

SHAREHOLDING

We were established as a joint stock limited company on 25 April 2006 and CNOOC, a State-owned enterprise, is our main Promoter. Prior to the Restructuring, our predecessor, CNOOC Chemical, was a wholly owned subsidiary of CNOOC. Following the Restructuring, CNOOC owned 96.67% of our issued share capital. Immediately after the completion of the Global Offering, CNOOC will own 62.73% of our issued share capital if the Over-allotment Option is not exercised (or 59.41% if the Over-allotment Option is exercised in full) and it will be our Controlling Shareholder.

NON-COMPETITION AGREEMENT

We entered into a non-competition agreement with CNOOC on 7 September 2006, pursuant to which CNOOC:

- (1) confirmed that as of the date of the agreement it and its subsidiaries (other than through us) were not engaged in any business or activity in respect of mineral fertilizers, methanol or other related chemical products business that we are engaged in; and
- (2) has undertaken that during the term of the non-competition agreement it will not, and it will procure its subsidiaries not to (a) directly or indirectly engage in, acquire, develop, operate or participate in businesses that compete or may compete with our core business at the relevant time, (b) develop or engage in new businesses or projects that compete or may compete directly or indirectly with our core business at the relevant time if we have definite plans to develop new businesses or projects in relation to our core business and CNOOC is or ought to be aware of such plans, or (c) under the circumstances of competition with our core business at the relevant time, intentionally solicit or entice away from us the custom of any person who has a business relationship with us or is in business negotiations with us, so that such person might terminate or reduce the business transactions with us.

For the purpose of the non-competition agreement, “our core business” refers to (1) the business with respect to nitrogenous fertilizers, methanol and other related chemical products conducted or engaged in by us as of the date of the agreement (except the compound fertilizers business we were engaged in as of the date of the agreement) and (2) the business with respect to mineral fertilizers, methanol and other related chemical products not yet conducted or engaged in by us as of the date of the agreement but will have been conducted or engaged in by us thereafter. Our core business at any time refers to the scope of businesses within (1) and (2) that we have engaged in at that relevant time.

If CNOOC or any of its subsidiaries becomes aware of an investment opportunity which competes or may compete directly or indirectly with our core business, CNOOC shall disclose to us of the major terms of such investment opportunity and offer us the first transaction right to take up such opportunity on such terms.

The undertakings referred to in paragraph (2) above do not apply in the following circumstances:

- (a) we have been offered the aforesaid first transaction right but we decide not to take up such opportunity, then CNOOC or its relevant subsidiary may take up such investment opportunity (the “Competing Business”);

- (b) CNOOC and its subsidiaries may hold or own any shares, securities or equity interest in a company that competes or may compete with our core business, provided that (i) such shares, securities or equity interest held by CNOOC or its subsidiaries represent not more than 5% of the relevant class of issued shares or securities or of the total equity interests of the investee company, (ii) there is a person who holds a higher percentage of the relevant class of issued shares or securities or of the total equity interests at any time and (iii) CNOOC and its subsidiaries hold or own such shares, securities or equity interests for the purpose of financial investment; and
- (c) CNOOC or its subsidiaries own equity interest in an entity that competes or may compete with our core business because of debt restructuring of that entity, provided that such equity interest shall not represent more than 5% of the equity interest in that competing entity. If such equity interest will represent more than 5% of equity interest in that competing entity, then CNOOC or its relevant subsidiary shall as soon as possible provide us the first transaction right as described above.

We have been granted by CNOOC the following option and right in relation to the Competing Business during the term of the non-competition agreement:

- Provided that the legitimate interest of third parties arising under applicable laws and regulations is not affected, we have the first option, subject to the relevant laws and regulations, to (a) purchase in one or more transactions any equity interest, assets or other benefits in the Competing Business or (b) operate on an entrustment basis, lease or operate on a sub-contracting basis the Competing Business or the related assets, in both cases at a price agreed in accordance with the form and procedures required by the applicable laws and regulations, by reference to a valuation conducted by an independent qualified valuer jointly appointed by CNOOC or its relevant subsidiary and us.
- Where CNOOC or its relevant subsidiary intends to sell, transfer, lease, license or otherwise dispose of any Competing Business to any third party, it will notify us in writing of the terms of such intended transaction, give us the pre-emptive right to purchase, acquire or otherwise take up the Competing Business on such terms and provide us with such information as we may reasonably require for us to make an informed investment decision. We may decide to take up the Competing Business or make a counter-offer by suggesting the terms on which we are willing to take up the Competing Business. If we decide not to take up the Competing Business or if CNOOC or its relevant subsidiary does not accept our counter-offer, then such Competing Business may be sold, transferred, leased, licensed or otherwise disposed of to a third party on terms not more favorable to the counterpart than the terms set out in the notice.

CNOOC undertakes to provide all information necessary for the enforcement of the non-competition agreement. Our independent non-executive Directors will review CNOOC's compliance with its undertakings given in the non-competition agreement at least on an annual basis.

After the Listing Date, CNOOC will conduct annual meetings with us with a view to (i) identifying any investment opportunity made available to CNOOC or its subsidiaries that competes or may compete with our core business and (ii) discussing the performance of the Competing Business (if any). Members of our Board or senior management will represent us at those meetings at which they may make enquiries in respect of the Competing Business to enable them to consider whether

exercising our first transaction right, first option or pre-emptive right pursuant to the non-competition agreement is in our interest.

For any decision relating to the exercise of our first transaction right, first option or pre-emptive right, (a) if all independent non-executive Directors are of the view that we should not exercise such right or option, the decision will be made in accordance with such common view; (b) if all or the majority of our independent non-executive Directors are of a view that we should exercise such right or exercise such option, the decision will be made in accordance with such view; and (c) in respect of other circumstances, we will convene a Board meeting and may, according to the resolution of the Board, convene a shareholders' general meeting to pass a resolution on the exercise of such rights according to our Articles.

We will comply with all relevant provisions of the Hong Kong Listing Rules when we exercise our first transaction right, first option or pre-emptive right granted under the non-competition agreement and disclose decisions on matters reviewed by our independent non-executive Directors relating to the enforcement of the non-competition agreement (if any) either through our annual reports or by way of public announcements. Further, we will disclose in our annual reports CNOOC's annual declaration that it has complied with its undertakings given in the non-competition agreement and in our annual corporate governance reports how such undertakings are enforced and how our rights under the agreement are exercised.

The non-competition agreement is conditional on (i) the granting by the CSRC and the Listing Committee of the Hong Kong Stock Exchange of listing of, and permission to deal in, our H Shares; and (ii) all conditions in the Underwriting Agreements having been satisfied or the obligations of the Underwriters having become unconditional. The agreement will remain effective until the earlier of the date on which the CNOOC is no longer our Controlling Shareholder and the date on which our Shares cease to be listed on the Hong Kong Stock Exchange or any other recognized international stock exchange except temporary suspensions for any reasons.

INDEPENDENCE FROM CNOOC

Having considered all relevant factors, we are satisfied that we can conduct our business independently of the CNOOC Group after the Global Offering:

Independence of our Board, our Supervisory Committee and our senior management

In our Board, only Mr. WU Mengfei will continue to hold positions with the CNOOC Group including a position with CNOOC as the chief financial officer and a position with COSL as a non-executive director. He is our Chairman and non-executive Director and will only be involved in high-level decisions in respect of important strategic and policy matters. Our day-to-day management decisions are made by our executive Directors and members of our senior management who do not hold any positions with any member of the CNOOC Group. Further, Mr. WU understands that his fiduciary duties are owed to us and our shareholders as a whole but not to any particular shareholder. Mr. WU will comply with our Articles and applicable laws and regulations in respect of any matters that involve any conflict of interests.

Mr. YIN Jihong, who is the chairman of our supervisory committee and is elected as shareholders' representative in the committee, is also the chairman of the supervisory committees of several members of the CNOOC Group including CNOOC itself. Nevertheless, he understands that his

duties as our Supervisor are owed to us and our shareholders as a whole but not to any particular shareholder.

Apart from Mr. WU and Mr. YIN, none of our Directors, Supervisors or members of senior management currently hold positions with any member of CNOOC Group. Therefore, we are of the view that the management of our Company will be conducted independently of the CNOOC Group.

Our assets and licenses

As our main Promoter, CNOOC used its entire interest in the net assets of CNOOC Chemical to establish our Company. It has not retained any business that competes or may compete with our core business as confirmed in the sub-section headed “Non-Competition Agreement” above. We have full control over our assets to continue our business independently of CNOOC Group.

We are engaged mainly in the production and sales of nitrogenous fertilizers and other chemical products and the provision of related services. We have full rights to make decisions on and to carry out our own business operations independently. We have sufficient capital, equipment and employees to operate our business independently.

Operational independence

Our operational decisions are made by our Directors and our senior management. We have established our own set of organization structure made up of individual departments, each with specific areas of responsibility. We have also established a set of internal controls to facilitate the effective operation of our business. We have been operating independently from the CNOOC Group during the Track Record Period and thereafter as we have not shared our production team, production facilities and equipment, or marketing, sales and general administration resources with CNOOC or its Associates apart from certain services and supplies we and the CNOOC Group have been providing to each other which, following the listing of our H Shares on the Hong Kong Stock Exchange, will be covered by the Comprehensive Services and Product Sales Agreement and the Waste Water Treatment Services Agreement described in the section headed “Connected Transactions”, which are not substantial to our operation and will not constitute our operational reliance on the CNOOC Group.

As disclosed in the sections headed “Risk Factors—Risks relating to our business operations—Our operating results may be significantly affected by changes in the supply of natural gas as a critical raw material”, and “Business—Raw materials and energy—Natural gas”, natural gas, as the key raw material for Fudao Phase I, Fudao Phase II and CNOOC Jiantao Methanol Plant, is sourced from gasfields operated by CNOOC Limited. There are no alternative proximate suppliers of natural gas that are able to supply the amount of natural gas required by our Hainan production facilities. We therefore purchase natural gas from those gasfields in order to better control our costs. We are of the view that our purchases of natural gas from CNOOC Limited’s gasfields are a result of geographical and industrial features. We entered into 20-year natural gas sale and purchase agreements to secure stable and reliable sources of natural gas supply for our benefit. Our contractual rights under such pre-existing agreements allow us to operate our production complexes independently. Nevertheless, Tianye Plant sources natural gas from an independent gasfield, namely, an onshore gasfield owned by PetroChina. See “Our Business—Raw materials and energy—Natural gas—For Tianye Plant”.

Continuing transactions with the CNOOC Group

From the Listing Date onwards, we will continue to conduct certain transactions with members of the CNOOC Group. These transactions are governed by agreements entered into in the ordinary and usual course of our business and on normal or better than normal commercial terms which are fair and reasonable and in the interests of our shareholders. More details of those transactions are set out in the section headed “Connected transactions”.

Finance Matters

We have our own financial auditing system independent from the CNOOC Group and have employed a sufficient number of dedicated financial accounting personnel responsible for financial auditing of our Company’s accounts. We have independent bank accounts and made independent tax registration.

All of our treasury operations are dealt with by our treasury department which is currently staffed by seven persons. The functions of such department include financing, treasury and cash management, as well as currency risk control. The department operates independently from the CNOOC Group (including CNOOC Finance) and there is no sharing of functions or resources between it and any member of the CNOOC Group. Our interaction with CNOOC Finance is conducted in a similar manner as is our interaction with third party banks or financial institutions.

Our choice of financial institutions is mainly based on the credit rating of the institutions and the terms offered by them. We have been using financial services provided by CNOOC Finance before the Listing Date and will continue to do so thereafter, as described in the section headed “Connected Transactions—Financial Services Agreement”, because we believe that (a) CNOOC Finance has credit ratings, asset size, banking credits and corporate governance practices comparable to major commercial banks in China and (b) the terms CNOOC Finance offers to us are the same or even more favorable to us compared with the terms offered by independent commercial banks or financial institutions.

Nevertheless, our Directors believe that we are able to secure loans and credit facilities and utilize other financial services from independent banks or financial institutions at reasonable rates given our financial strength. As of 30 June 2006, our credit facilities secured from major PRC banks amounted to RMB2.6 billion. Further, we have been using services from independent banks and we have not experienced any difficulties in our interaction with such financial institutions.

Notwithstanding our continuing utilization of CNOOC Finance’s financial services, such transactions are carried out in our ordinary and usual course of business and on an arm’s length basis. The provision of services by CNOOC Finance to us is subject to the supervision of the China Banking Regulatory Commission and the regulations of the PBOC. Additionally, on the Listing Date we will adopt internal control procedures and corporate governance measures in relation to our utilization of CNOOC Finance’s services, in addition to the control measures in connection with connected transactions, in order to protect the interests of our shareholders. See “Connected Transactions—Financial Services Agreement—Internal control procedures and corporate governance measures”.

Furthermore, we have settled all amounts (apart from trade balances) due from us to the CNOOC Group (except CNOOC Finance) and procured the release of all guarantees given for our benefit by the CNOOC Group or given by us in favor of the CNOOC Group prior to the Listing Date.

RELATIONSHIP WITH CNOOC

Based on the above, our Directors believe that we are able to maintain a reasonable level of financial independence from the CNOOC Group.