

Prior to the Restructuring, we and certain members of the CNOOC Group undertook various types of intra-group transactions. We also engaged in business relationships with our other connected persons (as defined in the Hong Kong Listing Rules) such as Hong Kong Kingboard and Hainan CNOOC Transportation. Following the Restructuring, we continued with such transactions and have commenced or will commence new transactions with our connected persons (including CNOOC and its Associates). To regulate such continuing business relationships, we have entered into various agreements with CNOOC and our other connected persons. Upon the listing of our H Shares on the Hong Kong Stock Exchange, transactions conducted under such agreements will constitute connected transactions under the Hong Kong Listing Rules.

We set forth below the descriptions of such connected transactions, including continuing connected transactions, historical figures and forecast figures (or, annual caps, where applicable) for those transactions based on our business assumptions. The historical amounts mentioned below should not be read or relied upon as an indication of future transaction amounts.

CONNECTED PERSONS

CNOOC and its Associates

CNOOC is one of our five Promoters. Immediately following the Global Offering (assuming the Over-allotment Option is not exercised), CNOOC will hold approximately 62.73% of our Company's issued share capital. As a result, CNOOC is our Controlling Shareholder and therefore CNOOC and its Associates (other than us) are our connected persons under Rule 14A.11 of the Hong Kong Listing Rules.

COSL is a subsidiary of CNOOC and is therefore an Associate of CNOOC. It is our connected person pursuant to Rule 19A.04 of the Hong Kong Listing Rules.

CNOOC Limited is a subsidiary of CNOOC and CNOOC China Limited is a wholly-owned subsidiary of CNOOC Limited. Both CNOOC Limited and CNOOC China Limited are Associates of CNOOC pursuant to Rule 19A.04 of the Hong Kong Listing Rules and are our connected persons.

CNOOC Finance is a subsidiary of CNOOC and is therefore an Associate of CNOOC. It is our connected person pursuant to Rule 19A.04 of the Hong Kong Listing Rules.

Hainan CNOOC Transportation

Hainan CNOOC Transportation, one of our subsidiaries, is owned as to 90% by Hainan Basuo (another subsidiary of our Company) and as to 10% by CNOOC Trust & Investment Co., Ltd., which is a subsidiary of CNOOC. CNOOC Trust & Investment Co., Ltd. is a substantial shareholder of Hainan CNOOC Transportation and therefore Hainan CNOOC Transportation is one of our connected persons according to Rule 14A.11(5) of the Hong Kong Listing Rules.

Hong Kong Kingboard and its Associates

CNOOC Jiantao is held as to 60% by us and as to 40% by Hong Kong Kingboard which is in turn a subsidiary of Kingboard Chemical. Although CNOOC Jiantao is treated as our jointly-controlled entity under IFRS, it is deemed to be one of our subsidiaries for the purpose of connected transactions. Hong Kong Kingboard is a substantial shareholder of CNOOC Jiantao, one of our subsidiaries, and

CONNECTED TRANSACTIONS

therefore it and its Associates (including Kingboard Chemical which is the parent company of Hong Kong Kingboard) are our connected persons according to Rules 1.01 and 14A.11(1) of the Hong Kong Listing Rules. For the purpose of this section, all historical transaction figures, forecast future transaction figures and future annual caps (where applicable) for CNOOC Jiantao are accounted for as to 60% of total transaction amounts, except in relation to connected transactions in Categories 9 and 12.

Minority Promoters and their Associates

Apart from CNOOC, our other Promoters are Zhejiang AMP, Guangdong AMP, Shanghai AMP and Transammonia (the “Minority Promoters”). Being Promoters, they are, on a strict interpretation of Rule 14A.11(3) of the Hong Kong Listing Rules, our connected persons and so are their respective Associates (including Guangxi Fudao AMP which is owned as to 70% by Zhejiang AMP and as to 30% by us). We have applied for, and the Hong Kong Stock Exchange has granted, a waiver to exempt our Minority Promoters and their Associates from being regarded as connected persons for the purpose of the Hong Kong Listing Rules in relation to all transactions contemplated in Category 14, and therefore, exempt all such transactions from all the requirements of Chapter 14A of the Hong Kong Listing Rules regarding connected transactions.

Hainan Development

One of our subsidiaries, Hainan Basuo, is owned as to 72.5% by us and as to 27.5% by Hainan Development. Hainan Development is a substantial shareholder of Hainan Basuo and is therefore one of our connected persons according to Rule 14A.11(1) of the Hong Kong Listing Rules.

SUMMARY OF CONNECTED TRANSACTIONS AND CONTINUING CONNECTED TRANSACTIONS

Category	Type of connected transactions	Nature	Waiver sought
Connected transaction with CNOOC			
1	Transactions under the Non-Competition Agreement	Exempted connected transactions	Not applicable
2	Indemnity under the Indemnity Agreement	Exempted connected transactions	Not applicable
Continuing connected transactions with CNOOC and its Associates			
3	Leases of properties by us from the CNOOC Group	Exempted continuing connected transactions	Not applicable
4	Use of CNOOC’s trademarks by us	Exempted continuing connected transactions	Not applicable
5	Provision of waste water treatment services by us to CNOOC China Limited	Exempted continuing connected transactions	Not applicable
8(c)	Sale of products by us to the CNOOC Group	Exempted continuing connected transactions	Not applicable

CONNECTED TRANSACTIONS

Category	Type of connected transactions	Nature	Waiver sought
9(c)	Provision of financial services to us by CNOOC Finance apart from Categories 9(a) and 9(b)	Exempted continuing connected transactions	Not applicable
6	Provision of transportation services by COSL to us	Non-exempted continuing connected transactions	Announcement requirement
7	Purchase of natural gas from CNOOC China Limited	Non-exempted continuing connected transactions	Announcement and independent shareholders' approval requirements
8(a)	Provision of services and supplies by the CNOOC Group to us	Non-exempted continuing connected transactions	Announcement and independent shareholders' approval requirements
8(b)	Provision of services and supplies by us to the CNOOC Group	Non-exempted continuing connected transactions	Announcement requirement
9(a)	Loans granted by CNOOC Finance to us	Non-exempted continuing connected transactions	Announcement and independent shareholders' approval requirements
9(b)	Deposits placed by us with CNOOC Finance	Non-exempted continuing connected transactions	Announcement and independent shareholders' approval requirements

Continuing connected transactions with Hainan CNOOC Transportation

10	Leases of property by Hainan CNOOC Transportation from us	Exempted continuing connected transactions	Not applicable
11(a)	Provision of transportation services by Hainan CNOOC Transportation to us	Non-exempted continuing connected transactions	Announcement requirement
11(b)	Provision of loading services by us to Hainan CNOOC Transportation	Non-exempted continuing connected transactions	Announcement requirement

Continuing connected transactions with Hong Kong Kingboard and its Associates

12	Provision by Kingboard Chemical of guarantees in relation to CNOOC Jiantao's borrowings	Exempted continuing connected transactions	Not applicable
13	Sale of products and provision of related services by us to Hong Kong Kingboard and/or its Associates	Non-exempted continuing connected transactions	Announcement and independent shareholders' approval requirements

CONNECTED TRANSACTIONS

Category	Type of connected transactions	Nature	Waiver sought
Continuing connected transactions with our Minority Promoters and their Associates			
14	Sale of products and provision of related services by us to our Minority Promoters and/or their Associates	Non-exempted continuing connected transactions	The Minority Promoters and their Associates being treated as connected persons

Potential connected transaction with Hainan Development

15	Exercise, acquisition, transfer or termination of Hainan Development's put option	Cannot be determined as of the Latest Practicable Date	Not applicable
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CONNECTED TRANSACTION WITH CNOOC

1. Non-Competition Agreement

In connection with the Restructuring, we entered into a non-competition agreement with CNOOC on 7 September 2006 (the “Non-Competition Agreement”), pursuant to which CNOOC (a) agreed that it will not, and it will procure its subsidiaries not to, directly or indirectly engage in businesses that compete or are likely to compete with our core business inside or outside China and (b) granted us the first transaction right, first option and pre-emptive right to acquire any competing businesses. See “Relationship with CNOOC—Non-Competition Agreement” for details of the terms of such agreement.

2. Indemnity Agreement

CNOOC entered into an indemnity agreement with us on 1 September 2006 (the “Indemnity Agreement”), pursuant to which CNOOC agreed to indemnify us against our direct economic losses arising from:

- (a) compensation payable by us to third parties in connection with environmental pollution resulting from our production operations before the Listing Date, including the pollution incident that occurred in 1997 when Fudao Phase I was operated by the predecessor of CNOOC Fudao (please refer to the description of such incident set out in “Our Business—Environmental Matters—Inspections”);
- (b) taxation, fines, penalties and charges payable by us resulting from our non-compliance with any tax laws and regulations before the Listing Date;
- (c) taxation claims made by any tax authority against us in respect of our tax liability incurred before the Listing Date;
- (d) our accrued or possible tax liability in respect of any action, omission or matter occurring before the Listing Date or in respect of any income, profits or gains accrued before the Listing Date; and
- (e) any misappropriation of our money placed with CNOOC Finance or any breach of CNOOC Finance's obligations in providing financial services to us. See “—Financial Services Agreement” in respect of such services.

CONNECTED TRANSACTIONS

CNOOC's indemnity in respect of items (c) and (d) above does not apply to the extent that:

- provision has been made for such taxation in our audited accounts for the periods up to 31 March 2006; or
- the taxation claim arises or the taxation liability increases as a consequence of any retrospective change in the law or regulation coming into force after the Listing Date.

CONTINUING CONNECTED TRANSACTIONS WITH CNOOC AND ITS ASSOCIATES

3. Properties Leasing Agreement

We leased certain properties for general commercial business and ancillary uses from certain members of the CNOOC Group (not being any of the three listed subsidiaries of CNOOC (the "Three Listed Subsidiaries"), namely, CNOOC Limited and COSL, which are listed on the Hong Kong Stock Exchange, and Offshore Oil Engineering Co., Ltd., which is listed on the Shanghai Stock Exchange). We have entered into a properties leasing agreement on 1 September 2006 with CNOOC (the "Properties Leasing Agreement") in relation to the terms and conditions for the leases of such properties.

The following table sets out the details of the properties covered by the Properties Leasing Agreement:

Landlord	Tenant	Type of premises	Current rental
(a) CNOOC Industry Company (中海實業公司)	Our Company	office space	RMB169,633.75 for a term from 19 June 2006 to 19 December 2006 inclusive of management fees
(b) CNOOC Pipeline Transportation Company Limited (中海石油管道輸氣有限公司)	Our Company (previously known as CNOOC Chemical)	office space	RMB133,324.80 per month inclusive of management fees for a term from 1 January 2006 to 31 December 2008

The term of the lease for each property shall not expire later than 31 December 2008, but may be renewed upon agreement provided that the requirements of the Hong Kong Listing Rules in relation to connected transactions are complied with. The rent and property management fee for each lease have been or will be agreed by the relevant parties considering factors such as the location and the state of the properties and shall not be higher than the market rental rates and property management rates of similar properties. We may, from time to time when the situation requires, enter into separate agreements in relation to the leases covered by the Properties Leasing Agreement which set out the specific terms and conditions of such leases according to the principles laid down in the Properties Leasing Agreement.

If we lease more properties from CNOOC or its Associates in the future, we will include such properties in the Properties Leasing Agreement. Similarly, once the lease of any property subject to the Properties Leasing Agreement is terminated, that property will be removed from the scope of the agreement.

Sallmanns (Far East) Limited, an independent valuer, has confirmed that the rent (and, where applicable, property management fee) for each lease under the Properties Leasing Agreement reflects the prevailing rates in the PRC and that the terms of the agreement are fair and reasonable to us.

Historical transaction figures

We incurred no rental expenditure for the properties subject to the Properties Leasing Agreement in 2003 and 2004. Our rental payment made to the CNOOC Group was approximately RMB250,000 for the year ended 31 December 2005 and approximately RMB463,000 for the three months ended 31 March 2006. The expenditure increased in 2006 as we commenced leasing property (b) from January 2006 onwards.

Forecast future transaction figures

Based on the above historical transaction values, the current agreed rental rates and the estimated future market rental rates of similar properties, our annual rental payments for properties leased from the CNOOC Group under the Properties Leasing Agreement are expected to be approximately RMB2,000,000, RMB2,080,000 and RMB2,080,000 for the three years ending 31 December 2006, 2007 and 2008, respectively. As the term of the lease for property (b), which is of a larger size with a correspondingly higher rental, commenced in 2006, the annual caps represent an increase from the 2005 historical figure.

4. CNOOC Trademarks Licence Agreement

We have been using certain of CNOOC's trademarks for our business. To regulate this business relationship, we and CNOOC entered into a trademarks licence agreement on 1 September 2006 (the "CNOOC Trademarks Licence Agreement"), under which CNOOC granted to us a non-exclusive licence to use such trademarks for our business. See paragraph II.2. of Appendix VIII to this Prospectus. Those trademarks were licensed to us at an annual royalty fee of RMB1,000 for a term commencing from the date of the CNOOC Trademarks Licence Agreement and expiring on the date when CNOOC and its Associates hold less than 30% of our Shares. CNOOC has agreed to pay for the registration cost for the trademarks during the term of the CNOOC Trademarks Licence Agreement. It has also agreed to increase the places of registration of the licensed trademarks upon our reasonable request and to pay for all expenses for enforcement against any infringement of the licensed trademarks by third parties.

Historical transaction figures

We did not pay any royalty to CNOOC for use of the licensed trademarks during the Track Record Period.

Forecast future transaction figures

Based on the agreed royalty amount set out in the Trademarks Licence Agreement, we believe that the annual royalty payable by us under the agreement will be not more than the de minimis threshold calculated under Rule 14A.33(3) of the Hong Kong Listing Rules for each of the three years ending 31 December 2006, 2007 and 2008.

5. Waste Water Treatment Services Agreement

CNOOC China Limited has been using our waste water facilities for processing its industrial waste water. To regulate this business relationship, we and CNOOC China Limited entered into a waste water treatment services agreement on 1 September 2006 (the “Waste Water Treatment Services Agreement”), under which we agreed to provide services to collect industrial waste water from CNOOC China Limited and to process it in our waste water facilities. CNOOC China Limited agreed to pay us a service fee which is determined by the volume of waste water we process and a unit service fee which is calculated based on our cost plus a margin of 15% on cost and currently is approximately RMB2.30 per tonne.

The term of the Waste Water Treatment Services Agreement commenced on the date of the agreement and will expire on 31 December 2008, but may be renewed upon agreement provided that the requirements of the Hong Kong Listing Rules in relation to connected transactions are complied with.

Historical transaction figures

Our annual revenue for providing waste water treatment services to CNOOC China Limited was approximately RMB25,000, RMB100,000 and RMB100,000 respectively for the three years ended 31 December 2003, 2004 and 2005 and approximately RMB25,000 for the three months ended 31 March 2006. We commenced providing waste water processing services to CNOOC China Limited in September 2003. During the Track Record Period, the monthly volume of waste water processed was an average of 3,600 tonnes and the unit service fee was an average of RMB2.30 per tonne.

Forecast future transaction figures

We believe that the volume of waste water we will process and the fee for services we provide under the Waste Water Treatment Services Agreement will be relatively stable in the near future. Based on the historical transaction values and our projection of service volumes, we expect that our annual revenue for providing waste water treatment services to CNOOC China Limited will be not more than the de minimis threshold calculated under Rule 14A.33(3) of the Hong Kong Listing Rules for each of the three years ending 31 December 2006, 2007 and 2008.

6. COSL Transportation Agreement

We intend to utilize ocean-going transportation services to be provided by COSL for our products including those to be produced by CNOOC Jiantao Methanol Plant following its completion of construction in September 2006, as COSL has a fleet of vessels available to provide us ocean-going transportation services at competitive fees. To regulate the provision of such services, our Company and COSL entered into a transportation services framework agreement on 1 September 2006 (the “COSL Transportation Agreement”), under which COSL may provide transportation services to us.

The transactions under the COSL Transportation Agreement will be conducted on normal commercial terms and conditions which shall not be less favorable than those offered to third parties and priced in accordance with the following pricing principles:

- (i) price prescribed by the PRC Government;

- (ii) where there is no government-prescribed price but there is a government guidance price, at a price not higher than the guidance price set by the PRC Government;
- (iii) where there is neither a government-prescribed price nor a government guidance price, the market price; and
- (iv) where none of the above is applicable, the price will be agreed between the relevant parties based on the cost plus a margin of up to 10% on cost.

Currently the transportation services covered by the COSL Transportation Agreement are not subject to any PRC Government prescribed or guidance price, but we consider it prudent to provide pricing principles (i) and (ii) in that agreement.

The term of the COSL Transportation Agreement commenced on the date of the agreement and will expire on 31 December 2008, but may be renewed upon agreement provided that the requirements of the Hong Kong Listing Rules in relation to connected transactions are complied with. COSL and we may, from time to time when the situation requires, enter into separate agreements which set out the specific scope of services, terms and conditions of providing such services according to the principles laid down by the COSL Transportation Agreement.

COSL did not provide any transportation services to us under the COSL Transportation Agreement during the Track Record Period and therefore there were no historical figures in relation to such agreement.

Future annual caps

We will start using transportation services under the COSL Transportation Agreement soon after commencement of operations of CNOOC Jiantao Methanol Plant. We anticipate that our demand for such services will increase in 2007 and 2008 when the plant undertakes mass production from 2007 onwards. Based on our projected future production volume of CNOOC Jiantao Methanol Plant, the expected market prices and our assumption that the PRC Government will not introduce prescribed or guidance prices in respect of the transportation services in the near future, we expect that our annual caps on expenditure for transportation services provided by COSL under the COSL Transportation Agreement will be RMB13,000,000, RMB45,000,000 and RMB48,000,000 respectively for the three years ending 31 December 2006, 2007 and 2008.

7. Natural Gas Sale and Purchase Agreements

CNOOC Limited and its subsidiaries mainly engage in offshore oil and natural gas exploration, development, production and sales, and own and operate Dongfang 1-1 Gasfield. Since such gasfield was CNOOC Limited's largest gasfield in terms of net proved reserves as of 31 December 2005, Fudao Phase II and CNOOC Jiantao use natural gas sourced from that gasfield as their principal raw material. For that purpose, we entered into two long-term agreements with CNOOC China Limited, a wholly-owned subsidiary of CNOOC Limited:

- (1) Dongfang 1-1 Offshore Gasfields Natural Gas Sale and Purchase Agreement between CNOOC China Limited and our Company dated 28 July 2003, under which CNOOC China Limited has committed to supply natural gas to our Company for Fudao Phase II at prices that are subject to adjustments on a quarterly basis by reference to the prices of four major types of crude oil in the international markets during the preceding quarter. The

term of this agreement commenced on 1 October 2003 and will expire on 30 September 2023.

- (2) Dongfang 1-1 Offshore Gasfields Natural Gas Sale and Purchase Agreement between CNOOC China Limited and CNOOC Jiantao dated 10 March 2005, under which CNOOC China Limited has committed to supply natural gas to CNOOC Jiantao for CNOOC Jiantao Methanol Plant at prices that are subject to adjustments on a monthly basis by reference to the prices of four major types of crude oil in the international markets during the preceding month. The term of this agreement is of 20 years commencing on 15 October 2006 although the earliest time CNOOC China Limited may provide natural gas to CNOOC Jiantao Methanol Plant is 9 May 2006.

Further, we may purchase natural gas from CNOOC China Limited for our future plants (including, subject to approvals from the relevant PRC authorities, a planned methanol production facility in Hainan with an annual designed production capacity of 1.13 million tonnes of methanol) and therefore we have entered into a natural gas sale and purchase framework agreement with CNOOC China Limited on 1 September 2006. This agreement does not include the transactions conducted under the two pre-existing agreements mentioned above. Under this framework agreement, CNOOC China Limited will sell natural gas to our Company and/or our subsidiaries at a price which is determined on a fair and reasonable basis (including by reference to the prices of four major types of crude oil in the international markets) and in accordance with normal commercial customs. The term of the agreement is of 20 years commencing on the date of the agreement. CNOOC China Limited and our Company or our relevant subsidiaries will enter into separate agreements which will set out the specific terms and conditions for natural gas sales and purchases according to the principles laid down by this framework agreement. As of the Latest Practicable Date, we have not purchased any natural gas under this framework agreement.

The three above-mentioned agreements are collectively referred to as the “Natural Gas Sale and Purchase Agreements”.

We believe a term of 20 years for each of the Natural Gas Sale and Purchase Agreements is appropriate because (a) the 20-year term was determined, according to market practice for offshore gasfields, based on the estimated reserves and production profile of CNOOC China Limited’s offshore gasfields, (b) the long term of the Natural Gas Sale and Purchase Agreements conforms with the normal business practice of CNOOC Limited in supplying natural gas from its gasfields of entering into supply contracts of 15 to 20 year terms in order for CNOOC Limited to secure return on its investment from exploration of natural gas, (c) through such long-term agreements, we have been able to secure a stable source of natural gas, which is a key raw material for our production, and to avoid unnecessary disruption to our operation, and (d) as the composition of natural gas varies between source gasfields and the design of our production facilities has to take into account and, in future, will take into account, the gas source, we are prevented from switching from one gas source to another without first reconfiguring such production facilities. Our relevant production complexes have been or will be designed to use natural gas from specific gasfields operated by CNOOC China Limited, and therefore long-term agreements are essential to justify our significant investment in production facilities.

Historical transaction figures

During the Track Record Period, we only purchased natural gas from CNOOC China Limited for Fudao Phase II as the construction of CNOOC Jiantao Methanol Plant was completed in September 2006. Our expenditure for the purchase of natural gas under the Natural Gas Sale and Purchase Agreement dated 28 July 2003 was approximately RMB95,818,000, RMB296,522,000 and RMB341,838,000 respectively for the three years ended 31 December 2003, 2004 and 2005 respectively and approximately RMB70,224,000 for the three months ended 31 March 2006. Fudao Phase II was completed and put in trial production in 2003 and only commenced mass production in 2004, leading to an increase in expenditure on natural gas purchases from 2003 to 2004. Expenditure incurred by Fudao Phase II on natural gas purchases in 2003 was capitalized as construction in progress in our accounts. The year-on-year increase in the historical figures was partly due to the increase in production volume from 2004 to 2005 and partly due to the increase in crude oil prices that resulted in upward adjustments in the prices at which we purchased natural gas.

Future annual caps

Based on the historical transaction values, our projection of future production volume of our Hainan plants, our expansion plan and the expected trends of movements of crude oil prices, we will cap our expenditure for purchases from CNOOC China Limited under the Natural Gas Sale and Purchase Agreements within RMB510,300,000, RMB657,090,000 and RMB1,046,640,000 for the three years ending 31 December 2006, 2007 and 2008, respectively.

The estimated rises in expenditure for purchases of natural gas from CNOOC China Limited from 2005 to 2006 and from 2006 to 2007 take into account the completion and commencement of trial operation of CNOOC Jiantao Methanol Plant in September 2006 which will bring about increased demand for natural gas for 2006. Our demand will further increase in 2007, which is the first full year of operation of CNOOC Jiantao Methanol Plant. Further, we anticipate that the natural gas prices will be adjusted upwards according to the adjustment mechanisms in the two pre-existing agreements given the current trends in crude oil price movements, therefore further increasing our expenditure. The estimated rise in expenditure from 2007 to 2008 is also attributed to the increase in natural gas purchases for our new projects (such as the additional methanol production facility described in the section headed “Our Business—Principal production facilities—Potential facilities” in this Prospectus) pursuant to the pricing principles set out in the natural gas sale and purchase framework agreement (including by reference to the prices of four major types of crude oil in the international markets).

As CNOOC Limited is a company listed on the Hong Kong Stock Exchange, its long-term sales of natural gas and liquefied natural gas to CNOOC and its Associates (including us) are subject to the requirements in Chapter 14A of the Hong Kong Listing Rules which include approval by independent shareholders of CNOOC Limited.

8. Comprehensive Services and Product Sales Agreement

We have been receiving services and supplies from, and providing services and supplies to, the CNOOC Group prior to the Restructuring and will continue to do so after the Listing Date. To regulate such business relationships, we entered into a comprehensive services and product sales framework agreement with CNOOC on 1 September 2006 (the “Comprehensive Services and Product Sales Agreement”), pursuant to which:

- (a) CNOOC and its Associates (but excluding for the purpose of the Comprehensive Services and Product Services Agreement the Three Listed Subsidiaries) may provide services and supplies that we may require for our business operation and production such as:
 - telecommunication and computer network services;
 - enterprise resources planning and office automation services;
 - construction of our production facilities and related construction project management and supervision;
 - machines and vehicle rental and maintenance;
 - production equipment rental and repair;
 - transportation services;
 - community services including catering, accommodation, hospital and schooling; and
 - training.
- (b) we may provide to CNOOC and its Associates services and supplies such as:
 - machines and vehicle rental;
 - transportation services;
 - business management services; and
 - catering and accommodation.
- (c) we may sell to CNOOC and its Associates products produced by us.

The transactions under the Comprehensive Services and Product Sales Agreement will be conducted on normal commercial terms and conditions which shall not be less favorable than those offered to third parties and priced in accordance with the following pricing principles:

- (i) price prescribed by the PRC Government;
- (ii) where there is no government-prescribed price but there is a government guidance price, at a price not higher than the guidance price set by the PRC Government;
- (iii) where there is neither a government-prescribed price nor a government guidance price, the market price; and
- (iv) where none of the above is applicable, the price will be agreed between the relevant parties based on the cost plus a margin of up to 10% on cost.

Currently, apart from certain products produced by us such as urea products that are subject to price controls imposed by the PRC Government, all services and supplies covered by the Comprehensive Services and Product Sales Agreement are not subject to any PRC Government

prescribed or guidance prices. However, we consider it prudent to provide pricing principles (i) and (ii) in the Comprehensive Services and Product Sales Agreement.

The term of the Comprehensive Services and Product Sales Agreement commenced on the date of the agreement and will expire on 31 December 2008, but may be renewed upon agreement provided that the requirements of the Hong Kong Listing Rules in relation to connected transactions are complied with. Each party is obliged to purchase the relevant products and services from the other party provided that the terms offered by the other party are no less favorable to that party than the terms offered by independent third parties. CNOOC (or its relevant Associate) and we may, from time to time when the situation requires, enter into separate agreements which set out the specific scope of services, supplies or products, terms and conditions of providing such services or supplies or selling products according to the principles laid down by the Comprehensive Services and Product Sales Agreement.

Historical transaction figures

Our expenditure on a pro-forma basis (as if Tianye Chemical had been our subsidiary during the Track Record Period) for acquiring services and supplies provided by CNOOC and its Associates was approximately RMB5,068,000, RMB10,556,000 and RMB53,783,000 respectively for the three years ended 31 December 2003, 2004 and 2005 and approximately RMB13,112,000 for the three months ended 31 March 2006. The increase in our expenditure from 2003 to 2004 was mainly due to the computer network services provided to us in 2004. The rise from the 2004 figure to the 2005 figure was primarily because we engaged CNOOC's Associates to provide construction and office automation services in 2005. Our revenue on a pro-forma basis for providing services and supplies to CNOOC and its Associates was approximately RMB549,000, RMB321,000 and RMB182,000 respectively for the three years ended 31 December 2003, 2004 and 2005 and approximately RMB390,000 for the three months ended 31 March 2006. We have not historically sold our products to CNOOC or its Associates during the Track Record Period.

Future annual caps

Based on the historical transaction values, the projection of future transaction volumes and market prices and our assumption that the PRC Government will not introduce prescribed or guidance prices for the services and supplies covered by the Comprehensive Services and Product Sales Agreement in the near future, we expect that our annual caps on expenditure for acquiring services and supplies provided by CNOOC and its Associates will be RMB278,520,000, RMB102,300,000 and RMB74,800,000 respectively for the three years ending 31 December 2006, 2007 and 2008, and our annual caps on revenue for providing services and supplies to CNOOC and its Associates will be approximately RMB4,400,000, RMB4,400,000 and RMB3,300,000 respectively for each of the three years ending 31 December 2006, 2007 and 2008.

The increase from the 2005 historical figure to the 2006 cap relating to our expenditure for acquiring services and supplies from the CNOOC Group is mostly due to the construction and enterprise resource planning services provided and to be provided to us in 2006. Most of our construction projects that require services from CNOOC and its Associates will be completed, and our ERP will also be established, between 2006 and 2007. Therefore, our demand for services and supplies from CNOOC and its Associates will gradually decrease from 2006 to 2008. Nevertheless, we expect that we will still require services and supplies in 2008 from the CNOOC Group apart from construction

services, including telecommunication and computer network, office automation and community services.

The historical figures relating to our revenue for providing services and supplies to the CNOOC Group are larger than the caps because more accommodation and catering services will be provided by us to the CNOOC Group both in Hainan and Inner Mongolia during the three years from 2006 to 2008. Nevertheless, we expect that the CNOOC Group will reduce its utilization of our services and supplies in Inner Mongolia from 2008 onwards and therefore the 2008 cap is smaller than the 2006 and 2007 caps.

As of the Latest Practicable Date, we have not sold any of our products to CNOOC and its Associates. We may or may not sell our products to CNOOC and its Associates in 2006 to 2008, and currently we are not in a position to determine the type of products we may sell to them. But if we sell products to them under the Comprehensive Services and Product Sales Agreement, our annual revenue in that regard is expected to be not more than the de minimis threshold calculated under Rule 14A.33(3) of the Hong Kong Listing Rules.

9. Financial Services Agreement

We utilize from time to time financial services provided by CNOOC Finance and therefore entered into a financial services framework agreement with CNOOC Finance on 1 September 2006 (the “Financial Services Agreement”), pursuant to which CNOOC Finance will provide to us a range of financial services including the following:

- (a) provision of loans to us which do not include entrustment loans referred to in Category (c2);
- (b) deposit services;
- (c1) bank notes discounting services;
- (c2) arrangement of entrustment loans between our Company and our subsidiaries; and
- (c3) settlement services which include settlement for transactions between our Company and our subsidiaries and for transactions between us and members of the CNOOC Group.

The fees and charges payable by us to CNOOC Finance under the Financial Services Agreement are determined on the following basis:

- (a) provision of loans to us: the interest rates for such loans are determined in accordance with the standard rates promulgated by the PBOC from time to time, and may be reduced where the relevant laws and regulations allow;
- (b) deposit services: the interest rates for such deposits are determined in accordance with the standard rates promulgated by the PBOC from time to time;
- (c1) bank notes discounting services: the interest rates for discounting services are determined in accordance with the standard rates promulgated by the PBOC from time to time less discounts set out in the specific agreements; and the interest for bank notes discounting is borne by the relevant parties presenting the notes;
- (c2) arrangement of entrustment loans between our Company and our subsidiaries: the annual service fee payable by us is set at a rate, such that the aggregate amount of service fee and

loan interest together will not exceed the interest for securing a loan of the same term directly from independent commercial banks; and

(c3) settlement services: no service fee is charged.

Under the Financial Services Agreement, we shall have a right of set off such that, in the event of any misuse or default by CNOOC Finance in respect of amounts deposited with it by us, we will be able to offset the amount due to us from CNOOC Finance against the amounts outstanding from us to CNOOC Finance. CNOOC Finance shall not have any offset right. The term of the Financial Services Agreement commenced on the date of the agreement and will expire one year after the Listing Date in respect of Category (b) services and on 31 December 2008 in respect of other services, but may be renewed upon agreement provided that the requirements of the Hong Kong Listing Rules in relation to connected transactions are complied with. CNOOC Finance and we may, from time to time when the situation requires, enter into separate agreements which set out the specific scope of services, terms and conditions of providing such financial services according to the principles laid down by the Financial Services Agreement.

CNOOC China Limited, CNOOC Finance and we entered into a natural gas sale and purchase settlement cooperation agreement on 28 July 2005 (the “Natural Gas Settlement Agreement”), pursuant to which our payments for purchases of natural gas from CNOOC China Limited will be settled by CNOOC Finance by debiting the relevant amounts from our account with CNOOC Finance and crediting the same amounts in CNOOC China Limited’s account with CNOOC Finance. Such settlement arrangements constitute connected transactions for us under Category (c3) above. CNOOC Finance and we entered into a settlement loan agreement (the “Settlement Loan Agreement”) on the same day. Pursuant to these two agreements, if we do not have enough balance in our account with CNOOC Finance to pay for natural gas purchased from CNOOC China Limited, CNOOC Finance provides us with a RMB300 million credit facility without our application. The granting of any loan under the Settlement Loan Agreement constitutes a connected transaction for us under Category (a) above. These two agreements are separate agreements referred to in the Financial Services Agreement.

Internal control procedures and corporate governance measures

In order to protect the interests of our shareholders, we will adopt upon the Listing Date the following 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:

- Our annual financing plans will be subject to the approval by our independent non-executive Directors. Such plans will include an average percentage of our loans from CNOOC Finance compared with our total borrowings (a “Loan Percentage”) for the year. In setting such percentage, we will refer to all relevant factors such as the average percentage for the previous year, the costs of different financing alternatives, our cash flow forecast and our capital expenditure plan for the year.
- When we need to enter into any loan or credit facilities agreements with CNOOC Finance after the Listing Date in relation to our borrowings from CNOOC Finance, we will obtain at least two comparable offers from independent commercial banks or financial institutions for a loan of the same term or a credit facility of the same nature (as the case may be). The terms of all such offers, together with the offer from CNOOC Finance, will be forthwith disclosed to our independent non-executive Directors in order for them to

decide whether we should accept CNOOC Finance's offer. Our independent non-executive Directors are expected to make a decision within a reasonable time based on factors including the terms of the offers and the reliability of the relevant banks or financial institutions.

- All our borrowings from CNOOC Finance (including drawdowns from credit facilities) will be conducted by us in accordance with the terms approved by our independent non-executive Directors.
- Any approval or decision mentioned above will be made by (a) the majority (that is, at least three out of four) of our independent non-executive Directors or (b) two of our independent non-executive Directors where the other two independent non-executive Directors abstain from voting for the decision or do not participate in the decision-making process within a reasonable time.
- We will report every six months to our independent non-executive Directors on the Loan Percentages and any changes in the credit ratings of CNOOC Finance during for the preceding six-month period.
- We will prepare regular projections on our expenditure for natural gas purchases from CNOOC China Limited and other products and services from other members of the CNOOC Group. We will direct our customers to make goods/services payments to our accounts maintained with independent banks and our accounts maintained with CNOOC Finance, so that the aggregate daily outstanding balance of our CNOOC Finance deposit accounts (excluding the balance for extending entrustment loans between our Company and our subsidiaries) will match with such projection but will not otherwise substantially exceed the projected amounts.
- We will regularly review the cash flows of each of our Company and our individual subsidiaries and project the requirements to extend intra-group entrustment loans.
- In order to allow our independent non-executive Directors to monitor the implementation of the procedures in relation to deposits, we will report on a quarterly basis to our independent non-executive Directors on the movements in each of our CNOOC Finance deposit accounts together with our banks accounts.
- The above-mentioned procedures and measures will be formalized into written manuals and highlighted to all members of our Board and our treasury department.

Background of CNOOC Finance

CNOOC Finance is a non-bank financial institution established in June 2002 with the approval of the PBOC. It is subject to the supervision of the China Banking Regulatory Commission. According to its business licence, it is authorized to provide to us all services set out in the Financial Services Agreement, provide similar services to other members of the CNOOC Group (but not other parties) and make investments in securities of financial institutions and marketable securities. It has been providing financial services to members of the CNOOC Group (including us) as an intra-group service provider.

As far as we are aware, the regulation by the China Banking Regulatory Commission of CNOOC Finance is more stringent than the regulation of commercial banks in certain respects. In accordance with the relevant requirements under the Administrative Rules Governing Corporate

Financial Institutions promulgated by the China Banking Regulatory Commission on 27 July 2004, group finance companies (including CNOOC Finance):

- are not allowed to engage in non-financial services business, including property investments or trading;
- must comply with the following ratio requirements: (a) the capital adequacy ratio shall not be lower than 10% (while the capital adequacy ratio applicable to commercial banks is only 8%), (b) the inter-bank borrowing balances shall not exceed the total registered capital of the relevant finance company, (c) the total amount of outstanding guarantees shall not be more than the total registered capital of the relevant finance company, (d) the short-term securities investments to total equity amount ratio shall not exceed 40%, (e) the ratio of long-term investment to total equity shall not exceed 30%, and (f) the ratio of self-owned fixed assets to total equity shall not exceed 20%; and
- are required to deposit a mandatory proportion of the deposits they receive with the PBOC.

CNOOC Finance was rated BBB+ by The Standard & Poor's and A2 by Moody's in March 2005. The Standard & Poor's rating was raised from BBB+ to A- in November 2005. We believe that such credit ratings are among the highest ratings assigned by these rating agencies to PRC financial institutions, including commercial banks.

As of 31 December 2005, CNOOC Finance had a total asset value of approximately RMB32.2 billion which included liquid assets (such as bank deposits, central bank notes and treasure bonds) of approximately RMB27.4 billion. It has secured lines of credit of an amount exceeding RMB10 billion from several major PRC commercial banks. CNOOC Finance's before-tax profits were approximately RMB137 million, RMB207 million and RMB201 million for the years ended 31 December 2003, 2004 and 2005 respectively, and its after-tax profits were approximately RMB97 million, RMB147 million and RMB142 million respectively, representing an annual return on equity of about 6.6%, 9.9% and 9.4% for the same periods. As of 31 December 2003, 2004 and 2005, the current ratios of CNOOC Finance were approximately 99.7%, 91.8% and 89.6%, respectively and its capital adequacy ratios were 42.9%, 44.5% and 22.7%, respectively.

As far as we are aware, the board of directors of CNOOC Finance established three committees (namely, the assets and liabilities management committee, credit assessment committee and investment decisions committee) to safeguard CNOOC Finance's assets and strengthen its corporate governance practices. In respect of day-to-day management, CNOOC Finance is operated by specific departments including the settlement department, credit department, investment department, treasury department, finance department, general management department and internal audit department. In particular, the internal audit department assumes an internal independent supervisory role and is responsible for examining and auditing the business operation of other departments with a mandate to identify operational risks from the perspective of organizational structure and inter-departmental coordination. Further, CNOOC Finance has in place intra-group check-and-balance mechanisms (such as division of duties, regular and random internal examination, re-assessment and upper level supervision) to identify operational bottlenecks and irregularities and to deal with problems (if any) in a timely and effective manner. It maintains a management system that delegates decision-making authority to its board, the chairman, board committees and the general manager respectively in accordance with the importance and risk level of the subject matter, with the aim of achieving effective identification and management of risks relating to specific decisions.

Reasons for utilizing financial services provided by CNOOC Finance

We believe that CNOOC Finance, with its credit ratings, asset size, banking credits and corporate governance practices, will be able to fulfil its obligations under the Financial Services Agreement. We also believe that the risk profile of CNOOC Finance, as a provider of financial services to us, is not any greater than those of independent commercial banks in China because:

- CNOOC Finance is regulated by the PBOC and the China Banking Regulatory Commission and it provides its services in full compliance with the relevant rules and operational requirements including capital risks guidelines and requisite capital adequacy ratios, of those regulatory authorities.
- As far as we are aware, CNOOC Finance has not defaulted on any of its credit obligations or breached any rules or operations requirements of such regulatory authorities.
- CNOOC Finance has implemented capital risk control measures that we believe are at least as stringent as those of the major commercial banks in China. It may provide us access to its books and accounts for inspection upon our request to enable us to monitor its risk control measures.

The advantages of utilizing financial services provided by CNOOC Finance over utilizing similar services provided by independent commercial banks can be realized in the following respects:

- (i) The terms (such as interest rates and loan conditions) of loans extended to us by CNOOC Finance are generally more favorable to us compared with those of loans from independent commercial banks, given CNOOC Finance's understanding of our financial status and business prospects. In our experience, the time required for approval of loans by CNOOC Finance tends to be shorter than the time for approval by commercial banks.
- (ii) In respect of deposit services, although CNOOC Finance provides interest rates that are the same as those offered by independent commercial banks, as such rates are regulated by the PBOC, CNOOC Finance assists us to formulate a beneficial deposit mix comprising different types of deposits such as current deposits, call deposits and fixed deposits, which allows us to increase our return on funds and retain sufficient working capital flexibility.
- (iii) Discounting of bank notes by CNOOC Finance provides our customers flexibility in payment terms and accelerates our collection of sale proceeds. Upon discount of the notes, we may receive the sale proceeds as if the sale was effected as a cash sale while the interest of the discounting services is borne by our relevant customers who present the bank notes as payment for purchasing our products. This arrangement helps to efficiently reduce our receivables and accelerate our fund flows which may eventually result in savings of financial costs and improve our financial structure.
- (iv) PRC laws do not permit companies, including affiliates, to extend intra-group loans directly without going through a financial agency. CNOOC Finance serves as the financial agency, through which the funds of our Company and our subsidiaries may be channelled to be used by each other by way of entrustment loans.
- (v) Through CNOOC Finance's settlement services, we are able to achieve same-day zero-rate settlement at no cost. As CNOOC Finance is more familiar with the business and transaction pattern of the CNOOC Group, the settlement services provided by CNOOC Finance tend to provide a more efficient and orderly platform than those that could be provided by independent commercial banks for processing transactions between our

CONNECTED TRANSACTIONS

Company and our subsidiaries and between us and members of the CNOOC Group. Such a platform also helps to reduce our transaction costs such as handling fees for transfers of funds, time costs and other administrative expenses.

- (vi) Through the information system of CNOOC Finance, we may inquire at any time the status of receipts and payments of funds made through CNOOC Finance at no cost.
- (vii) As an intra-group service provider, CNOOC Finance generally has better and more efficient communication with us compared with independent banks and financial institutions.

However, if independent commercial banks offer advantages and fund security of a level that is more favorable to us in respect of the financial services set out in the Financial Services Agreement, we may discontinue our use of CNOOC Finance's service and turn to independent banks and financial institutions without having to incur unreasonable extra costs.

Historical transaction figures

A breakdown of the approximate historical transaction figures on a pro-forma basis (as if Tianye Chemical had been our subsidiary during the Track Record Period) is as follows:

	For the year ended 31 December 2003 (in RMB)	For the year ended 31 December 2004 (in RMB)	For the year ended 31 December 2005 (in RMB)	For the three months ended 31 March 2006 (in RMB)
(a) Maximum daily outstanding balance of loans (including accrued interest) granted by CNOOC Finance to us excluding entrustment loans referred to in Category (c2)	3,700,000	2,500,000	6,250,000	22,950,000
(b) Maximum daily outstanding balance of deposits (including accrued interest) placed by us with CNOOC Finance excluding the deposits for the purpose of extending entrustment loans referred to in Category (c2)	252,301,000	708,008,000	1,108,893,000	1,398,634,000
(c) Fees and charges paid by us to CNOOC Finance relating to entrustment loans between our Company and our subsidiaries	—	—	2,500	1,600

Future annual caps

Based on the historical transaction values and the projected growth of future transactions, we expect that in respect of Category (a), the annual caps on the maximum daily outstanding balance, after the listing of our H Shares on the Hong Kong Stock Exchange, of loans (including accrued interest) granted by CNOOC Finance to us excluding entrustment loans referred to in Category (c2) will be RMB400,000,000, RMB500,000,000 and RMB600,000,000 respectively for the three years ending 31 December 2006, 2007 and 2008. The increase from the 2005 historical figure to the annual caps for 2006 to 2008 is partly due to the loan that CNOOC Jiantao may require from CNOOC Finance for the construction of CNOOC Jiantao Methanol Plant under the pre-existing loan facilities pursuant to which

CNOOC Finance will lend up to RMB280,000,000 to CNOOC Jiantao. CNOOC Jiantao intends to borrow an amount of about such limit from 2006. The full repayment of such loan does not fall due before 31 December 2008 according to the relevant loan facilities agreement and therefore the majority amount of such loan is expected to remain outstanding throughout the three years from 2006 to 2008. See “—Kingboard Guarantee Arrangements”. The other reason for the increase is that our Directors expect that we will utilize the RMB300,000,000 on credit facility extended to us under the Natural Gas Settlement Agreement and the Settlement Loan Agreement in order to improve our working capital efficiency. The maximum amounts that we expect to borrow from CNOOC Finance under such credit facility are expected to increase gradually from 2006 to 2008 following the expansion of our business which will lead to increasing purchases of natural gas from CNOOC China Limited and resultant increased utilization of the credit facility under the Natural Gas Settlement Agreement and the Settlement Loan Agreement as part of our cash flow and financial management.

For Category (b), we expect that the cap on the maximum daily outstanding balance, after the listing of our H Shares on the Hong Kong Stock Exchange, of deposits (including accrued interest) placed by us with CNOOC Finance excluding deposits for the purpose of extending entrustment loans referred to in Category (c2) will be RMB300,000,000 for a period of one calendar year commencing on the Listing Date. This cap amount was calculated on the basis of several factors including the requirement to settle accounts payables to the CNOOC Group (including those arising from our purchases of natural gas from CNOOC China Limited) through our deposit accounts maintained with CNOOC Finance, the expected amount of interest income compared with interest income that could otherwise be realized by placing deposits with independent commercial banks and the strategies in our treasury management.

Both the historical figures and the future caps refer to the maximum daily outstanding balances during the relevant period. They are not cumulative in nature and therefore even if the historical figures were relatively high, we can still limit the loan and deposit balances within the cap figures in the future after the listing of our H Shares on the Hong Kong Stock Exchange.

In respect of Categories (c1), (c2) and (c3), we expect that the aggregate fees and charges payable by us to CNOOC Finance will not be more than the de minimis threshold calculated under Rule 14A.33(3) of the Hong Kong Listing Rules for each of the three years ending 31 December 2006, 2007 and 2008.

CONTINUING CONNECTED TRANSACTIONS WITH HAINAN CNOOC TRANSPORTATION

10. Hainan CNOOC Transportation Property Leasing Agreement

Hainan CNOOC Transportation has been leasing a property with an area of approximately 80 m² as an office from CNOOC Fudao under a property leasing agreement dated 1 January 2006 entered into between CNOOC Fudao and Hainan CNOOC Transportation (the “Hainan CNOOC Transportation Property Leasing Agreement”). The term of the agreement commenced on 1 January 2006 and will expire on 31 December 2008 and is subject to renewal.

The rental for the property is RMB43,200 per year and is payable in full on the first month of the fourth quarter of each year. The rental is inclusive of all utility fees. Should the rental be adjusted during the term of the agreement, it will be subject to arms’ length negotiation between the parties.

Sallmanns (Far East) Limited, an independent valuer, has confirmed that the rent for the lease under the Hainan CNOOC Transportation Property Leasing Agreement reflects the prevailing market rates in the PRC and the terms of the agreement are fair and reasonable to us.

Historical transaction figures

There was no historical revenue figure for each of the years from 2003 to 2005. Our revenue generated from the Hainan CNOOC Transportation Property Leasing Agreement was RMB10,800 for the three months ended 31 March 2006.

Forecast future transaction figures

Based on the agreed rent in the Hainan CNOOC Transportation Property Leasing Agreement, we believe that our annual revenue for leasing the relevant property to Hainan CNOOC Transportation will be not more than the de minimis threshold calculated under Rule 14A.33(3) of the Hong Kong Listing Rules for each of the three years ending 31 December 2006, 2007 and 2008.

11. Transportation Agreement

We use Hainan CNOOC Transportation to transfer our products and we also provide loading services to Hainan CNOOC Transportation. To regulate the provision of such services between Hainan CNOOC Transportation and us (excluding Hainan CNOOC Transportation), our Company and Hainan CNOOC Transportation entered into a loading and transportation services framework agreement on 1 September 2006 (the “Transportation Agreement”), under which:

- (a) Hainan CNOOC Transportation may provide transportation services to us; and
- (b) we may provide loading services to Hainan CNOOC Transportation.

The transactions under the Transportation Agreement will be conducted on normal commercial terms and conditions which shall not be less favorable than those offered to third parties and priced in accordance with the following pricing principles:

- (i) price prescribed by the PRC Government;
- (ii) where there is no government-prescribed price but there is a government guidance price, at a price not higher than the guidance price set by the PRC Government;
- (iii) where there is neither a government-prescribed price nor a government guidance price, the market price; and
- (iv) where none of the above is applicable, the price will be agreed between the relevant parties based on the cost plus a margin of up to 10% on cost.

Currently the transportation services covered by the Transportation Agreement are not subject to any PRC Government prescribed or guidance price, but we consider it prudent to provide pricing principles (i) and (ii) in that agreement.

The term of the Transportation Agreement commenced on the date of the agreement and will expire on 31 December 2008, but may be renewed upon agreement provided that the requirements of the Hong Kong Listing Rules in relation to connected transactions are complied with. Services under the agreement are provided on a non-exclusive basis. Each party is obliged to acquire the relevant

services from the other party provided that the terms offered by the other party are no less favorable to that party than the terms offered by independent third parties. Hainan CNOOC Transportation and we may, from time to time when the situation requires, enter into separate agreements which set out the specific scope of services, terms and conditions of providing such services according to the principles laid down by the Transportation Agreement.

Historical transaction figures

Our expenditure for transportation services provided by Hainan CNOOC Transportation were approximately RMB1,913,000, RMB3,391,000 and RMB1,504,000 respectively for the three years ended 31 December 2003, 2004 and 2005. We did not incur any expenditure in that regard for the three months ended 31 March 2006. The fluctuations in historical expenditure were a direct reflection and result of the fluctuations in the volume of our export sales in corresponding years during the Track Record Period. Please refer to “Our business—Sales and marketing—Sales of urea products”.

Our revenue for loading services provided to Hainan CNOOC Transportation was generated by Hainan Basuo and was approximately RMB6,422,000 for the year ended 31 December 2005 and approximately RMB3,155,000 for the three months ended 31 March 2006. There was no revenue in that regard for the years 2003 and 2004 as Hainan Basuo was incorporated in 2005.

Future annual caps

We believe that, as our demand for transportation services to be provided by Hainan CNOOC Transportation increases, there will be more transactions under the Transportation Agreement. Based on the historical transaction values, projection of future transactions growth and market service fees and our assumption that the PRC Government will not introduce prescribed or guidance prices in respect of transportation services in the near future, we expect that our annual caps on expenditure for transportation services provided by Hainan CNOOC Transportation under the Transportation Agreement will be RMB5,300,000, RMB5,700,000 and RMB6,000,000, respectively for the three years ending 31 December 2006, 2007 and 2008, and our revenue for loading services provided to Hainan CNOOC Transportation will be RMB19,000,000, RMB20,000,000 and RMB21,000,000, respectively for the three years ending 31 December 2006, 2007 and 2008.

Although no expenditure was incurred by us for transportation services provided by Hainan CNOOC Transportation during the three months ended 31 March 2006 as there were no export sales during those three months when the PRC Government imposed a seasonal tariff on exports, we expect that we will enhance our export sales effort from 2006 to 2008 and therefore will continue to require such transportation services for those three years. The increase from the historical figures to the caps reflects the expected increase in future export sales compared with historical export sales.

The increase from the historical figures to the caps relating to our revenue for loading services provided to Hainan CNOOC Transportation is because Hainan CNOOC Transportation is expected to require more services from us from 2006 onwards when Hainan CNOOC Transportation’s business expands following the overall expansion of our business. This trend is evidenced by the comparison of the 2005 whole year figure with the 2006 first quarter figure.

CONTINUING CONNECTED TRANSACTIONS WITH HONG KONG KINGBOARD AND ITS ASSOCIATES

12. Kingboard Guarantee Arrangements

CNOOC Jiantao is a Sino-foreign equity joint venture currently held as to 60% by us and as to 40% by Hong Kong Kingboard. It has secured financing for the construction of CNOOC Jiantao Methanol Plant and the lenders, in line with common practice in the PRC banking industry, required security from CNOOC Jiantao's shareholders. Accordingly, we and Kingboard Chemical (the holding company of Hong Kong Kingboard) provided guarantees in relation to the borrowings of CNOOC Jiantao on a several (but not a joint and several) basis in the initial ratio of 60:40, which is the same ratio of the respective shareholdings in CNOOC Jiantao of us and Hong Kong Kingboard. When the completion certificate for CNOOC Jiantao Methanol Plant has been issued and the injection of capital has reached 80% of the total project investment amount, the proportion of our and Kingboard Chemical's guarantee of CNOOC Jiantao's borrowings will be adjusted to 50:50. All such guarantees are provided for CNOOC Jiantao's benefit on normal commercial terms. No security over our assets or the assets of CNOOC Jiantao is granted in favor of Kingboard Chemical or Hong Kong Kingboard in respect of the guarantees given by Kingboard Chemical. Details of the guarantees are set out as follows:

<u>Lender</u>	<u>Maximum loan amount set out in the relevant loan agreement</u>	<u>Outstanding loan amount as of 31 July 2006</u>	<u>Drawdown period</u>	<u>Term of the loan</u>
Industrial and Commercial Bank of China	RMB50 million	RMB30 million	1 January 2005 to 30 June 2007	120 months from the first drawdown date which was 30 May 2006
Bank of China	U.S.\$69.6 million	U.S.\$55.5 million	1 January 2005 to 30 June 2007	120 months from the first drawdown date which was 24 November 2005
China Construction Bank	RMB20 million	RMB20 million	1 January 2005 to 30 June 2007	120 months from the first drawdown date which was 16 May 2006
CNOOC Finance	RMB280 million	RMB60 million	1 January 2005 to 30 June 2007	120 months from the first drawdown date which was 6 March 2006

All guarantees given by us and Kingboard Chemical in relation to CNOOC Jiantao's borrowings will be released when construction of CNOOC Jiantao Methanol Plant has been completed and CNOOC Jiantao has mortgaged its assets in favor of the lenders, such events being expected to occur at the end of 2006.

13. Kingboard Product Sales and Services Agreement

Upon the commencement of operation of CNOOC Jiantao Methanol Plant, we intend to sell methanol products to Hong Kong Kingboard or its Associates. We therefore entered into with Hong Kong Kingboard a product sales and related services framework agreement on 22 August 2006 (the "Kingboard Product Sales and Services Agreement"), pursuant to which we agreed to sell products

produced by us and to provide related services such as transportation services to Hong Kong Kingboard and its Associates.

The transactions under the Kingboard Product Sales and Services Agreement will be conducted on normal commercial terms and conditions which shall not be less favorable than those offered to third parties and priced in accordance with the following pricing principles:

- (i) price prescribed by the PRC Government;
- (ii) where there is no government-prescribed price but there is a government guidance price, at a price not higher than the guidance price set by the PRC Government;
- (iii) where there is neither a government-prescribed price nor a government guidance price, the market price; and
- (iv) where none of the above is applicable, the price will be agreed between the relevant parties based on the cost plus a margin of up to 15% on cost.

Currently methanol products and related services covered by the Kingboard Product Sales and Services Agreement are not subject to any PRC Government prescribed or guidance prices, but we consider it prudent to provide pricing principles (i) and (ii) in that agreement.

The term of the Kingboard Product Sales and Services Agreement commenced on the date of the agreement and will expire on 31 December 2008 but may be renewed upon agreement provided that the requirements of the Hong Kong Listing Rules in relation to connected transactions are complied with. Hong Kong Kingboard (and/or its Associates) and we may, from time to time when the situation requires, enter into separate agreements which set out the specific products and scope of services, terms and conditions of selling products or providing services according to the principles laid down by the Kingboard Product Sales and Services Agreement.

There were no sales of products or provision of services between Hong Kong Kingboard or its Associates and us during the Track Record Period as CNOOC Jiantao Methanol Plant had not yet commenced operation before September 2006.

Future annual caps

Based on the projected production capacity of CNOOC Jiantao Methanol Plant and market prices, our business relationship with Hong Kong Kingboard, as well as our assumption that the PRC Government will not introduce prescribed or guidance prices in respect of methanol products and related services covered by the Kingboard Product Sales and Services Agreement in the near future, we expect that our annual revenue from transactions under the Kingboard Product Sales and Services Agreement will be RMB220,000,000, RMB730,000,000 and RMB730,000,000, respectively for the three years ending 31 December 2006, 2007 and 2008. For the avoidance of doubt, such cap figures account for 60% of the expected revenue generated by CNOOC Jiantao. As the methanol plant is expected to commence trial operation in September of 2006, the annual cap for 2006 only refers to the sale of products to Hong Kong Kingboard for the part of the year after commencement of operation, while the annual caps for 2007 and 2008 refer to the sale of products during the whole of the relevant years and therefore there is a relatively large increase from the 2006 figure to the 2007 figure.

CONTINUING CONNECTED TRANSACTIONS WITH OUR MINORITY PROMOTERS AND THEIR ASSOCIATES***14. Promoter Product Sales and Services Agreements***

As we sell our products and provide related services to each of Zhejiang AMP, Guangdong AMP, Shanghai AMP and Transammonia and their respective Associates, we entered into with each of them a product sales and related services framework agreement on 22 August 2006 (each, a “Promoter Product Sales and Services Agreement”), pursuant to which we agreed to sell products produced by us and provide related services such as transportation services to each such Minority Promoter and its Associates.

The transactions under each Promoter Product Sales and Services Agreement will be conducted on normal commercial terms and conditions which shall not be less favorable than those offered to third parties not being any of the Minority Promoters and priced in accordance with the following pricing principles:

- (i) price prescribed by the PRC Government;
- (ii) where there is no government-prescribed price but there is a government guidance price, at a price not higher than the guidance price set by the PRC Government;
- (iii) where there is neither a government-prescribed price nor a government guidance price, the market price; and
- (iv) where none of the above is applicable, the price will be agreed between the relevant parties based on the cost plus a margin of up to 15% on cost.

Currently, certain products produced by us such as urea products are subject to price controls imposed by the PRC Government. However, some of our other products including methanol products and related services covered by the Promoter Product Sales and Services Agreements are not subject to any PRC Government prescribed or guidance price. In any event, we consider it prudent to provide pricing principles (i) and (ii) in such agreements.

The term of each Promoter Product Sales and Services Agreement commenced on the date of the agreement and will expire on 31 December 2008 but may be renewed upon agreement provided that the requirements of the Hong Kong Listing Rules in relation to connected transactions are complied with. The Minority Promoters (and/or their respective Associates) and we may, from time to time when the situation requires, enter into separate agreements which set out the specific products or scope of services, terms and conditions of selling products or providing services according to the principles laid down by the Promoter Product Sales and Services Agreement.

CONNECTED TRANSACTIONS

Historical transaction figures

Our approximate sales of products and services to our Minority Promoters and their respective Associates during the Track Record Period (as if Tianye Chemical had been our subsidiary during the Track Record Period) is set out in the following table:

	For the year ended 31 December 2003 (in RMB)	For the year ended 31 December 2004 (in RMB)	For the year ended 31 December 2005 (in RMB)	For the three months ended 31 March 2006 (in RMB)
Zhejiang AMP and its Associates	130,042,000	247,177,000	395,854,000	102,853,000
Guangdong AMP and its Associates	77,241,000	179,690,000	307,017,000	76,545,000
Shanghai AMP and its Associates	21,205,000	63,186,000	86,080,000	20,752,000
Transammonia and its Associates	274,976,000	635,761,000	350,435,000	—

POTENTIAL CONNECTED TRANSACTION WITH HAINAN DEVELOPMENT

15. Hainan Basuo's put option

We and Hainan Development entered into an agreement in relation to Hainan Basuo on 28 February 2006 (the “Hainan Basuo Agreement”) pursuant to which, among other things, Hainan Development has been granted a put option to require us to acquire equity interests it holds in Hainan Basuo at a fair price within an agreed time period, provided that its equity interest in Hainan Basuo after such acquisition shall not be less than 5%. The Hainan Basuo Agreement did not set out the basis for determining the fair price, the length of the agreed time period, or any conditions that the put option may be acquired, transferred or terminated. As of the Latest Practicable Date, the put option has neither been exercised, acquired, transferred nor terminated, but the exercise, acquisition, transfer or termination of such put option after the Listing Date will constitute a connected transaction for us.

WAIVERS

Opinion of our Directors

Our Directors (including our independent non-executive Directors) are of the opinion that each of the transactions described in this section headed “Connected transactions” has been entered into, and will be carried out following the completion of the Global Offering, in the ordinary and usual course of our business, on an arm's length basis, and on normal commercial terms which are fair and reasonable and in the interests of our shareholders.

No waivers applied for certain categories of connected transactions

We have notified the Hong Kong Stock Exchange that we do not apply for waivers in relation to transactions in Categories 1, 2, 3, 4, 5, 8(c), 9(c), 10, 12 and 15.

For transactions in Category 1, the performance of CNOOC's obligations and our enjoyment of the rights under the Non-Competition Agreement from the Listing Date onwards will technically constitute our connected transactions. Our Directors (including the independent non-executive Directors) are of the view that such transactions are put in place for our benefit. Moreover, any claims that might arise would merely be performance of the Non-Competition Agreement entered into before the Listing Date. Accordingly, no general waiver from compliance with the requirements of Chapter 14A of the Hong Kong Listing Rules in respect of such transactions is required.

For transactions in Category 2, the indemnities given by CNOOC under the Indemnity Agreement from the Listing Date onwards will technically constitute our connected transactions. Nevertheless, our Directors (including the independent non-executive Directors) are of the view that such transactions are put in place for the benefit of us and of our independent shareholders. There are no monetary limits on such indemnities and we are not in a position to give any estimate of the amount of indemnities before any claim is made by us against CNOOC under the Indemnity Agreement. Therefore, no general waiver from compliance with the requirements of Chapter 14A of the Hong Kong Listing Rules in respect of such indemnities is required.

For each type of the continuing connected transactions under Categories 3, 4, 5, 8(c), 9(c) and 10, each of the percentage ratios (other than the profits ratio), where applicable, calculated by reference to Rule 14.07 of the Hong Kong Listing Rules on the basis of projections for the years 2006 to 2008 measured against benchmarks as of 31 December 2005, is less than 0.1%. Accordingly, these transactions qualified under Rule 14A.33(3) of the Hong Kong Listing Rules as de minimis transactions that are exempt from reporting, announcement and independent shareholders' approval requirements.

The guarantees under Category 12 constitute financial assistance that is exempted under Rule 14A.65(4) of the Hong Kong Listing Rules from reporting, announcement and independent shareholders' approval requirements applicable to continuing connected transactions under Chapter 14A of the Hong Kong Listing Rules as they are on normal commercial terms and no security is given by us.

As of the Latest Practicable Date, Hainan Basuo's put option in the Hainan Basuo Agreement has neither been exercised by Hainan Development nor acquired, transferred or terminated, and therefore we do not apply for any waiver from the Hong Kong Stock Exchange in relation to the connected transactions under Category 15. When the put option is exercised, acquired, transferred or terminated after the Listing Date, we will comply with Chapter 14 and 14A of the Hong Kong Listing Rules (including the seeking of independent shareholders' approval where appropriate and other requirements that a listed issuer would have to comply with after the Listing Date under Chapter 14A) and relevant PRC laws and regulations.

Waivers from compliance with announcement and/or independent shareholders' approval requirements

The continuing connected transactions under Categories 6, 7, 8(a), 8(b), 9(a), 9(b), 11(a), 11(b) and 13 would normally be subject to reporting, announcement and (where applicable) independent shareholders' approval requirements. Our Directors (including our independent non-executive Directors) consider that disclosure and approval of these transactions in full compliance with the Hong Kong Listing Rules would be impracticable and would add unnecessary administrative costs for us. In addition, we believe that it is in our interests to continue with these transactions after the Listing Date. Accordingly, in respect of such transactions, we have applied to the Hong Kong Stock Exchange for, and the Hong Kong Stock Exchange has granted, a waiver from compliance with the announcement and (where applicable) independent shareholders' approval requirements pursuant to Rule 14A.42(3) for a period expiring on 31 December 2008, subject to the annual value of such continuing connected transactions for each financial year not exceeding the relevant cap amounts which are summarized in the following table, except in respect of Category 9(b) for which the waiver will expire after one calendar year following the Listing Date and is subject to the value during that calendar year not

CONNECTED TRANSACTIONS

exceeding the cap amount set out in the following table. Our Directors (including our independent non-executive Directors) are of the opinion that the proposed caps for the relevant continuing connected transactions are fair and reasonable and in the interests of our shareholders as a whole.

Category	Basis of the cap in respect of the continuing connected transactions	Annual cap (RMB) for the year ending 31 December		
		2006	2007	2008
Continuing connected transactions with CNOOC and its Associates				
6	Annual expenditure for acquiring transportation services by us from COSL	13,000,000	45,000,000	48,000,000
7	Annual expenditure for purchases of natural gas from CNOOC China Limited	510,300,000	657,090,000	1,046,640,000
8(a)	Annual expenditure for acquiring services and supplies by us from the CNOOC Group	278,520,000	102,300,000	74,800,000
8(b)	Annual revenue for providing services and supplies by us to the CNOOC Group	4,400,000	4,400,000	3,300,000
9(a)	Maximum daily outstanding balance after listing of loans (including accrued interest) granted by CNOOC Finance to us but excluding entrustment loans referred to in Category 9(c2)	400,000,000	500,000,000	600,000,000
9(b)	Maximum daily outstanding balance after listing of deposits (including accrued interest) placed by us with CNOOC Finance	300,000,000 (This cap amount applies for a period of one calendar year commencing on the Listing Date.)		Not applicable
Continuing connected transactions with Hainan CNOOC Transportation				
11(a)	Annual expenditure for acquiring transportation services from Hainan CNOOC Transportation by us	5,300,000	5,700,000	6,000,000
11(b)	Annual revenue for providing loading services by us to Hainan CNOOC Transportation	19,000,000	20,000,000	21,000,000
Continuing connected transactions with Hong Kong Kingboard and its Associates				
13	Annual revenue for selling products and providing related services by us to Hong Kong Kingboard and/or its Associates	220,000,000	730,000,000	730,000,000

Where the actual annual amount of any type of the above continuing connected transactions may exceed the relevant annual cap, we will seek independent shareholders' approval to revise the annual cap in accordance with the applicable requirements under Chapter 14A of the Hong Kong Listing Rules.

Waiver for our Minority Promoters and their Associates being treated as connected persons

Pursuant to Rules 1.01, 14A.11(3) and 19A.04 of the Hong Kong Listing Rules, our Minority Promoters and their Associates would be our connected persons upon the listing of our H Shares on the Hong Kong Stock Exchange. Accordingly, the transactions with our Minority Promoters and their

Associates under Category 14 would be considered to be continuing connected transactions that are subject to the reporting, announcement and independent shareholders' approval requirements under Chapter 14A of the Hong Kong Listing Rules, unless otherwise exempted under Rules 14A.33 and 14A.34.

Our Directors consider that our Minority Promoters and their Associates should not be treated as our connected persons for the following reasons:

1. Insignificant control or influence over us: Our Minority Promoters will have insignificant control and influence over our Company given the following circumstances:
 - (a) Small stake in our Company: Each Minority Promoter currently holds approximately 0.83% of our issued share capital. Such shareholding will be further decreased to approximately 0.57% immediately following the completion of the Global Offering if the Over-allotment Option is not exercised and, as the case may be, to approximately 0.54% immediately following the full exercise of the Over-allotment Option. Even if all our Minority Promoters' shareholdings are aggregated, their shareholding in our issued share capital is only approximately 3.33% which will be reduced, following the completion of the Global Offering, to approximately 2.27% if the Over-allotment Option is not exercised or to approximately 2.17% if the Over-allotment Option is exercised in full.
 - (b) Independence: As far as we are currently aware, our Minority Promoters are independent of each other and also independent of our Controlling Shareholder, CNOOC.
 - (c) No influence on the board or supervisory committee of our Company and our subsidiaries: We currently have eight Directors, four of whom were in fact (but not by right) proposed by CNOOC while the other four are independent non-executive Directors. Further, no director and no supervisor of any of our subsidiaries (including CNOOC Jiantao) is in fact proposed by a Minority Promoter. Therefore, we believe that none of our Minority Promoters is, either individually or in collaboration with each other, in a position to influence or control the board or the supervisory committee of our Company or our subsidiaries.
 - (d) No special rights as shareholders: Our Minority Promoters do not have special rights as our shareholders (other than those enjoyed by all shareholders), either contractual or statutory.
2. No level playing field: If we were not a PRC issuer, the Minority Promoters and their Associates would not have been regarded as our connected persons because under the Hong Kong Listing Rules, a shareholder of a non-PRC company which individually has less than 10% of the voting shares of that company would not be treated as a connected person. In our case, our Minority Promoters and their Associates fall under the definition of connected persons under the Hong Kong Listing Rules not because of their influence as substantial shareholders but merely due to the fact that the Hong Kong Listing Rules define each promoter of a PRC issuer and its Associates as connected persons, regardless of the promoter's shareholding percentage in the PRC issuer.

For the reasons set out above, we have applied to the Hong Kong Stock Exchange for, and the Hong Kong Stock Exchange has granted, a waiver under Rule 14A.42 of the Hong Kong Listing

Rules to exempt our Minority Promoters and their Associates from being regarded as connected persons for the purpose of the Hong Kong Listing Rules in relation to all transactions contemplated in Category 14, and therefore, exempt all such transactions from all the requirements of Chapter 14A of the Hong Kong Listing Rules regarding connected transactions, subject to the condition that none of the Minority Promoters will have any representation on the board or supervisory committee of our Company or our subsidiaries (which include, for the purpose of such waiver application, CNOOC Jiantao).

In connection with the waiver application, each Minority Promoter has given an undertaking to our Company that it will not exercise its rights to appoint any representatives on the board or the supervisory committee of our Company or any of our subsidiaries and will not exert any influence over our Company and our subsidiaries through its role as Promoter.

Confirmation from the Joint Sponsors

As set out above, each of the Natural Gas Sale and Purchase Agreements has a term of 20 years, exceeding the three year term set out under Rule 14A.35(1) of the Hong Kong Listing Rules. The Directors and the Joint Sponsors have confirmed that they consider that a term of 20 years for each of the Natural Gas Sale and Purchase Agreements is appropriate because:

- (a) the 20 year term was determined based on the estimated reserves and production profile of CNOOC China Limited's offshore gasfields, in accordance with market practice for offshore gasfields;
- (b) the long term of the Natural Gas Sale and Purchase Agreements conforms with the normal business practice of CNOOC Limited in supplying natural gas from its gasfields of entering into supply contracts of 15 to 20 year terms in order for CNOOC Limited to secure return on its investment from exploration of natural gas;
- (c) through such long-term agreements, we have been able to secure a stable source of natural gas, a key raw material for our operation, thereby avoiding unnecessary disruption to our operations; and
- (d) as the composition of natural gas varies between source gasfields and the design of our production facilities has taken into account and, in future, will take in to account, the gas source, we are prevented from switching from one gas source to another without first reconfiguring our production facilities; and our relevant production complexes have been or will be designed to use natural gas from specific gasfields operated by CNOOC China Limited, and therefore long-term agreements are essential to justify our significant investment in production facilities.

The Joint Sponsors consider that it is normal business practice for offshore natural gas sale and purchase contracts of this type to be of such duration.

The Joint Sponsors are of the view that (i) the continuing connected transactions described above for which waivers are sought have been entered into in the ordinary course of business of our Company on normal commercial terms and are fair and reasonable and in the interests of our shareholders as a whole and (ii) the proposed annual caps for the relevant continuing connected transactions for which waivers are sought are fair and reasonable and in the interests of our shareholders as a whole.