance with the requirement of the Company's Articles of Association, it was resolved that our redundant, chairman of the nomination committee, chief executive director, and president Yuan Guangyu preside over the annual general meeting as the Chairman of the Board of Directors was not able to chair the meeting. For future annual general meetings, the Company will consider the actual situation of annual general meetings (for instance, when holders of H shares attend the meeting in person) and will require the Chairman of the Board to preside over and the chairman of each of the special committees to attend annual general meetings.

Saved as disclosed above, the Board of Directors of the Company is not aware of any information that may reasonably indicate the Company's deviation from the Code during the period under review. The Board of Directors believes that the Company has fully complied with all the requirements of the Code.

In conclusion, the Board is of the opinion that the Company has adhered to the principles of treating all shareholders equally, protecting their interests and has fulfilled the requirements in respect of disclosure regarding the Company's business results, thus successfully combining the concept of corporate governance with actual practice.

II. Directors' Involvement in Securities Transactions

Following specific enquiries of all directors, the Board confirmed that during the 12 months ended 31 December 2005, the provisions of the Model Code for Securities Transaction by Directors of Listed Issuers ("the Model Code") set out in Appendix 10 of the Listing Rules were observed. At present, the Company

has not adopted any code of conduct for securities transactions by directors that exceeds the provisions set out in the Model Code. The Company has adopted all the provisions of the Model Code.

III. The Board of Directors

(I) Composition of the Board of Directors

Directors during the year and/or on the date of this report are as follows:

Chairman of the Board and non-executive director: Fu Chengyu
Executive directors: Yuan Guangyu, Wu Mengfei
Non-executive director: Wang Zhongan (Resigned on 19 September 2005)
Independent non-executive directors: Andrew Y. Yan, Gordon C.K. Kwong, Simon X. Jiang

The Board of Directors convened four meetings during the year. Except for Wang Zhongan who did not personally attend the second annual meeting of the Board of Directors on 30 March 2005 but did designate in writing another director to act on his behalf, all other directors attended all meetings of the Board during the year.

(II) The Roles of the Board of Directors and the Management

The Articles of Association of the Company clearly define the duties and functions of the Board of Directors and the Management. The responsibilities of the Board of Directors are as follows:

1. Convene shareholders' general meetings and report the Board's work at such meetings;
2. Implement the resolutions of shareholders' general meetings;
3. Decide on the Company's business plans and investment plans;
4. Formulate the Company's annual budgets and accounts;
5. Formulate the Company's plans for profit distribution and plans for recovery of losses;
6. Formulate plans for increase or decrease in the Company's registered capital and the issue of corporate debentures;
7. Formulate plans for merger, division or dissolution of the Company;
8. Decide on the establishment of the Company's internal management structure;
9. Appoint or dismiss the President of the Company, and at the recommendation of the President, appoint or dismiss the Vice President and other members of senior management (including the financial controller), and fix their remuneration; appoint or replace the members of the Board of Directors and Board of Supervisors of wholly owned subsidiaries, and appoint, replace or recommend representatives of shareholders, directors and supervisors of controlled subsidiaries and subsidiaries with equity holding;

10. Formulate the Company's basic management system;
11. Formulate proposals for amendments to the Company's Articles of Association;
12. Exercise the Company's power of financing and borrowing and decide on the matters of leasing and contracting in accordance with the provisions of relevant laws, regulations, these Articles of Association as well as the authorization of shareholders' general meetings;
13. Propose to shareholders' general meetings the appointment or replacement of accounting firms as auditors for the Company;
14. Other duties and powers under the Articles of Association or conferred by shareholders' general meetings.

The duties and functions of the Company's management is mainly defined in the Articles of Association and other corporate documents of the Company and are principally concerned with the responsibilities and powers of the Chief Executive Officer and the President, which are mainly set by resolutions passed at the meetings of executive directors and their powers in respect of the day-to-day management of the company's production and operations. In particular, the Board of Directors' decision-making process and its implementation of such decisions can be gleaned from the powers and duties as granted to and carried out by the Chief Executive Officer, which include responsibility for coming up with and implementing the Company's strategies.

In short, the division of functions between the Board of Directors and the management of the Company is clearly defined. In respect of delegation of powers by the Board of Directors to management, the Board is careful to prepare specific documentation stating the extent of the powers delegated and is careful to give specific guidance when such delegated powers are exercised. For instance, when the Board authorizes certain decision-making power regarding investment in view of production and operation needs, the extent and procedures for exercising such powers by the management is provided by specific documents approved by the Board. The content of annual reports and interim reports of operating results and proposals at shareholders' general meetings as disclosed or included in statements made by the Company are decided by the Board of Directors. Other announcements can be made by the management with authorization from the Board for disclosure. In addition, the directors have discharged their duties in good faith and with diligence and played an important role in decision-making in relation to the operations of and risk control by the Company.

(III) Other matters

During the period under review, the number and qualifications of independent non-executive directors of the Company were in compliance with the Listing Rules 3.10(1) and (2), and the independence of current independent non-executive directors

of the Company is in compliance with the requirement set out in the Listing Rules 3.13.

IV. Chairman and Chief Executive Officer

The functions of the Chairman and the Chief Executive Officer of the Company are clearly defined and such positions are at present separately held by two persons, i.e., Fu Chengyu as Chairman and Yuan Guangyu as the Chief Executive Officer.

V. Terms of office of non-executive directors are as follows:

The term of office of Fu Chengyu and Andrew Y. Yan is from 20 September 2005 to 19 September 2008. The term of office of Gordon C.K. Kwong is from 30 October 2005 to 29 October 2008. The term of office of Simon X. Jiang is from 27 May 2004 to 26 May 2007. The term of office of Wang Zhongan, non-executive director, was three years starting from 20 September 2002 and his term of office ended on 19 September 2005. His successor will be nominated by the Board of Directors and elected at a general meeting of the shareholders.

VI. Directors' Remuneration

(I) The composition and functions of the Remuneration and Review Committee

The Remuneration and Review Committee of the Company consists of five members, namely Andrew Y. Yan, Gordon C.K. Kwong, Simon X. Jiang, Yuan Guangyu and Wu Mengfei, of which three are independent non-executive directors and Andrew Y. Yan, independent non-executive director, acts as Chairman.

The functions of this committee are to formulate the standard for assessing the performance of directors, supervisors and members of senior management and to conduct such assessment, formulate and review the remuneration policy and scheme for directors, supervisors and the senior management.

(II) The work of the Remuneration and Review Committee during the year

The committee held two meetings on 24 August 2005 and 8 December 2005, respectively, during the period under review and all of these meetings were attended by the three members Andrew Y. Yan, Gordon C.K. Kwong and Simon X. Jiang (the two members Yuan Guangyu and Wu Mengfei were appointed by way of by-election on 9 December 2005, thus, there was no record of their attendance at such meetings). The work and achievements of the committee during the year are summarized as follows:

1. Researched and formulated the policy and framework of incentive and discipline measures for the Company's management and determined the structure and levels of reference regarding the management's remuneration.

2. Researched and formulated the long-term incentive scheme for the Company's senior management.

Directors fee are subject to shareholders approval at general meetings. Other emoluments are determined by the Company's board of directors with reference to directors duties, responsibilities, the remuneration committee are the performance and results of the Group. The Group had not implemented any long term incentive scheme during 2005.

VII. The Nomination of Directors

(I) The composition and functions of the Nomination Committee

The Nomination Committee of the Company consists of three members, namely Yuan Guangyu, Andrew Y. Yan, and Simon X. Jiang, of which two are independent non-executive directors and Yuan Guangyu acts as Chairman.

Major functions of the committee are to select and recommend candidates for directors of the Company and to recommend the standards and procedures for selecting such candidates.

(II) The work of the Nomination Committee during the year; procedures and standards for nomination

The Nomination Committee held one meeting during the period under review which was attended by all members. The committee also passed two resolutions through voting by way of facsimile.

The Nomination Committee passed the resolution of arranging for the re-appointment of directors, and nominated two vice presidents to the Board of Directors for their appointment and proposed a recommendation to the Board in respect of the structure of the Board of Directors during the period under review. The committee nominated directors and senior management members according to the following procedure:

1. Communicated with the management of the Company and researched on the need of the Company for new directors and senior management members;
2. Sought extensively for candidates for directors and senior management from within the Company and from controlled (and equity holding) enterprises as well as in the market;
3. Collected information about the occupations, education background, job titles, detailed working experience, information relating to part time jobs, etc of preliminary candidates;
4. Sought the consent of nominees for nomination without which they could not become candidates for directors or members of senior management;
5. Convened meeting of the Nomination Committee, examined the qualifications of preliminary candidates for directors and Secretary to the Board with reference to the requirements

regarding such positions as well as the qualifications required for positions of other senior management personnel nominated by the President;

6. Before electing new directors and appointing new senior management personnel, the Nomination Committee should recommend candidates for directors and new senior management personnel to be appointed and forward relevant materials to the Board.
7. Followed up on decisions of the Board and feedback opinions.

The standards for selecting and recommending directors and senior management personnel by the committee is determined by the requirements of the Company as well as all factors relating to the candidates including their work experience, abilities and conduct.

VIII. The Remuneration of Auditor

The Company re-appointed Ernst & Young as auditor of the Company and the fees for the audit and non-audit work provided to the Company during the period of report were as follows:

- The audit fees of audit/review of annual and interim accounting reports totalled RMB3,350,000.
- The non-audit fees of advising the Company on its acquisition project and providing tax consultation for overseas business totalled RMB576,000.

IX. The Audit Committee

(I) The composition and functions of the Audit Committee

The Audit Committee consists of three members, namely, Andrew Y. Yan, Gordon C.K. Kwong and Simon X. Jiang, all of whom are independent non-executive directors and of whom Gordon C.K. Kwong acts as the Chairman.

The functions of this committee are to review the accounting policy, financial condition and financial reporting procedures of the Company; to review the internal control structure; to recommend and engage external audit body; and to be mainly responsible for the communication, supervision and review of the internal and external audit of the Company.

(II) The work of the Audit Committee for the year

The Audit Committee held three meetings during the period under review and all members attended the meetings. The major work of the Audit Committee for the year was:

1. It examined the financial reports of the annual operating results of 2004, the interim operating results and annual results of 2005 of the Company. The members performed sufficient and necessary communication with the auditor and the management of the Company in the process of examination and fulfilled its duties in ensuring the Company's compliance with the regulations, and the completeness

and accuracy of the operating results disclosed by the Company.

2. Reviewed the financial reporting system and internal control system of the Company. During the reporting period, the committee received the report of the management in relation to the scheme for improving the management of finance and IT system and studied the relevant recommendations in the "Report to the Audit Committee" from the auditor to the Company and issued relevant opinions to the Board of Directors and management. During the reporting period, the bulk of the review of the internal control procedure of the Company performed by the committee was to discuss and study the efficiency of internal controls and risk management with management and help management improve the system and structure. For example, the committee received a special report of the management in relation to the financial control system and the management of the purchase system of the Company, discussed with management these matters and put forward proposals, and put forward proposals for improvement of the information management system of the Company and for establishing an ERP system as early as possible.
3. Proposed to the Company the re-appointment of the auditor. The committee considered that Ernst & Young proved appropriate to act as the external auditor of the Company and the Board of Directors approved the proposal for re-appointment of the auditor.

X. Responsibilities Undertaken

The Board of Directors acknowledges its responsibilities of preparing the accounts of the Company and the auditor will also make a statement about its responsibilities of reporting in the "Report of Auditors" on page 51; the Board of Directors undertakes the responsibility for the effective internal control of the Company and its subsidiaries and has completed the relevant review and assessment during the reporting period, and concluded that there in no major deficiencies in the internal controls of the Company and its subsidiaries; the Board of Directors undertakes herewith that save as disclosed by the Company in the annual report for this period, there are no major events and circumstances of uncertainty which may affect the operation of the Company as a going concern.

Board of Directors Meetings and Professional Committee Meetings Held In 2005

Meeting	Time	Place	Attendant	Moderator	Notes
First Meeting of Board of Directors	7 January 2005	Dongguan	Fu Chengyu Yuan Guangyu Wu Mengfei Wang Zhongan Andrew Y. Yan Gordon C. K. Kwong Simon X. Jiang	Fu Chengyu	Four supervisors attended as a non voting delegate
Second Meeting of Board of Directors	30 March 2005	Shenzhen	Fu Chengyu Yuan Guangyu Wu Mengfei Andrew Y. Yan Gordon C. K. Kwong Simon X. Jiang	Fu Chengyu	Four supervisors attended as a non voting delegate
Third Meeting of Board of Directors	29 August 2005	Beijing	Fu Chengyu Yuan Guangyu Wu Mengfei Wang Zhongan Andrew Y. Yan Gordon C. K. Kwong Simon X. Jiang	Fu Chengyu	Four supervisors attended as a non voting delegate
Fourth Meeting of Board Directors	9 December 2005	Shenzhen	Fu Chengyu Yuan Guangyu Wu Mengfei Andrew Y. Yan Gordon C. K. Kwong Simon X. Jiang	Fu Chengyu	Four supervisors attended as a non voting delegate
First Meeting of Audit Committee	17 March 2005	Beijing	Andrew Y. Yan Gordon C. K. Kwong Simon X. Jiang	Gordon C. K. Kwong	
Second Meeting of Audit Committee	24 August 2005	Beijing	Andrew Y. Yan Gordon C. K. Kwong Simon X. Jiang	Gordon C. K. Kwong	
Third Meeting of Audit Committee	8 December 2005	Shenzhen	Andrew Y. Yan Gordon C. K. Kwong Simon X. Jiang	Gordon C. K. Kwong	
First Meeting of Remuneration Committee	24 August 2005	Beijing	Andrew Y. Yan Gordon C. K. Kwong Simon X. Jiang	Andrew Y. Yan	
Second Meeting of Remuneration Committee	8 December 2005	Shenzhen	Andrew Y. Yan Gordon C. K. Kwong Simon X. Jiang	Andrew Y. Yan	
Meeting of Nomination Committee	8 December 2005	Shenzhen	Yuan Guangyu Andrew Y. Yan Simon X. Jiang	Yuan Guangyu	

The Board of Directors
China Oilfield Services Limited
22 March 2006