

## OVERVIEW

Historically, CNOOC and its subsidiaries were responsible for the exploration and production of oil and natural gas offshore China as well as related oilfield services. In October 1999, CNOOC Limited was created to undertake the exploration and production of oil and natural gas offshore China and was listed on the Stock Exchange and the New York Stock Exchange in February 2001.

Prior to December 2001, CNOOC provided drilling, well and geophysical services primarily through five PRC wholly owned subsidiaries and offered marine support and transportation services through two other wholly owned subsidiaries. On December 25, 2001, CNOOC incorporated us as the operating company for the business operations of the five subsidiaries that perform drilling, well and geophysical services and combined the two marine support and transportation subsidiaries into one entity on December 29, 2001. In preparation for this Global Offering, we further consolidated our drilling, well and geophysical services operations and undertook a statutory merger with the marine support and transportation subsidiary. After this Reorganization, we became the sole existing company within the CNOOC group to undertake these oilfield services. On September 26, 2002, with the approval of the PRC Government, we were restructured into a joint stock limited liability company in China.

In connection with our Reorganization, we entered into and novated a number of agreements and arrangements with CNOOC. Upon the listing of our H Shares on the Stock Exchange, the following transactions will constitute connected transactions under the Listing Rules.

## CONNECTED TRANSACTIONS AND WAIVERS

We have engaged, and expect to continue after our Global Offering to engage, in the following connected transactions. They will constitute connected transactions under the Listing Rules after our H Shares are listed on the Stock Exchange for so long as CNOOC and/or CNOOC Limited remain our connected persons within the meaning of the Listing Rules. The Stock Exchange has indicated that it will grant a conditional waiver from strict compliance with the relevant connected transactions requirements as set out in the Listing Rules for these transactions.

### *Our Provision of Offshore Oilfield Services to CNOOC and Its Associates*

Since the establishment of CNOOC, we, including our predecessors, have provided oilfield services, including labor services, to CNOOC and its associates, including CNOOC Limited, in connection with their offshore oil and gas exploration, development and production activities. Our predecessors provided these oilfield services on the basis of agreements they entered into with CNOOC and its associates. By virtue of our Reorganization and a novation, we have assumed the rights and obligations of our predecessors under these agreements with CNOOC and its associates, including CNOOC Limited.

The prices we charged to CNOOC and its associates, including CNOOC Limited, primarily reflected our negotiations with CNOOC and its associates under prevailing local market conditions, including considerations such as volume of sales, length of contracts, overall customer relationship and other market factors. Because CNOOC Limited is the dominant petroleum company in our principal market of offshore China and has been the largest purchaser of our offshore oilfield services, our prices charged to CNOOC Limited did not reflect the prices we typically charged independent third parties. We expect that, after our Global Offering, we will offer our offshore oilfield services to CNOOC Limited at

prices that are based on arm's length negotiations and reflect considerations such as volume of sales, length of contracts, package of services, overall customer relationship and other market factors. Any discounts that we offer to CNOOC Limited are also available to other customers whose volume of business and contract terms are similar to those of CNOOC Limited.

For the three years ended December 31, 2001 and the six-month period ended June 30, 2002, we earned gross revenue of approximately Rmb 906.7 million, Rmb 1,219.2 million, Rmb 1,449.1 million and Rmb 840.7 million, respectively, for offshore oilfield services provided to CNOOC and its associates, of which Rmb 811.4 million, Rmb 1,111.5 million, Rmb 1,293.6 million and Rmb 774.6 million, respectively, were derived from our services provided to CNOOC Limited.

In addition, by virtue of an equity transfer agreement and as a part of our Reorganization, CNOOC transferred to us its 60% equity interest in China Nanhai-Magcobar Mud Corporation Limited ("Magcobar"). This joint venture company has provided, and will continue after our Global Offering to provide, well services to CNOOC and its associates, including CNOOC Limited. For the three years ended December 31, 2001 and the six-month period ended June 30, 2002, Magcobar received approximately Rmb 69.9 million, Rmb 56.5 million, Rmb 76.4 million and Rmb 54.6 million, respectively, for well services provided to CNOOC and its associates. During these periods, Magcobar provided its services to CNOOC and its associates, including CNOOC Limited, at prevailing local market prices. We expect that Magcobar will continue to provide its services to CNOOC and its associates on this same basis in the future.

### *CNOOC Provision of Materials, Utilities, Labor and Ancillary Support Services to Us*

In the past, CNOOC and its associates provided us and our majority-owned joint venture, Magcobar, with various materials, utilities, labor and other ancillary services. In order to secure continued provision by CNOOC and its associates of such materials, utilities, labor and other ancillary support services to us after our Reorganization, we entered into a comprehensive service agreement with CNOOC on September 27, 2002. Under the comprehensive service agreement and various specific service agreements attached and incorporated by reference to the comprehensive service agreement, CNOOC and its associates will provide us with such materials, utilities, labor and ancillary services, including:

- warehousing and storage;
- supply and transportation of materials;
- communications services;
- wharf services (including loading, unloading, mooring, unmooring, cleaning and utility services);
- construction services (including road pavement and construction of wharf terminals, improvements and factories);
- medical care, child care and social welfare services;
- technical training (including vocational training, safety training and on-the-job training);
- accommodation and personnel transportation services;
- offshore facility monitoring, maintenance and repair services;

- catering services;
- use of property (including sites, equipment and facilities);
- insurance arrangements; and
- labor services.

CNOOC and its associates historically have provided us and Magcobar with the above services at prices determined as follows:

- (i) at State-prescribed prices; or
- (ii) where there was no State-prescribed price, market prices, including the local or national market prices or the prices, at which CNOOC and its associates previously provided the relevant materials, utilities, labor and ancillary services, transportation, repair and maintenance, and management services to independent third parties; or
- (iii) when neither (i) nor (ii) was applicable, the cost to CNOOC and its associates of providing the relevant materials, utilities, labor and ancillary services, transportation, repair and maintenance, and management services, including the cost of sourcing or purchasing from independent third parties, plus a margin of not more than 5%, before any applicable taxes.

Pursuant to the comprehensive services agreement of September 27, 2002, CNOOC and certain CNOOC associates have undertaken to provide us with these services at certain stipulated prices. These prices are based on our arm's length negotiation with CNOOC and its associates. We believe these prices are similar to the prices that CNOOC and its associates currently charge other parties and that they are fair to us and to our independent shareholders. The comprehensive services agreement is for a term of one year, but will be automatically extended for additional one-year periods unless we cancel it by providing notice to CNOOC 60 days before the relevant expiration date.

In addition to the above service categories, we use a majority-owned Nigerian subsidiary of CNOOC, Haiyang Petroservices Limited ("Haiyang"), to market our drilling rigs and enter into drilling contracts on our behalf offshore Nigeria. Nigerian government policies require us to use a locally incorporated company, such as Haiyang, to execute contracts in that region. Pursuant to a non-exclusive logistic services agreement, Haiyang has undertaken to provide us with logistic services to support our drilling operations offshore Nigeria. These services include regulatory compliance, rig maintenance and inspection, accommodation and catering for our personnel, first-aid medical service on board our rig, travelling documentation and arrangements, work permits, communication, onshore support and other services. We have agreed to pay Haiyang a commission and a management fee as well as to reimburse certain out-of-pocket expenses. Our aggregate payments under the agreement will not exceed 20% of the operating revenue derived from our drilling contracts arranged by or through Haiyang. The terms of this agreement were based on local market conditions and negotiated on an arm's length basis. We believe the pricing under the agreement is fair to us and our independent Shareholders. We and Haiyang may each terminate the non-exclusive logistic services agreement by giving 30 days prior written notice to the other.

For the three years ended December 31, 2001 and the six-month period ended June 30, 2002, we paid, in aggregate, approximately Rmb 135.5 million, Rmb 142.3 million, Rmb 196.3 million and Rmb 96.1 million, respectively, for materials, utilities, labor and other ancillary support services provided by CNOOC and its associates. These historical amounts primarily consist of services that are now included in the comprehensive services agreement mentioned above.

In addition, for the three years ended December 31, 2001 and the six-month period ended June 30, 2002, Magcobar paid, in aggregate, approximately Rmb 3.7 million, Rmb 3.9 million, Rmb 4.1 million and Rmb 2.1 million, respectively, for materials, utilities, labor and other ancillary support services provided by CNOOC and its associates.

### *Lease and Property Management Agreements with CNOOC and its Associates*

In the past, we and Magcobar have leased certain premises used in our respective business operations from CNOOC and its associates. In addition to these leased premises, CNOOC and its associates have provided our company with certain other office and production premises free of charge because we were a wholly owned subsidiary of CNOOC. In order to secure continued provision by CNOOC and its associates of these office and production spaces, we have entered into new lease and property management agreements with the relevant parties.

The existing leases with CNOOC and its associates include (i) a lease of January 14, 2002 entered into between a CNOOC associate and us for a gross floor area of 721 square meters for office and production use in Shenzhen, Guangdong Province for an aggregate annual rental of approximately Rmb 700,812 (including an aggregate annual water, electricity and service fee of Rmb 302,820); and (ii) two leases entered into between CNOOC associates and Magcobar for a gross floor area of 510 square meters for office and production use in the Tianjin Municipality for an aggregate annual rental of approximately Rmb 221,760. The lease between the CNOOC associate and us is for a term of one year commencing on January 15, 2002, and may be extended by the parties. If this lease arrangement is extended, the annual fees will be renegotiated on an arm's length basis. The first lease dated March 15, 2002 between the CNOOC associate and Magcobar is for a term of three years commencing from March 1, 2002, while the second lease dated January 20, 2002 is for a term of one year commencing from January 15, 2002, and may be extended by the parties. If the second lease between the CNOOC associate and Magcobar is extended, the annual fee will be renegotiated on an arm's length basis.

On September 27, 2002, we entered into three new lease agreements with CNOOC associates for (i) a gross floor area of 33,305.48 square meters for office and production use in the Yanjiao Development Zone, Hebei Province for an aggregate annual rental of approximately Rmb 5.2 million payable on a quarterly basis, (ii) a gross floor area of 21,498.72 square meters for office and production use in Zhanjiang, Guangdong Province for an aggregate annual rental of approximately Rmb 0.6 million payable on a monthly basis, and (iii) a gross floor area of 21,918.00 square meters for office and production use in Tanggu, Tianjin Municipality for an aggregate annual rental of approximately Rmb 1.8 million payable on a quarterly basis. These leases are each for a duration of one year, renewable continuously at our option for another one-year term upon our written notice to the landlords in the case of (i) and (ii) above, 60 days prior to their expiration and, in the case of (iii) above, three months prior to its expiration. If we decide to extend the terms of the leases, the lease agreements require the annual rental payments to be renegotiated on an arm's length basis. We also have a unilateral right of termination upon 60 days prior notice to our landlords. In addition to rental payments, we are also obligated under property management agreements with some of our landlords or their associates to pay them various fees relating to property management, utility, security, heating and air conditioning, forestation and other services. These property management agreements typically have a one-year duration, but are renewable for additional one-year periods. If the management agreements are renewed, the annual fees will be renegotiated on an arm's length basis. Sallmanns (Far East) Limited, an independent valuer, has confirmed that the rental value of each of the existing and new leases either reflects or is lower than the fair market rates for these premises.

For the three years ended December 31, 2001 and the six-month period ended June 30, 2002, we and Magcobar paid, in aggregate, approximately Rmb 3.0 million, Rmb 4.1 million, Rmb 5.9 million and Rmb 3.4 million, respectively, for premises leased to us by CNOOC and its associates.

### *Financial Services by CNOOC Associate*

We expect that we will from time to time utilize the financial services available from CNOOC Finance Corporation Limited, a majority-owned non-bank finance subsidiary of our controlling Shareholder, CNOOC. The financial services provided by the finance company will include our cash deposits and settlement services for transactions concluded between us and our customers. For potential risks involved in, and additional information relating to, such finance services, see the section headed “Risk Factors—We will continue to engage in connected transactions with CNOOC and its associates, including CNOOC Limited and CNOOC Finance Corporation Limited” and the section headed “Corporate Structure—Relationship with CNOOC—CNOOC Finance Corporation Limited.”

### *Waiver from the Stock Exchange*

The transactions described above will constitute connected transactions for us under the Listing Rules once our H Shares are listed on the Stock Exchange. Pursuant to the Listing Rules, each of these transactions would normally require full disclosure and prior approval by independent Shareholders subject to the nature and the value of the transactions. Given that these transactions will be conducted in the ordinary course of business and on a regular basis, our Directors believe that disclosure and approval of these transactions in full compliance with the Listing Rules would be impracticable and add additional administrative costs. Accordingly, our Directors have requested the Stock Exchange to grant a waiver from full compliance with the Listing Rules in respect of these transactions. The Stock Exchange has indicated that a conditional waiver from strict compliance with the relevant connected transaction requirements of the Listing Rules in respect of these transactions will be granted for a period of three financial years expiring on December 31, 2004 and subject to the following conditions:

- (i) that the transactions be on an arm’s length basis, that is:
  - entered into by us in the ordinary and usual course of our business; and either
  - on normal commercial terms; or
  - where there is no available comparison, on terms no less favorable than those available from or to independent third parties; and
  - in accordance with the relevant agreements governing such transactions, on terms that are fair and reasonable to our independent Shareholders and in the interests of our Shareholders as a whole; and
  - if applicable, with the annual aggregate value of each category of connected transactions not exceeding the relevant annual caps.

## CONNECTED TRANSACTIONS

- (ii) that we disclose, in our annual report and accounts for the relevant year, the following details of the transactions in each year as required by Rule 14.25(1) of the Listing Rules:
- the date or period of the transactions;
  - the parties thereto and a description of their connected relationship;
  - a brief description of the transactions and the purpose of the transactions;
  - the total consideration and the terms; and
  - the nature and extent of the interest of the connected person in the transactions;
- (iii) that our independent non-executive Directors shall review annually the transactions and confirm, in our annual report and accounts of the year in question, that such transactions have been conducted in the manner stated in paragraph (i) above and in compliance with the caps in paragraph (vi) below;
- (iv) that our auditors shall review annually the transactions and confirm to our Directors in writing (with a copy to the Stock Exchange at least 10 business days prior to the bulk printing of our annual report) whether the transactions:
- have received the approval of our Board of Directors with any Director that has a conflict of interest abstaining;
  - have been entered into in accordance with the terms of the agreements governing the transactions or, where there is no agreement, on terms that are not less favorable than terms available from or to independent third parties; and
  - have not exceeded the caps specified in paragraph (vi) below;
- (v) that for the purpose of the above review and reporting on the transactions by our auditors, CNOOC shall provide to the Stock Exchange an undertaking that, for so long as our Shares are listed on the Stock Exchange, it will provide our auditors with access to its accounting records and the accounting records of its associates;
- (vi) the maximum aggregate annual value for each category of connected transactions not exceed the limits set out below:

**Transaction**

Our provision of offshore oilfield services to CNOOC and its associates (including CNOOC Limited)

Provision of offshore oilfield services by Magobar to CNOOC and its associates (including CNOOC Limited)

**Proposed annual limit**

In respect of each of the three financial years ending December 31, 2002, 2003 and 2004, Rmb 2.10 billion, Rmb 2.94 billion and Rmb 4.12 billion, respectively.

In respect of each of the three financial years ending December 31, 2002, 2003 and 2004, Rmb 120 million, Rmb 144 million and Rmb 173 million, respectively.

## CONNECTED TRANSACTIONS

### Transaction

Provision of materials, utilities, labor and other ancillary support services by CNOOC and its associates to us

Provision of materials, utilities, labor and other ancillary support services by CNOOC and its associates to Magcobar

Provision of office and production premises by CNOOC and its associates to us (including Magcobar)

Provision of depositary and transaction settlement services by CNOOC Finance Corporation Limited to us in respect of our total daily outstanding deposits plus interest income

### Proposed annual limit

In respect of each of the three financial years ending December 31, 2002, 2003 and 2004, Rmb 253 million, Rmb 317 million and Rmb 382 million, respectively.

In respect of each of the three financial years ending December 31, 2002, 2003 and 2004, Rmb 6 million, Rmb 8 million and Rmb 10 million, respectively.

In respect of each of the three financial years ending December 31, 2002, 2003 and 2004, Rmb 15 million, Rmb 20 million and Rmb 26 million, respectively.

10% of our audited consolidated total turnover for the immediately preceding fiscal year.

We have undertaken to the Stock Exchange that if any material term of our agreements or arrangements referred to above are altered (unless as provided for under the terms of these agreements or arrangements) or if we enter into any new agreement or arrangement with any connected person (within the meaning of the Listing Rules) in the future or if the limits referred to above will be exceeded, we will comply with the provisions of Chapter 14 of the Listing Rules dealing with connected transactions unless we apply for and obtain a separate waiver from the Stock Exchange.

Based on the documents, information and historical figures provided by us and in reliance upon the representations and confirmations made by us, our Directors and our Supervisors that the connected transactions described in this section above are: (i) on normal commercial terms; (ii) in the ordinary course of our business and the relevant parties concerned; and (iii) on terms that are fair and reasonable as far as our Shareholders as a whole are concerned, the Joint Sponsors and the Directors (including the Independent non-executive Directors) have confirmed that, in their view, the connected transactions described in this section are in the ordinary course of our business and are fair and reasonable as far as our Shareholders as a whole are concerned.

It should be noted that: (i) the Joint Sponsors have, in reaching their above opinion, assumed and relied very significantly, without conducting any independent verification, upon the accuracy and completeness of the documentation, information, historical figures, representations and confirmations provided to them and reviewed by them for the purposes of expressing the view stated above; (ii) no independent valuations or appraisals, or evaluation or investigation of our assets and liabilities have been performed by the Joint Sponsors nor have the Joint Sponsors been furnished with any such valuations, appraisals, evaluation or investigation; and (iii) the view of the Joint Sponsors referred to above represents their view as at the date of this Prospectus and such view is necessarily based on, and assumes no change in, economic, market and other conditions in effect on the date of this Prospectus, and the information made available to them for the purposes hereof. Changes in economic, market or other conditions subsequent to the date hereof could impact the views of the Joint Sponsors stated above but the Joint Sponsors assume no obligation to update their views.

## ADDITIONAL TRANSACTIONS

In connection with our Reorganization and the Global Offering, we have entered or will enter into the following additional agreements with CNOOC. Our performance of these agreements will technically be considered connected transactions after the listing of our H Shares.

### *Reorganization Agreement*

In connection with the Reorganization, we entered into the Reorganization Agreement with CNOOC, which contains indemnities given by CNOOC and us. Pursuant to such indemnities, CNOOC has agreed to indemnify us in relation to the period before completion of the Reorganization and we have agreed to indemnify CNOOC against the breach of any provision of the Reorganization Agreement on our part.

Pursuant to the Reorganization Agreement, CNOOC has agreed to convert an aggregate of Rmb 600 million of our current liabilities due to CNOOC to long-term liabilities without interest. This amount consisted largely of our distributions declared but not yet paid. We have agreed with CNOOC to pay this amount in three annual installments of Rmb 200 million each commencing May 1, 2005.

### *CNOOC Undertakings*

CNOOC has provided various undertakings to us. For further details of these and other undertakings, see “Corporate Structure—Relationship with CNOOC—CNOOC’s Undertakings.”

### *Trademark License Agreement*

CNOOC is the registered owner of the “CNOOC” trademark. Under a non-exclusive license agreement dated September 27, 2002, we have the right to use the trademark for a term of ten years for a one-time payment of Rmb 1,000. The registration of the trademark will expire on December 6, 2008. CNOOC has undertaken that so long as it is our controlling Shareholder (as defined in the Listing Rules), it will renew the registration of the trademark to enable us to continue to use it without any additional payment.

### *Sino-Japanese Joint Venture Management Agreement*

We have entered into a management agreement with CNOOC with respect to its Sino-Japanese equity joint venture, China Bohai-Japan Offshore Drilling Company Limited. For further details of this arrangement, see “Corporate Structure—Relationship with CNOOC—CNOOC’s Undertakings.” This management agreement is subject to the consent of the Japanese partners and CNOOC has undertaken to us to obtain such consent within 60 days of the signing of the management agreement.