

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**  
Washington, D.C. 20549

**FORM 20-F**

(Mark One)

- REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR (g) OF THE SECURITIES EXCHANGE ACT OF 1934
- OR
- ANNUAL REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934
- FOR THE FISCAL YEAR ENDED DECEMBER 31, 2008
- OR
- TRANSITION REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934
- FOR THE TRANSITION PERIOD FROM \_\_\_\_\_ TO \_\_\_\_\_
- OR
- SHELL COMPANY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934  
DATE OF EVENT REQUIRING THIS SHELL COMPANY REPORT  
FOR THE TRANSACTION PERIOD FROM \_\_\_\_\_ TO \_\_\_\_\_

COMMISSION FILE NUMBER 1-15138

中国石油化工股份有限公司

**CHINA PETROLEUM & CHEMICAL CORPORATION**  
(Exact name of Registrant as specified in its charter)

**The People's Republic of China**  
(Jurisdiction of incorporation or organization)

**22 Chaoyangmen North Street  
Chaoyang District, Beijing, 100728  
The People's Republic of China**  
(Address of principal executive offices)

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(Name, Telephone, Email and/or Facsimile number and Address of Company Contact Person)

Securities registered or to be registered pursuant to Section 12 (b) of the Act.

<b><u>Title of Each Class</u></b>	<b><u>Name of Each Exchange On Which Registered</u></b>
American Depositary Shares, each representing 100 H Shares of par value RMB 1.00 per share	New York Stock Exchange, Inc.
H Shares of par value RMB 1.00 per share	New York Stock Exchange, Inc.*

\* Not for trading, but only in connection with the registration of American Depositary Shares.  
Securities registered or to be registered pursuant to Section 12 (g) of the Act.

**None**  
(Title of Class)

Securities for which there is a reporting obligation pursuant to Section 15 (d) of the Act.

**None**  
(Title of Class)

Indicate the number of outstanding shares of each of the issuer's classes of capital or common stock as of the close of the period covered by the annual report.

Shares with selling restriction, par value RMB 1.00 per share	57,087,800,493
H Shares, par value RMB 1.00 per share	16,780,488,000
A Shares, par value RMB 1.00 per share	12,834,150,507

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes  No

If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934.

Yes  No

Note - Checking the box above will not relieve any registrant required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 from their obligations under those Sections.

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15 (d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer  Accelerated filer  Non-accelerated filer

Indicate by check mark which basis of accounting the registrant has used to prepare the financial statements included in this filing:

U.S. GAAP  International Financial Reporting Standards  Other   
as issued by the International Accounting Standards Board

If "Other" has been checked in response to the previous question, indicate by check mark which financial statement item the registrant has elected to follow.

Item 17  Item 18

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

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## CERTAIN TERMS AND CONVENTIONS

### Definitions

Unless the context otherwise requires, references in this annual report to:

- "Sinopec Corp.", "we", "our" and "us" are to China Petroleum & Chemical Corporation, a PRC joint stock limited company, and its subsidiaries;
- "Sinopec Group Company" are to our controlling shareholder, China Petrochemical Corporation, a PRC limited liability company;
- "Sinopec Group" are to the Sinopec Group Company and its subsidiaries other than Sinopec Corp. and its subsidiaries;
- "China" or the "PRC" are to the People's Republic of China, excluding for purposes of this annual report Hong Kong, Macau and Taiwan;
- "provinces" are to provinces and to provincial-level autonomous regions and municipalities in China which are directly under the supervision of the central PRC government;
- "RMB" are to Renminbi, the currency of the PRC;
- "HK\$" are to Hong Kong dollar, the currency of the Hong Kong Special Administrative Region of the PRC; and
- "US\$" are to US dollars, the currency of the United States of America.

### Conversion Conventions

Conversions of crude oil from tonnes to barrels are made at a rate of one tonne to 7.35 barrels for crude oil we purchase from external sources and one tonne to 7.1 barrels for crude oil we produce, representing the American Petroleum Institute ("API") gravity of the respective source of crude oil. Conversions of natural gas from cubic meters to cubic feet are made at a rate of one cubic meter to 35.31 cubic feet.

### Glossary of Technical Terms

Unless otherwise indicated in the context, references to:

- "billion" are to a thousand million.
- "BOE" are to barrels-of-oil equivalent; natural gas is converted at a ratio of 6,000 cubic feet of natural gas to one BOE.
- "primary distillation capacity" are to the crude oil throughput capacity of a refinery's crude oil distillation units, calculated by estimating the number of days in a year that such crude oil distillation units are expected to operate, excluding downtime for regular maintenance, and multiplying that number by the amount equal to the units' optimal daily crude oil throughput.
- "rated capacity" are to the output capacity of a given production unit or, where appropriate, the throughput capacity, calculated by estimating the number of days in a year that such production unit is expected to operate, excluding downtime for regular maintenance, and multiplying that number by an amount equal to the unit's optimal daily output or throughput, as the case may be.

## CURRENCIES AND EXCHANGE RATES

We publish our financial statements in Renminbi. Unless otherwise indicated, all translations from Renminbi to US dollars have been made at a rate of RMB 6.8225 to US\$1.00, the noon buying rate as certified for customs purposes by the Federal Reserve Bank of New York on December 31, 2008. We do not represent that Renminbi or US dollar amounts could be converted into US dollars or Renminbi, as the case may be, at any particular rate, the rates below or at all. On May 15, 2009, the noon buying rate was RMB 6.8225 to US\$1.00.

The following table sets forth noon buying rate for US dollars in New York City for cable transfers in Renminbi as certified for customs purposes by the Federal Reserve Bank of New York for the periods indicated:

	<b>Noon Buying Rate</b>			
	<b>End</b>	<b>Average<sup>(1)</sup></b>	<b>High</b>	<b>Low</b>
	<b>(RMB per US\$1.00)</b>			
2004	8.2765	8.2767	8.2774	8.2764
2005	8.0702	8.1826	8.2765	8.0702
2006	7.8041	7.9723	8.0702	7.9723
2007	7.2946	7.5806	7.8127	7.2946
2008	6.8225	6.9193	7.2946	6.7800
November 2008	6.8254	6.8281	6.8373	6.8220
December 2008	6.8225	6.8539	6.8842	6.8225
January 2009	6.8392	6.8360	6.8392	6.8225
February 2009	6.8395	6.8363	6.8470	6.8241
March 2009	6.8329	6.8360	6.8438	6.8240
April 2009	6.8180	6.8304	6.8361	6.8180
May 2009 (up to May 15, 2009)	6.8225	6.8210	6.8248	6.8176

(1) Annual averages are determined by averaging the rates on the last business day of each month during the relevant period. Monthly averages are calculated using the average of the daily rates during the relevant period.

## FORWARD-LOOKING STATEMENTS

This annual report includes "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. All statements, other than statements of historical facts, included in this annual report that address activities, events or developments which we expect or anticipate will or may occur in the future are hereby identified as forward-looking statements for the purpose of the safe harbor provided by Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. The words such as believe, intend, expect, anticipate, project, estimate, predict, plan and similar expressions are also intended to identify forward-looking statements. These forward-looking statements address, among others, such issues as:

- amount and nature of future exploration and development,
- future prices of and demand for our products,
- future earnings and cash flow,
- development projects and drilling prospects,
- future plans and capital expenditures,
- estimates of proved oil and gas reserves,
- exploration prospects and reserves potential,
- expansion and other development trends of the petroleum and petrochemical industry,
- production forecasts of oil and gas,
- expected production or processing capacities, including expected rated capacities and primary distillation capacities, of units or facilities not yet in operation,
- expansion and growth of our business and operations, and
- our prospective operational and financial information.

These statements are based on assumptions and analyses made by us in light of our experience and our perception of historical trends, current conditions and expected future developments, as well as other factors we believe are appropriate in particular circumstances. However, whether actual results and developments will meet our expectations and predictions depends on a number of risks and uncertainties which could cause actual results to differ materially from our expectations, including the risks set forth in "Item 3. Key Information — Risk Factors" and the following:

- fluctuations in crude oil prices,
- fluctuations in prices of our products,
- failures or delays in achieving production from development projects,
- potential acquisitions and other business opportunities,
- general economic, market and business conditions, and
- other risks and factors beyond our control.

Consequently, all of the forward-looking statements made in this annual report are qualified by these cautionary statements and readers are cautioned not to place undue reliance on these forward-looking statements. These forward-looking statements should be considered in light of the various important factors set forth above and elsewhere in this Form 20-F. In addition, we cannot assure you that the actual results or developments anticipated by us will be realized or, even if substantially realized, that they will have the expected effect on us or our business or operations.

**ITEM 1. IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISORS**

Not applicable.

**ITEM 2. OFFER STATISTICS AND EXPECTED TIMETABLE**

Not applicable.

**ITEM 3. KEY INFORMATION**

**A. SELECTED FINANCIAL DATA**

The selected consolidated income statement data and consolidated cash flow data for the years ended December 31, 2006, 2007 and 2008, and the selected consolidated balance sheet data as of December 31, 2007, and 2008 have been derived from, and should be read in conjunction with, the audited consolidated financial statements included elsewhere in this annual report. The selected consolidated income statement data and consolidated cash flow data for the years ended December 31, 2004 and 2005 and the selected consolidated balance sheet data as of December 31, 2004, 2005 and 2006 are derived from our audited consolidated financial statements which are not included elsewhere in this annual report and the financial statements of the acquired businesses described below.

We acquired from Sinopec Group Company the operations of Sinopec Group Tianjin Petrochemical Company, Sinopec Group Luoyang Petrochemical General Plant, Zhongyuan Petrochemical Company Limited, Sinopec Group Guangzhou Petrochemical General Plant and certain catalyst plants (collectively, Petrochemical and Catalyst Assets) in 2004, the equity interests in Sinopec Hainan Refining and Chemical Company Limited (Sinopec Hainan) and certain oil and gas production companies (Oil Production Plants) in 2006, and the equity interests in Zhanjiang Dongxing Petroleum Company Limited, Sinopec Hangzhou Oil Refinery Plant, Yangzhou Petrochemical Plant, Jiangsu Taizhou Petrochemical Plant and Sinopec Qingjiang Petrochemical Company Limited (collectively, Refinery Plants) in 2007. As we and these companies are under the common control of Sinopec Group Company, our acquisitions are reflected in our consolidated financial statements as combination of entities under common control in a manner similar to a pooling-of-interests. Accordingly, the acquired assets and related liabilities have been accounted for at historical cost and our consolidated financial statements for periods prior to the combinations have been restated to include the financial condition and the results of operation of these companies on a combined basis.

Moreover, the selected financial data should be read in conjunction with our consolidated financial statements and “Item 5. Operating and Financial Review and Prospects” included elsewhere in this annual report. Our consolidated financial statements are prepared and presented in accordance with International Financial Reporting Standards, or IFRS.



	Years Ended December 31,				
	2004	2005	2006	2007	2008
	RMB	RMB	RMB	RMB	RMB
	(in millions, except per share and per ADS data)				
<b>Consolidated Income Statement Data<sup>(1)</sup>:</b>					
Operating revenues	617,951	817,048	1,061,741	1,204,843	1,452,101
Other income	-	9,777	5,161	4,863	50,342
Operating expenses	(555,003)	(758,848)	(986,270)	(1,123,842)	(1,474,320)
Operating income	62,948	67,977	80,632	85,864	28,123
Earnings before income tax	59,386	64,525	78,542	83,464	24,317
Tax (expense)/benefit	(18,096)	(19,872)	(23,504)	(24,721)	1,883
Net income attributable to equity shareholders of the Company	35,289	41,354	53,603	56,533	29,769
Basic earnings per share	0.41	0.48	0.62	0.65	0.34
Basic earnings per ADS <sup>(2)</sup>	40.70	47.70	61.82	65.20	34.33
Diluted earnings per share <sup>(2)</sup>	0.41	0.48	0.62	0.65	0.30
Diluted earnings per ADS <sup>(2)</sup>	40.70	47.70	61.82	65.20	30.29
Cash dividends declared per share	0.10	0.12	0.13	0.16	0.145
<b>Segment results</b>					
Exploration and production	26,397	48,334	63,182	48,766	66,569
Refining	4,917	(3,695)	(25,710)	(10,452)	(61,538)
Marketing and distribution	14,716	10,350	30,234	35,727	38,209
Chemicals	18,843	14,186	14,458	13,306	(13,102)
Corporate and others	(1,925)	(1,198)	(1,532)	(1,483)	(2,015)
Operating income	62,948	67,977	80,632	85,864	28,123

	As of December 31,				
	2004	2005	2006	2007	2008
	RMB	RMB	RMB	RMB	RMB
	(in millions)				
<b>Consolidated Balance Sheet Data<sup>(1)</sup>:</b>					
Cash and cash equivalents	18,817	15,088	7,063	7,696	6,948
Total current assets	125,862	148,984	146,490	185,116	164,311
Total non-current assets	355,729	396,169	464,342	547,609	603,516
Total assets	481,591	545,153	610,832	732,725	767,827
Total current liabilities	151,361	177,706	216,372	265,355	274,537
Short-term debts and loans from Sinopec Group Company and its affiliates (including current portion of long-term debts)	45,231	46,674	63,480	60,494	98,483
Long-term debts and loans from Sinopec Group Company and its affiliates (excluding current portion of long-term debts)	95,784	103,408	100,637	120,314	127,144
Equity attributable to equity shareholders of the Company	195,239	226,099	264,334	307,433	328,669
Capital employed <sup>(3)</sup>	349,909	392,267	443,711	505,870	568,001

	Years Ended December 31,				
	2004	2005	2006	2007	2008
	RMB	RMB	RMB	RMB	RMB
	(in millions)				
<b>Other Financial Data<sup>(1)</sup>:</b>					
Net cash generated from operating activities	68,076	78,663	92,507	119,594	67,712
Net cash used in investing activities	(72,794)	(78,113)	(103,385)	(113,587)	(110,158)
Net cash generated from/(used in) financing activities	6,250	(4,257)	2,878	(5,310)	41,777

Capital expenditure					
Exploration and production	23,199	25,479	35,198	54,498	57,646
Refining	15,789	20,270	22,587	22,763	12,491
Marketing and distribution	16,678	10,954	11,319	12,548	14,148
Chemicals	11,025	9,386	12,629	16,184	20,622
Corporate and others	1,550	1,164	2,170	3,289	2,393
Total	68,241	67,253	83,903	109,282	107,300

- (1) The acquisitions of Petrochemical and Catalyst Assets in 2004, the acquisitions of equity interests in Sinopec Hainan and Oil Production Plants in 2006 and the acquisitions of equity interests in the Refining Plants in 2007 from Sinopec Group Company are treated as “combination of entities under common control” which are accounted in a manner similar to a pooling-of-interests. Accordingly, the acquired assets and liabilities have been accounted for at historical cost and the consolidated financial statements for periods prior to the combinations have been restated to include the financial condition and results of operation of these acquired companies on a combined basis. The considerations for these acquisitions were treated as equity transactions.
- (2) Basic earnings per share have been computed by dividing net income attributable to equity shareholders of the Company by the weighted average number of shares in issue. For the years ended December 31, 2004, 2005, 2006 and 2007, diluted earnings per share and per ADS are calculated on the same basis as basic earnings per share and per ADS, respectively, since there were no dilutive potential ordinary shares during the years. The calculation of diluted earnings per share for the year ended December 31, 2008 is based on the diluted net income attributable to equity shareholders of the Company of RMB 26,592 million and the diluted weighted average number of the shares of 87,789,799,595. Basic and diluted earnings per ADS have been computed as if all of our issued or potential ordinary shares, including domestic shares and H shares, are represented by ADSs during each of the years presented. Each ADS represents 100 shares.
- (3) Capital employed is derived by the sum of short-term debts, long-term debts, loans from Sinopec Group Company and its affiliates and total equity less cash and cash equivalents.

#### **B. CAPITALIZATION AND INDEBTEDNESS**

Not applicable.

#### **C. REASONS FOR THE OFFER AND USE OF PROCEEDS**

Not applicable.

#### **D. RISK FACTORS**

#### **Risks Relating to Our Business Operation**

##### *Our business may be adversely affected by the fluctuation of crude oil and refined petroleum product prices.*

We currently consume a large amount of crude oil to produce our refined products and petrochemical products. While we try to adjust the sale price of our products to track international crude oil price fluctuations, our ability to pass on the increased cost resulting from crude oil price increases to our customers is dependent on international and domestic market conditions as well as the PRC government’s price control over refined petroleum products. For example, the international crude oil price reached its historically high level in July 2008, but we were not able to effectively pass the increased cost to our customers of refined petroleum products. Although the current price-setting mechanism for refined petroleum products in China allows the PRC government to adjust price in the PRC market when the average international crude oil price fluctuates beyond certain levels within a certain time period, the PRC government still retains discretion as to whether or when to adjust the refined petroleum products price. The PRC government will exercise certain price control over refined petroleum products once international crude oil price experiences sustained growth or becomes significantly volatile. As a result, our results of operations and financial condition may be materially and adversely affected by the fluctuation of crude oil and refined petroleum product prices.

##### *Our continued business success depends in part on our ability to replace reserves and develop newly discovered reserves.*

Our ability to achieve our growth objectives is dependent in part on our level of success in discovering or acquiring additional oil and natural gas reserves and further exploring our current reserve base. Our exploration and

development activities for additional reserves also expose us to inherent risks associated with drilling, including the risk that no economically productive oil or natural gas reservoirs might be discovered. Exploring for, developing and acquiring reserves is highly risky and capital intensive. Without reserve additions through further exploration and development or acquisition activities, our reserves and production will decline over time, which may materially and adversely affect our results of operations and financial condition.

***We rely heavily on outside suppliers for crude oil and other raw materials, and we may even experience disruption of our ability to obtain crude oil and other raw materials.***

We purchase a significant portion of our crude oil and other feedstock requirements from outside suppliers located in different countries and areas in the world. In 2008, approximately 74% of the crude oil required for our refinery business was sourced from international suppliers, some of which are from countries or regions that are on the sanction list published and administered by the Office of Foreign Assets Control of the US Department of Treasury. In addition, our development requires us to source an increasing amount of crude oil from outside suppliers. We are subject to the political, geographical and economic risks associated with these countries and areas. If one or more of our material supply contracts were terminated or disrupted due to any natural disasters or political events, it is possible that we would not be able to find sufficient alternative sources of supply in a timely manner or on commercially reasonable terms. As a result, our business and financial condition would be materially and adversely affected.

***Our business faces operation risks and natural disasters that may cause significant property damages, personal injuries and interruption of operations, and we may not have sufficient insurance coverage for all the financial losses incurred by us.***

Exploring for, producing and transporting crude oil and natural gas and producing and transporting refined and petrochemical products involve a number of operating hazards. Significant operating hazards and natural disasters may cause interruption to our operations, property or environmental damages as well as personal injuries, and each of these incidents could have a material adverse effect on our financial condition and results of operations.

We have been paying high attention to the safety of our operation and implemented Health, Safety and Environment Management System within our company with the view to preventing accident, and reducing personal injuries, property losses and environment pollution. We also maintain insurance coverage on our property, plant, equipment and inventory. However, our preventative measures may not be effective and our insurance coverage may not be sufficient to cover all the financial losses caused by the operation risks and natural disasters. Losses incurred or payments required to be made by us due to operating hazards or natural disasters, which are not fully insured, may have a material adverse effect on our financial condition and results of operations.

***The oil and natural gas reserves data in this annual report are only estimates, and our actual production, revenues and expenditures with respect to our reserves may differ materially from these estimates.***

There are numerous uncertainties inherent in estimating quantities of proved oil and natural gas reserves, and in the timing of development expenditures and the projection of future rates of production. The reserve data set forth in this annual report represent estimates only. Adverse changes in economic conditions may render it uneconomical to develop certain reserves. Our actual production, revenues, taxes and fees payable and development and operating expenditures with respect to our reserves may likely vary from these estimates.

The reliability of reserves estimates depends on:

- the quality and quantity of technical and economic data;
- the prevailing oil and gas prices applicable to our production;
- the production performance of the reservoirs;
- extensive engineering judgments; and
- consistency in the PRC government's oil policies.

In addition, new drilling, testing and production following the estimates may cause substantial upward or downward revisions in the estimates.

***Our operations may be adversely affected by the global and domestic economic conditions.***

Our results of operations are materially affected by economic conditions in China and elsewhere around the world. Concerns over stability of the global financial market, inflation, energy costs, geopolitical issues, the availability and cost of credit and commodities have contributed to unprecedented levels of market volatility and diminished expectations for the global economy and the markets in the future. These factors, combined with declining business, consumer confidence and market demand, have precipitated an economic slowdown or even a recession. If the current market fluctuation continues and the global economy, particularly the Chinese economy and other markets where our products are sold, experiences significant or continuous slowdown or downturn, our business, financial condition, results of operations would be adversely affected.

***Our operations may be adversely affected by the cyclical nature of the market.***

Most of our revenues are attributable to sales of refined petroleum products and petrochemical products, and certain of these businesses and related products have historically been cyclical and sensitive to a number of factors that are beyond our control. These factors include the availability and prices of feedstock and general economic conditions, such as changes in industry capacity and output levels, cyclical changes in regional and global economic conditions, prices and availability of substitute products and changes in consumer demand. With the further reduction of tariffs and other import restrictions in the PRC on refined petroleum products and petrochemical products, many of our products have become increasingly subject to the cyclicity of global markets, and hence, our operations may be adversely affected by the cyclical nature of the market.

***We face strong competition from domestic and foreign competitors.***

Among our competitors, some are major integrated petroleum and petrochemical companies within and outside the PRC, which have recently become more significant participants in the petroleum and petrochemical industry in China. On December 4, 2006, Ministry of Commerce of the PRC promulgated the “Administrative Rules for Crude Oil Market” and “Administrative Rules for Refined Petroleum Products Market” to open the wholesale market of crude oil and refined petroleum products to new market entrants. As a result, we expect to face more competition in both crude oil and refined petroleum product markets. We believe such trend will continue. Increased competition may have a material adverse effect on our financial condition and results of operations.

***Our financing costs are subject to change in interest rates.***

Changes in the interest rate in China, which is subject to governmental control, have affected and will continue to affect our financing costs and our results of operations. The People’s Bank of China, or the PBOC, adjusts the benchmark interest rate according to China’s macroeconomic conditions. In 2008, the PBOC reduced the benchmark interest rate five times, and the benchmark one-year lending rate was reduced from 7.47% to 5.31%. There is no assurance that the PBOC will further reduce the benchmark interest rate or keep it at the current level. Any increase in the benchmark interest rate by the PBOC will result in an increase in the financing costs on our debt financing activities, and may materially and adversely affect our business, financial condition and results of operations.

**Risks Relating to Our Controlling Shareholder**

***Related party transactions.***

We have engaged from time to time and will continue to engage in a variety of transactions with Sinopec Group, which provides to us a number of services, including, but not limited to, ancillary supply, engineering, maintenance, transport, lease of land use right, lease of buildings, as well as educational and community services. The nature of our transactions with Sinopec Group is governed by a number of service and other contracts between Sinopec Group and us. We have established various schemes in those agreements so that these transactions would be entered into under terms at arm’s length. However, we cannot assure you that Sinopec Group Company or any of its members would not take actions that may favor its interests or its other subsidiaries' interests over ours.

### ***Non-competition.***

Sinopec Group Company has interests in certain businesses, such as oil refining, petrochemical producing and retail service stations, which compete or are likely to compete, either directly or indirectly, with our businesses. To avoid the adverse effects brought by the competition between us and Sinopec Group Company to the maximum extent possible, we and Sinopec Group Company have entered into a non-competition agreement whereby Sinopec Group Company has agreed to: refrain from operating new businesses which compete or could compete with us in any of our domestic or international markets; grant us an option to purchase Sinopec Group Company's operations that compete or could compete with our businesses; operate its sales enterprises and service stations in a manner uniform to our sales and service operations; and appoint us as sales agent for certain of its products which compete or could compete with our products. Notwithstanding the foregoing contractual arrangements, because Sinopec Group Company is our controlling shareholder, Sinopec Group Company may take actions that may conflict with our own interests.

### **Risks Relating to the PRC**

#### ***Government regulations may limit our activities and affect our business operations.***

The PRC government, though gradually liberalizing its regulations on entry into the petroleum and petrochemical industry, continues to exercise certain controls over the petroleum and petrochemical industry in China. These control mechanisms include granting the licenses to explore and produce crude oil and natural gas, granting the licenses to market and distribute crude oil and refined petroleum products, setting the pricing policy for the refined petroleum products, collecting special gain levies, assessing taxes and fees payable, deciding import and export quotas and procedures for the oil and gas industry, and setting safety, environmental and quality standards. As a result, we may face constraints on our flexibility and ability to expand our business operations or to maximize our profitability.

#### ***Our business operations may be adversely affected by present or future environmental regulations.***

As an integrated petroleum and petrochemical company, we are subject to extensive environmental protection laws and regulations in China. These laws and regulations permit:

- the imposition of fees for the discharge of waste substances;
- the levy of fines and payments for damages for serious environmental offenses; and
- the government, at its discretion, to close any facility which fails to comply with orders and require it to correct or stop operations causing environmental damage.

Our production operations produce substantial amounts of waste water, gas and solid waste materials. In addition, our production facilities require operating permits that are subject to renewal, modification and revocation. We have established a system to treat waste materials to prevent and reduce pollution.

The PRC government has moved, and may move further, toward more rigorous enforcement of applicable laws, and toward the adoption of more stringent environmental standards, which, in turn, would require us to incur additional expenditures on environmental matters.

#### ***Some of our development plans require compliance with state policies and regulatory confirmation and registration.***

We are currently engaged in a number of construction, renovation and expansion projects. Some of our large construction, renovation and expansion projects are subject to governmental confirmation and registration. The timing and cost of completion of these projects will depend on numerous factors, including when we can receive the required confirmation and registration from relevant PRC government authorities and the general economic condition in China. If any of our important projects required for our future growth are not confirmed or registered, or not confirmed or registered in a timely manner, our results of operations and financial condition could be adversely impacted.

***Foreign enterprise holders of H shares may be subject to PRC taxation.***

In accordance with the new Enterprise Income Tax Law and its implementation rules that became effective on January 1, 2008, dividends derived from the revenues accumulated from January 1, 2008 and are paid by PRC companies to non-resident enterprises, which are established under the laws of non-PRC jurisdictions and have no establishment or place of business in China or whose dividends from China do not relate to their establishment or place of business in China, are generally subject to a PRC withholding tax levied at a rate of 10% unless exempted or reduced pursuant to an applicable double-taxation treaty or other exemptions. Under the notice issued by the State Administration of Taxation of the PRC on November 6, 2008, we are required to withhold PRC income tax at the rate of 10% on dividends paid for 2008 and later years payable to our H Share investors that are “non-resident enterprises”. Accordingly, the investors of our American Depositary Shares representing our H Shares will be subject to such withholding of the PRC income tax at the rate of 10%.

***Government control of currency conversion and exchange rate fluctuation may adversely affect our operations and financial results.***

We receive substantially all of our revenues in Renminbi. A portion of such revenues will need to be converted into other currencies to meet our foreign currency needs, which include, among other things:

- import of crude oil and other materials;
- debt service on foreign currency-denominated debt;
- purchases of imported equipment;
- payment of the principals and interests of bonds issued overseas; and
- payment of any cash dividends declared in respect of the H shares (including ADS).

The existing foreign exchange regulations have significantly reduced government foreign exchange controls for transactions under the current account, including trade and service related foreign exchange transactions and payment of dividends. Foreign exchange transactions under the capital account, including principal payments in respect of foreign currency-denominated obligations, continue to be subject to significant foreign exchange controls and require the approval of the State Administration of Foreign Exchange. These limitations could affect our ability to obtain foreign exchange through debt or equity financing, or to obtain foreign exchange for capital expenditures. The PRC government has stated publicly that it intends to make the Renminbi freely convertible in the future. However, we cannot predict whether the PRC government will continue its existing foreign exchange policy and when the PRC government will allow free conversion of Renminbi.

The exchange rate of the Renminbi against the U.S. dollar and other foreign currencies fluctuates and is affected by, among other things, the foreign exchange control policies of the PRC government and the changes in the PRC’s and international political and economic conditions. On July 21, 2005, the PRC government introduced a floating exchange rate system to allow the value of the Renminbi to fluctuate within a regulated band based on market supply and demand and by reference to a basket of foreign currencies. From July 21, 2005 to December 31, 2008, the value of the Renminbi has appreciated by approximately 21% against the U.S. dollar. We purchase a significant portion of the crude oil from international suppliers, and the purchase price are benchmarked to US dollar-denominated international prices. Fluctuations in the exchange rate of the Renminbi against the US dollars and certain other foreign currencies may materially and adversely affect our financial condition and results of operations.

***Risks relating to enforcement of shareholder rights; Mandatory arbitration.***

Currently, the primary sources of shareholder rights are our articles of association, the PRC Company Law and the Listing Rules of the Hong Kong Stock Exchange, which, among other things, impose certain standards of conduct, fairness and disclosure on us, our directors and our controlling shareholder. In general, their provisions for protection of shareholder's rights and access to information are different from those applicable to companies incorporated in the United States, the United Kingdom and other Western countries. In addition, the mechanism for enforcement of rights under the corporate framework to which we are subject may also be relatively undeveloped and untested. To our knowledge, there has not been any published report of judicial enforcement in the PRC by H share shareholders of their rights under constituent documents of joint stock limited companies or the PRC Company Law or

in the application or interpretation of the PRC or Hong Kong regulatory provisions applicable to PRC joint stock limited companies. We cannot assure you that our shareholders will enjoy protections that they may be entitled in other jurisdictions.

China does not have treaties providing for the reciprocal recognition and enforcement of judgments of courts with the United States, the United Kingdom or most other Western countries, and therefore recognition and enforcement in China of judgments of a court in any of these jurisdictions in relation to any matter not subject to a binding arbitration provision may not be assured. Our articles of association as well as the Listing Rules of the Hong Kong Stock Exchange provide that most disputes between holders of H shares and us, our directors, supervisors, officers or holders of domestic shares, arising out of the articles of association or the PRC Company Law concerning the affairs of our company or with respect to the transfer of our shares, are to be resolved through arbitration by arbitration organizations in Hong Kong or China, rather than through a court of law. On June 18, 1999, an arrangement was made between Hong Kong and the PRC for the mutual enforcement of arbitral awards. This new arrangement was approved by the Supreme People's Court of the PRC and the Hong Kong Legislative Council, and became effective on February 1, 2000. So far as we are aware, no action has been brought in China by any shareholder to enforce an arbitral award, and we are uncertain as to the outcome of any action brought in China to enforce an arbitral award granted to shareholders.

#### **ITEM 4. INFORMATION ON THE COMPANY**

##### **A. HISTORY AND DEVELOPMENT OF THE COMPANY**

Our legal and commercial name is China Petroleum & Chemical Corporation. Our head office is located at 22 Chaoyangmen North Street, Chaoyang District, Beijing 100728, the People's Republic of China, our telephone number is (8610) 5996-0028 and our fax number is (8610) 5996-0386. We have appointed our subsidiary in the United States, SINOPEC-USA Co., Ltd., 410 Park Avenue, 22nd Fl., New York, NY 10022, USA (telephone number: (212) 759-5085; fax number: (212) 759-6882) as our agent for service of processes for actions brought under the U.S. securities laws.

We were established as a joint stock limited company on February 25, 2000 under the Company Law of the PRC with Sinopec Group Company as the sole shareholder. Our principal businesses consist of petroleum and petrochemical businesses transferred to us by Sinopec Group Company pursuant to a reorganization agreement. Such businesses include:

- exploration for, development, production and marketing of crude oil and natural gas;
- refining of crude oil and marketing and distribution of refined petroleum products, including transportation, storage, trading, import and export of petroleum products; and
- production and sales of petrochemical products.

Sinopec Group Company's continuing activities consist, among other things, of:

- exploring and developing oil and gas reserves overseas;
- operating certain petrochemical facilities, small capacity refineries and retail service stations that it retained;
- providing geophysical exploration, and well drilling, survey, logging and downhole operational services;
- manufacturing production equipment and providing equipment maintenance services;
- providing construction services;
- providing utilities, such as electricity and water; and
- providing other operational services including transportation services.

Sinopec Group Company transferred the businesses to us either by transferring its equity holdings in subsidiaries or by transferring their assets and liabilities. Sinopec Group Company also agreed in the reorganization agreement to transfer to us its exploration and production licenses and all rights and obligations under the agreements in connection with its core businesses transferred to us. The employees relating to these assets were also transferred to us.

In order to expand our core businesses, prevent competition between us and members of Sinopec Group and reduce related party transactions, between 2001 and 2007 we have acquired from Sinopec Group Company Sinopec National Star Petroleum Company, Sinopec Group Maoming Petrochemical Company, Tahe Oilfield Petrochemical Factory and Xi'an Petrochemical Main Factory, Petrochemical and Catalyst Assets, Refinery Plants and certain service stations, Oil Production Plants, and Sinopec Hainan. We have also sold and disposed of certain auxiliary assets to third parties. In addition, we have completed the privatization of Beijing Yanhua Petrochemical Co., Ltd. and Sinopec Zhenhai Refinery and Chemicals Co., Ltd. and the tender offers for the acquisition of publicly-held A-shares of four subsidiaries formerly listed on stock exchanges in China, namely Sinopec Qilu Petrochemical Co., Ltd., Sinopec Yangzi Petrochemical Co., Ltd., Sinopec Zhongyuan Petroleum Co., Ltd., and Shengli Oil Field Dynamic Co., Ltd.

In 2007, we also acquired 20 service stations and fuel business in Hong Kong from China Resources Enterprise, Ltd. We issued HK\$ 11.7 billion zero-coupon convertible bonds, the net proceeds from which were used to repay the foreign currency loans borrowed from domestic banks in connection with the privatization of the former Beijing Yanhua Petrochemical Co., Ltd. and Sinopec Zhenhai Refining & Chemical Co., Ltd.

On February 20, 2008, we issued bonds with detachable warrants in the amount of RMB 30 billion. The bonds have a 6-year term and 0.8% per annum fixed interest rate. The 3.03 billion warrants have an exercise ratio of two for one A Share and a term of two years. The initial exercise price of the warrants is RMB 19.68 per A Share, subject to further adjustment. The warrants are exercisable within 5 trading days prior to the expiration of the term of the warrants. The bonds and warrants were listed on Shanghai Stock Exchange on March 4, 2008. The proceeds from the issuance will be primarily used to fund our Sichuan-to-East China Gas Project, Tianjin one million tonnes per annum ethylene project, and Zhenhai one million tonnes per annum ethylene project. We also used a portion of the proceeds to repay our bank loans. The proceeds from the exercise of warrants was primarily used to fund our Tianjin one million tonnes per annum ethylene project, Zhenhai one million tonnes per annum ethylene project, and Wuhan ethylene project, as well as to repay our bank loans and to fund our working capital.

On June 26, 2008, we entered into a series of assets acquisition agreements with Shengli Oilfields Administrative Bureau, Zhongyuan Petroleum Exploration Bureau, Henan Petroleum Exploration Bureau, Jiangnan Oilfield Administrative Bureau, Jiangsu Petroleum Exploration Bureau and Huadong Petroleum Bureau, each of which is the wholly-owned entity of Sinopec Group Company, to acquire all their downhole operation assets. The consideration for the acquisition was RMB1,624 million. We used our internal resources to fund the acquisition. The acquisition was completed on June 30, 2008.

On December 22, 2008, we issued RMB 15 billion debentures with a term of six months and at a fixed interest rate of 2.30% per annum. The short-term debentures were sold to institutional investors among Chinese banks on the domestic bond market.

On March 27, 2009, we entered into agreements with Sinopec Group Company to acquire the 100% equity interests in Sinopec Qingdao Petrochemical Company Limited and certain other assets relating to our exploration and production, refining and marketing and distribution operations from Sinopec Group Company. On the same date, we also entered into agreement with Sinopec Group Company to dispose certain assets in our chemical segment to Sinopec Group Company. The consideration for the acquisition is RMB 1,839 million and the consideration for the disposal is RMB 157 million.

## **B. BUSINESS OVERVIEW**

### **Exploration and Production**

#### *Overview*

We currently explore for, develop and produce crude oil and natural gas in a number of areas across China. As of December 31, 2008, we held 190 production licenses with an aggregate acreage of 18,096 square kilometers and



with terms ranging from 10 to 80 years. Our production licenses are renewable upon our application at least 30 days prior to expiration. During the term of our production license, we pay an annual production license fee of RMB 1,000 per square kilometers. Shengli oilfield is the second largest oilfield in China and accounted for approximately 58% of our total crude oil and natural gas production in 2008.

As of December 31, 2008, we held 334 exploration licenses for various blocks in which we engaged in exploration activities. The maximum term of our exploration licenses is 7 years and the authorized total acreage under such licenses are 965,000 square kilometers. Our exploration licenses may be renewed upon our application at least 30 days prior to expiration of the original term with each renewal for a two-year term. We are obligated to make an annual minimum exploration investment in each of the exploration blocks which we obtained the exploration licenses. In addition, we are also obligated to pay an annual exploration license fee ranging from RMB 100 to RMB 500 per square kilometer. However, we are entitled under PRC laws and regulations for reduction and exemption of exploration license fee for exploration in China's western region, northeast region and offshore China.

### **Properties**

We currently operate 16 oil and gas producing fields, each of which consists of many oil and gas producing blocks and all of which are located in China.

Shengli oilfield is our most important producing oil field and the second largest producing oil field in China. It consists of 70 producing blocks of various sizes extending over an area of 2,564 square kilometers in northern Shandong province. Most of Shengli's blocks are located in the Jiyang trough with various oil producing levels. In 2008, Shengli field produced 200 million barrels of crude oil and 27.19 billion cubic feet of natural gas, with an average daily production of 552 thousand barrels-of-oil equivalent, accounting for approximately 58% of our total crude oil and natural gas production for the year.

### **Oil and Natural Gas Reserves**

Our estimated proved reserves of crude oil and natural gas as of December 31, 2008 were 4,001 million barrels-of-oil equivalent (including 2,841 million barrels of crude oil and 6,959 billion cubic feet of natural gas), representing an increase of 2.5% from 2007. Our estimated proved reserves do not include additional quantities recoverable beyond the term of the relevant production licenses, or that may result from extensions of currently proved areas, or from application of improved recovery processes not yet tested and determined to be economical.

The following tables set forth our proved oil and gas reserves and related data as of and for the years ended December 31, 2006, 2007 and 2008.

	<b>As of and for the Years Ended December 31,</b>		
	<b>2006</b>	<b>2007</b>	<b>2008</b>
<b>Proved developed and undeveloped reserves (crude oil)</b>	<b>(in million barrels)</b>		
Beginning of year	3,294	3,293	3,024
Revisions of previous estimates	(10)	(250)	(94)
Improved recovery	146	125	98
Extensions and discoveries	148	148	110
Production	(285)	(292)	(297)
End of year	<u>3,293</u>	<u>3,024</u>	<u>2,841</u>
<b>Proved developed reserves (crude oil)</b>	<b>(in million barrels)</b>		
Beginning of year	<u>2,870</u>	<u>2,903</u>	<u>2,651</u>
End of year	<u>2,903</u>	<u>2,651</u>	<u>2,451</u>
<b>Proved developed and undeveloped reserves (natural gas)</b>	<b>(in billion cubic feet)</b>		
Beginning of year	2,952	2,856	6,331
Revisions of previous estimates	(9)	222	203
Extensions and discoveries	170	3,536	718
Production	(257)	(283)	(293)
End of year	<u>2,856</u>	<u>6,331</u>	<u>6,959</u>
<b>Proved developed reserves (natural gas)</b>	<b>(in billion cubic feet)</b>		

Beginning of year	1,557	1,472	1,518
End of year	1,472	1,518	1,571

The following tables set forth proved developed and undeveloped crude oil and natural gas reserves of our primary oil and gas producing fields as of December 31, 2006, 2007 and 2008.

	<b>As of December 31,</b>		
	<b>2006</b>	<b>2007</b>	<b>2008</b>
	(in million barrels)		
<b>Proved developed and undeveloped crude oil reserves</b>			
Shengli	2,352	2,231	2,151
Zhongyuan	302	235	165
Xibei	288	280	275
Henan	136	96	81
Jiangsu	91	87	91
Others	124	95	78
Total	<u>3,293</u>	<u>3,024</u>	<u>2,841</u>

	<b>As of December 31,</b>		
	<b>2006</b>	<b>2007</b>	<b>2008</b>
	(in billion cubic feet)		
<b>Proved developed and undeveloped natural gas reserves</b>			
Shengli	313	328	264
Zhongyuan	355	361	189
Xibei	147	198	452
Jiangsu	12	10	12
Xinan	807	757	682
Huabei	792	781	709
Puguang	-	3,509	4,001
Others	430	387	650
Total	<u>2,856</u>	<u>6,331</u>	<u>6,959</u>

#### ***Oil and Natural Gas Production***

In 2008, we produced an average of 945 thousand barrels-of-oil equivalent per day, of which approximately 85.64% was crude oil and 14.36% was natural gas.

The following tables set forth the average daily production of crude oil and natural gas for the years ended December 31, 2006, 2007 and 2008. The production of crude oil includes condensed oil.

	<b>For the Years Ended December 31,</b>		
	<b>2006</b>	<b>2007</b>	<b>2008</b>
	(in thousand barrels)		
<b>Average daily crude oil production</b>			
Shengli	533	539	538
Zhongyuan	60	59	58
Xibei	92	104	116
Henan	35	35	35
Jiangsu	33	33	33
Others	28	29	31
Total Production	<u>781</u>	<u>799</u>	<u>811</u>

	<b>For the Years Ended December 31,</b>		
	<b>2006</b>	<b>2007</b>	<b>2008</b>
	(in million cubic feet)		
<b>Average daily natural gas production</b>			
Shengli	78	76	74
Zhongyuan	159	143	102
Xibei	84	92	123
Henan	8	7	6
Jiangsu	6	5	6
Xinan	213	260	261
Huabei	101	140	185
Others	54	51	44
<b>Total Production</b>	<b>703</b>	<b>774</b>	<b>801</b>

#### *Lifting Cost & Realized Prices*

The following table sets forth our average lifting costs per barrel-of-oil equivalent of crude oil and natural gas produced, average sales prices per barrel of crude oil and average sales prices per thousand cubic meters of natural gas for the years ended December 31, 2006, 2007 and 2008.

	<b>Total</b>	<b>Shengli</b>	<b>Others</b>
	(RMB)	(RMB)	(RMB)
<b>For the year ended December 31, 2008</b>			
Average petroleum lifting cost per BOE	88.80	92.24	83.99
Average realized sales price			
Per barrel of crude oil	601.22	598.99	605.80
Per thousand cubic meters of natural gas	941.47	992.15	939.48
<b>For the year ended December 31, 2007</b>			
Average petroleum lifting cost per BOE	84.62	87.23	80.78
Average realized sales price			
Per barrel of crude oil	435.94	421.66	466.17
Per thousand cubic meters of natural gas	822.83	939.92	817.72
<b>For the year ended December 31, 2006</b>			
Average petroleum lifting cost per BOE	73.31	77.16	67.34
Average realized sales price			
Per barrel of crude oil	449.93	443.66	463.70
Per thousand cubic meters of natural gas	794.28	899.76	788.02

#### *Exploration and Development Activities*

The following table sets forth the numbers of our exploration and development wells, including a breakdown of successful or productive wells and dry holes we drilled during the years ended December 31, 2006, 2007 and 2008.

	<b>Total</b>	<b>Shengli</b>	<b>Xibei</b>	<b>Others</b>
<b>For the year ended December 31, 2008</b>				
Exploration				
— Successful	248	128	26	94
— Dry holes	296	105	18	173
Development				
— Productive	3,128	1,563	141	1,424
— Dry holes	24	4	12	8
<b>For the year ended December 31, 2007</b>				
Exploration				
— Successful	251	118	16	117
— Dry holes	306	119	24	163
Development				
— Productive	2,956	1,136	112	1,708
— Dry holes	20	2	8	10
<b>For the year ended December 31, 2006</b>				

Exploration				
— Successful	226	118	20	88
— Dry holes	269	57	19	193
Development				
— Productive	2,620	1,125	94	1,401
— Dry holes	29	4	10	15

The following table sets forth the numbers of our development crude oil and natural gas wells as of December 31, 2008.

	<b>As of December 31, 2008</b>		
	<b>Total</b>	<b>Shengli</b>	<b>Others</b>
Crude oil development wells			
— Total	36,893	24,303	12,590
— Productive	29,485	18,889	10,596
Natural gas development wells			
— Total	2,886	394	2,492
— Productive	2,875	394	2,481

In 2008, we continued to increase our production capacity and scale of our reserve development. We made progress with our key exploration and development projects in northeastern Sichuan and Tahe. As a result, our crude oil production capacity increased by 5.80 million tonnes per annum and our natural gas production capacity increased by 1.33 billion cubic meters per annum in 2008. In addition, the Sichuan-to-East China Gas Project and the construction of Songnan gas field have been progressing on schedule.

## Refining

### Overview

We processed approximately 169.0 million tonnes of crude oil in 2008, representing approximately 53% of China's total crude oil throughput. We produce a full range of refined petroleum products. The following table sets forth our production of our principal refined petroleum products for the years ended December 31, 2006, 2007 and 2008.

	<b>For the Years Ended December 31,</b>		
	<b>2006</b>	<b>2007</b>	<b>2008</b>
	(in million tonnes)		
Gasoline	24.5	26.0	29.1
Diesel	60.2	62.5	68.8
Kerosene including jet fuel	6.4	8.3	8.0
Light chemical feedstock	22.7	23.5	23.0
Lubricant	1.1	1.3	1.2
Liquefied petroleum gas	6.9	7.4	8.0
Fuel oil	6.0	7.3	4.9

Gasoline and diesel are our largest revenue producing products, and are sold mostly through our marketing and distribution segment through both wholesale and retail channels. We use most of our production of chemical feedstock as feedstock for our own chemical operations. Most of our refined petroleum products were sold domestically to a wide variety of industrial and agricultural customers, and a small amount are exported.

### Refining Facilities

Currently we operate 33 refineries in China, all of which are located in our principal market. As of December 31, 2008, our total primary distillation capacity was 205.5 million tonnes per annum.

The following table sets forth our total primary distillation capacity per annum and crude oil throughputs as of and for the years ended December 31, 2006, 2007 and 2008.

	<b>As of and for the Years Ended December 31,</b>		
	<b>2006</b>	<b>2007</b>	<b>2008</b>
Primary distillation capacity (million tonnes per annum)	178.9	189.4	205.5
Crude oil throughputs (million tonnes)	152.4	161.5	168.8

In 2008, measured by the total output from our refineries, our overall gasoline yield was 17.23%, overall diesel yield was 40.75%, overall kerosene yield was 4.73% and overall light chemical feedstock yield was 13.62%. Other products include lubricant, liquefied petroleum gas, solvent, asphalt, petroleum coke, paraffin and fuel oil. For the years ended December 31, 2006, 2007 and 2008, our overall yield for all refined petroleum products at our refineries was 93.47%, 93.95% and 94.07%, respectively.

The following table sets forth the primary distillation capacity per annum as of, and refinery throughput for the years ended, December 31, 2006, 2007 and 2008 of each of our refineries with the primary distillation capacity of 8 million tonnes or more per annum as of December 31, 2008.

Refinery	<b>As of and for the Years Ended December 31,</b>					
	<b>2006</b>		<b>2007</b>		<b>2008</b>	
	Primary Distillation Capacity	Refinery Throughput	Primary Distillation Capacity	Refinery Throughput	Primary Distillation Capacity	Refinery Throughput
	<b>(in million tonnes)</b>					
Zhenhai	20.0	17.7	20.0	18.6	20.0	19.4
Shanghai	14.0	9.1	14.0	8.9	14.0	9.2
Maoming	13.5	14.0	13.5	13.1	13.5	13.0
Guangzhou	13.2	7.4	13.2	10.4	13.2	11.6
Jinling	13.0	10.8	13.0	11.5	13.0	11.2
Yanshan	8.0	8.0	13.0	8.6	13.0	10.7
Gaoqiao	11.0	9.3	11.0	8.1	11.0	10.2
Qilu	10.5	10.5	10.5	10.6	10.5	10.0
Qingdao <sup>(1)</sup>	-	-	-	-	10.0	5.1
Yangzi	8.0	7.9	8.0	8.2	8.0	7.5
Hainan	8.0	2.2	8.0	8.0	8.0	7.8
Luoyang	6.5	5.2	6.5	5.2	8.0	4.8
Wuhan	5.0	4.0	5.0	4.3	8.0	4.0

(1) Qingdao Refinery Project was completed and commenced operation in May 2008.

In 2008, we revamped or ramped up 581 sets of refining facilities, representing an increase of 23.9 million tonnes per annum of our primary distillation capacity of crude oil, including an increase of 16.7 million tonnes per annum in the distillation capacity of high-sulfur crude oil, from 2007. In addition, our hydro-refining capacity and coking capacity increased by 10.13 million tonnes per annum and 7.7 million tonnes per annum, respectively, in 2008 compared to 2007. The revamping projects for a number of refining facilities to improve refined petroleum product quality were also progressing as planned.

#### **Sources of Crude Oil**

Crude oil is our most important raw material. The following table sets forth the sources of our crude oil supply for the years ended December 31, 2006, 2007 and 2008.

Source of Supply	<b>For the Years ended December 31,</b>		
	<b>2006</b>	<b>2007</b>	<b>2008</b>
	<b>(in million tonnes)</b>		
Self-supply	30.81	30.83	30.88
PetroChina Company Ltd.	8.81	6.89	6.13
CNOOC Ltd.	6.38	7.42	7.55
Import	106.52	116.87	125.61
Total	152.52	162.01	170.17

## Marketing and Sales of Refined Petroleum Products

### Overview

We operate the largest sales and distribution network for refined petroleum products in China. In 2008, we distributed and sold in China approximately 122.98 million tonnes of gasoline, diesel and kerosene including jet fuel, representing a market share of approximately 60.1% in China. Most of the refined petroleum products sold by us are produced internally. In 2008, approximately 81% of our gasoline sales volume and approximately 88% of our diesel sales volumes were produced internally.

The table below sets forth a summary of key data in the marketing and sales of refined petroleum products for the year ended December 31, 2006, 2007 and 2008.

	For the Years Ended December 31,		
	2006	2007	2008
<b>Sales volume of refined petroleum products</b> (in million tonnes)	111.68	119.39	122.98
Of which: Retail	72.16	76.62	84.10
Direct Sales	18.95	20.17	19.63
Wholesale	20.57	22.60	19.25
<b>Average annual throughput of service stations</b> (tonnes per station)	2,577	2,694	2,935
<b>Total number of service stations under Sinopec brand as of December 31 of the respective year</b>	28,801	29,062	29,279
Of which: Self-operated service stations	28,001	28,405	28,647
Franchised service stations	800	657	632

### Retail

All of our retail sales are made through a network of service stations and petroleum shops operated under the Sinopec brand. Through this unified network we are more able to implement consistent pricing policies, maintain both product and service quality standards and more efficiently deploy our retail network.

In 2008, we sold approximately 84.1 million tonnes of refined petroleum products through our retail network, representing approximately 64.2% of our total refined petroleum products sales volume. Our retail market share in 2008 was approximately 79.8% in our principal market. As of December 31, 2008, our retail network mainly consists of service stations that are wholly-owned and operated by us or jointly-owned and operated or leased by us and franchised service stations that are owned and operated by third parties.

In 2008, we further improved our refined petroleum products retail networks through acquisition, construction and renovation of service stations, and added 720 new service stations into our retail network. We believe we have further strengthened our leading position in our principal market, and further improved our brand awareness and customer loyalty.

### Direct Sales

In 2008, we sold approximately 19.63 million tonnes of refined petroleum products, including 2.58 million tonnes of gasoline, 16.96 million tonnes of diesel and 0.09 million tonnes of kerosene, through direct sales to commercial customers such as industrial enterprises, hotels, restaurants and agricultural producers.

### Wholesale

In 2008, we sold approximately 19.25 million tonnes of refined petroleum products through wholesale channels, representing approximately 15.7% of our total sales volume of refined petroleum products. Our wholesale sales include sales to large commercial or industrial customers and independent distributors as well as sales to certain long-term customers such as railway, airlines, shipping and public utilities.

Through our wholesale centers, we operate 414 storage facilities with a total capacity of approximately 14.1 million cubic meters, substantially all of which are wholly-owned by us. Our wholesale centers are connected to our refineries by railway, waterway and, in some cases, by pipelines. We also own some dedicated railways, oil wharfs and oil barges, as well as a number of rail tankers and oil trucks.

## Chemicals

### Overview

We are the largest petrochemical producer in China. We produce a full range of petrochemical products including intermediate petrochemicals, synthetic resins, synthetic fiber monomers and polymers, synthetic fibers, synthetic rubber and chemical fertilizers. Synthetic resins, synthetic fibers, synthetic rubber, chemical fertilizers and some intermediate petrochemicals comprise a significant majority of our external sales. Synthetic fiber monomers and polymers and intermediate petrochemicals, on the other hand, are mostly internally consumed as feedstock for the production of other chemical products. Our chemical operations are integrated with our refining businesses, which supply a significant portion of our chemical feedstock such as naphtha. Because of strong domestic demand, most of our petrochemical products are sold in China's domestic market.

In 2008, our Fujian refinery and ethylene project, Tianjin refinery and ethylene project and Zhenhai ethylene project progressed smoothly. In addition, our Jinling para-xylene project, Yangzi butadiene project and the expansion project of Yanshan isobutylene isoprene rubber have been completed and commenced operation in 2008.

### Products

#### Intermediate Petrochemicals

We are the largest ethylene producer in China. Our rated ethylene capacity was 6.15 million tonnes per annum, which represented 61.5% of China's total domestic ethylene capacity, as of December 31, 2008. In 2008, we produced 6.29 million tonnes of ethylene, representing approximately 61.3% of the total domestic output. Nearly all of our olefins production is used as feedstock for our petrochemical operations.

We produce aromatics mainly in the forms of benzene and para-xylene, which are used primarily as feedstock for purified terephthalic acid, or PTA, the preferred raw material for polyester. We are the largest aromatics producer in China.

Organic chemicals extracted mainly from olefins and aromatics are intermediate petrochemicals and are essential raw materials for synthetic resins, synthetic rubber and synthetic fibers. We are the largest producer of butanol, styrene, paraxylene, vinyl acetate, phenol and acetone in China.

The following table sets forth our rated capacity per annum, production volume and major plants of production as of or for the year ended December 31, 2008 for our principal intermediate petrochemical products. These operational data include 100% of the rated capacity and production of the two joint ventures, SECCO and BASF-YPC, which we own 50% each.

	<b>Our Rated Capacity</b> (thousand tonnes per annum)	<b>Our Production</b> (thousand tonnes)	<b>Major Plants of Production</b>
Ethylene	6,145	6,289	Yanshan, Shanghai, Yangzi, Qilu, Maoming, Guangzhou, Tianjin, Zhongyuan, SECCO and BASF-YPC
Propylene	5,545	5,830	Yanshan, Shanghai, Yangzi, Qilu, Maoming, Guangzhou, Tianjin, Zhongyuan, SECCO, BASF-YPC, Gaoqiao, Anqing, Jinan, Jingmen and Wuhan
Benzene	2,699	2,236	Yanshan, Shanghai, Yangzi, Qilu, Guangzhou, Zhenhai, Tianjin, Luoyang, SECCO and BASF-YPC

Styrene	964	983	Yanshan, Qilu, Guangzhou, Maoming and SECCO
Para-xylene	2,768	1,932	Shanghai, Yangzi, Qilu, Tianjin and Luoyang
Phenol	350	346	Yanshan and Gaoqiao

*Synthetic Resins*

We are the largest producer of polyethylene, polypropylene and polystyrene and supplier of major synthetic resins products in China.

The following table sets forth our rated capacity per annum, production volumes and major plants of production for each of our principal synthetic resins as of or for the year ended December 31, 2008. These operational data include 100% of the rated capacity and production of the two joint ventures, SECCO and BASF-YPC, which we own 50% each.

	<b>Our Rated Capacity</b> (thousand tonnes per annum)	<b>Our Production</b> (thousand tonnes)	<b>Major Plants of Production</b>
Polyethylene	4,323	4,454	Yanshan, Shanghai, Yangzi, Qilu, Maoming, Guangzhou, Tianjin, Zhongyuan, SECCO and BASF-YPC
Polypropylene	3,672	3,897	Yanshan, Shanghai, Yangzi, Qilu, Guangzhou, Maoming, Tianjing, Zhongyuan, SECCO, Wuhan Fenghuang, Jingmen and Fujian
Polyvinyl chloride	600	575	Qilu
Polystyrene	536	374	Yanshan, Qilu, Maoming, Guangzhou and SECCO
Acrylonitrile butadiene styrene	200	135	Gaoqiao

*Synthetic Fiber Monomers and Polymers*

Our principal synthetic fiber monomers and polymers are purified terephthalic acid, ethylene glycol, acrylonitrile, caprolactam, polyester, polyethylene glycol and polyamide fiber. Based on our 2008 production, we are the largest producer of purified terephthalic acid, ethylene glycol, caprolactam and polyester in China. Most of our production of synthetic fiber monomers and polymers are used as feedstock for synthetic fibers.

The following table sets forth our rated capacity per annum, our production volume and major plants of production as of or for the year ended December 31, 2008 for each type of our principal synthetic fiber monomers and polymers. These operational data include 100% of the rated capacity and production of the two joint ventures, SECCO and BASF-YPC, which we own 50% each.

	<b>Our Rated Capacity</b> (thousand tonnes per annum)	<b>Our Production</b> (thousand tonnes)	<b>Major Plants of Production</b>
Purified terephthalic acid	3,034	2,894	Shanghai, Yangzi, Yizheng, Tianjin and Luoyang



Ethylene glycol	1,413	1,057	Yanshan, Shanghai, Yangzi, Tianjing, Maoming and BASF-YPC
Acrylonitrile	510	494	Shanghai, Anqing, Qilu and SECCO
Caprolactam	210	193	Shijiazhuang and Baling
Polyester	2,713	2,511	Shanghai, Yizheng, Tianjin and Luoyang

#### *Synthetic Fibers*

We are the largest producer of polyester and acrylic fibers in China. Our principal synthetic fiber products are polyester fiber and acrylic fiber.

The following table sets forth our rated capacity per annum, production volume and major plants of production for each type of our principal synthetic fibers as of and for the year ended December 31, 2008.

	<b>Our Rated Capacity</b>	<b>Our Production</b>	<b>Major Plants of Production</b>
	(thousand tonnes per annum)	(thousand tonnes)	
Polyester fiber	1,461	941	Yizheng, Shanghai, Tianjin and Luoyang
Acrylic fiber	315	314	Shanghai, Anqing and Qilu

#### *Synthetic Rubbers*

Our principal synthetic rubbers are cis-polybutadiene rubber, styrene butadiene rubber, or SBR, styrene butadiene-styrene thermoplastic elastomer and isobutadiene isoprene rubber, or IIR. Based on our 2008 production, we are the largest producer of SBR and cis-polybutadiene rubber and the only producer of IIR in China.

The following table sets forth our rated capacity per annum, production volume and major plants of production as of or for the year ended December 31, 2008 for each of our principal synthetic rubbers.

	<b>Our Rated Capacity</b>	<b>Our Production</b>	<b>Major Plants of Production</b>
	(thousand tonnes per annum)	(thousand tonnes)	
Cis-polybutadiene rubber	266	290	Yanshan, Qilu, Maoming and Gaoqiao
Styrene butadiene rubber	365	335	Yanshan, Qilu, Maoming and Gaoqiao and Yangzi
Styrene-butadiene-styrene thermoplastic elastomers	170	165	Yanshan and Maoming
Isobutylene isoprene rubber	30	44	Yanshan

#### *Chemical Fertilizers*

We produce synthetic ammonia and urea. Our synthetic ammonia is used to manufacture urea, caprolactam and acrylic nitrile.

The following table sets forth our rated capacity per annum, our production volume and major plants of production for ammonia and urea as of or for the year ended December 31, 2008.

	<u>Our Rated Capacity</u> (thousands of tonnes per annum)	<u>Our Production</u> (thousands tonnes)	<u>Major Plants of Operation</u>
Ammonia	1,935	1,087	Zhenhai, Jinling, Anqing, Jiujiang, Qilu, Hubei and Baling
Urea	3,130	1,649	Zhenhai, Jinling, Anqing, Jiujiang, Qilu, Hubei and Baling

### ***Marketing and Sales of Petrochemicals***

Price and volume of petrochemical sales are primarily market driven. The southern and eastern regions in China, where most of our petrochemical plants are located, constitute the major petrochemical market in China. Our proximity to the major petrochemical market gives us a geographic advantage over our competitors.

Our principal sales and distribution channels consist of direct sales to end-users, most of which are large- and medium-sized manufacturing enterprises, and sales to distributors in our national sales network. In 2008, we sold approximately 77% of our petrochemical products directly to end-users and 23% to our distributors.

We also provided after-sale services to our customers, including technical support. We continuously strive to improve our product mix and enhance our product quality to meet market needs.

### **Competition**

#### ***Exploration and Production***

Because our production of crude oil can only meet approximately 18.1% of our crude oil requirements, we generally do not compete for crude oil customers. However, we compete with other market participants for the acquisition of desirable crude oil and natural gas prospects.

#### ***Refining and Marketing of Refined Petroleum Products***

Market participants compete primarily on the basis of quality of products and service, efficiency of operations including proximity to customers, awareness of brand name and price. While we constantly face competition from other market participants, we believe that we have a competitive advantage in our principal market over our competitors in most of these aspects.

#### ***Chemicals***

We compete with domestic and foreign chemicals producers in the chemicals market. We believe our proximity to customers has given us significant geographical advantages. Most of our petrochemical production facilities are located in the eastern and southern regions in China, an area which has experienced higher economic growth rates in China in the past two decades. Proximity of our production facilities to our markets has given us an advantage over our competitors in terms of easy access to our customers, resulting in lower transportation costs, more reliable delivery of products and better service to customers.

### **Patents and Trademarks**

In 2008, we were granted 572 patents in China and overseas. As of December 31, 2008, we owned a total of 4,477 patents in China. We may use certain patents of Sinopec Group Company under royalty-free licenses. These patents expire from time to time and cover many products, processes and product uses. We also have royalty-free licenses from Sinopec Group Company to use certain Sinopec Group Company's trademarks and brands, including the "Sinopec" brand, for our products and services. Our trademark licenses from Sinopec Group Company are for a term of ten years commencing on February 25, 2000, and the licenses are renewable at our option.

### **Regulatory Matters**

#### ***Overview***

China's petroleum and petrochemical industry has seen significant liberalization in the past ten years. However, the exploration, production, marketing and distribution of crude oil and natural gas, as well as the

production, marketing and distribution of certain refined petroleum products are still subject to regulation of many government agencies including:

*National Development and Reform Commission ("NDRC")*

The NDRC is responsible for formulating and implementing key policies in respect of petroleum and petrochemical industry, including:

- Formulating guidance plan for annual production, import and export amount of crude oil, natural gas and gasoline nationwide based on its forecast on macro economic conditions in China;
- Setting the pricing policy for refined petroleum products;
- Approving certain domestic and overseas resource investment projects which are subject to NDRC's approval as required by the Catalogue of Investment Projects Approved by the Government (2004); and
- Approving foreign investment projects that are in excess of certain investment limits.

*The Ministry of Commerce ("MOFCOM")*

MOFCOM is responsible for examining and approving production sharing contracts, Sino-foreign equity joint venture contracts and Sino-foreign cooperation joint venture contracts for oil and gas development within the PRC. It is also responsible to issue quotas and licenses for import and export of crude oil and refined oil.

*Ministry of Land and Resources ("MLR")*

The MLR is responsible for issuing the licenses that are required to explore and produce crude oil and natural gas in China.

**Regulation of Exploration and Production**

*Exploration and Production Rights*

The PRC Constitution provides that all mineral and oil resources belong to the state. In 1986, the Standing Committee of the National People's Congress passed the Mineral Resources Law which authorizes the Ministry of Land and Resources, or the MLR, to exercise administrative authority over the exploration and production of the mineral and oil resources within the PRC, including its territorial waters. The Mineral Resources Law and its supplementary regulations provide the basic legal framework under which exploration licenses and production licenses are granted. The MLR has the authority to grant exploration licenses and production licenses on a competitive bidding or other basis it considers appropriate. Applicants for these licenses must be companies approved by the State Council to engage in oil and gas exploration and production activities. Currently, only we, PetroChina, CNOOC and Yanchang Petroleum Group Ltd. have received such exploration licenses and production licenses in oil and gas industry. In addition, pursuant to the Regulation on the Administration of Geological Survey Qualifications promulgated by the State Council, which will become effective from July 1, 2008, any entity engaging in geological survey activities shall obtain a geological survey qualification certificate. Oil and natural gas survey qualifications, among others, shall be examined, approved and granted by the MLR.

Applicants for exploration licenses must first register with the MLR blocks in which they intend to engage in exploration activities. The holder of an exploration license is obligated to make an annual minimum exploration investment relating to the exploration blocks in respect of which the license is issued. Investment ranges from RMB 2,000 per square kilometer for the initial year to RMB 5,000 for the second year and to RMB 10,000 for the third and subsequent years. Additionally, the holder has to pay an annual exploration license fee of RMB 100 per square kilometer for each of the first three years. Afterwards, the annual fee increases by an additional RMB 100 per square kilometer per year up to a maximum of RMB 500 per square kilometer. The maximum term of an exploration license is 7 years. The exploration license may be renewed upon application by the holder at least 30 days prior to expiration of the original term with each renewal for a two-year term.

At the exploration stage, an applicant can also apply for a progressive exploration and production license that allows the holder to test and develop reserves not yet fully proved. The progressive exploration and production license

has a maximum term of 15 years. When the reserves become proved for a block, the holder must apply for a full production license in order to undertake production.

The MLR issues full production licenses to applicants on the basis of the reserve reports approved by relevant authorities. The maximum term of a full production license is 30 years unless a special dispensation is given by the State Council. Due to a special dispensation granted to us by the State Council, the maximum term of our full production licenses is 80 years. The full production license is renewable upon application by the holder at least 30 days prior to expiration of the original term. A holder of the full production license has to pay an annual full production right usage fee of RMB 1,000 per square kilometer.

All companies approved by the State Council to engage in oil and gas exploration and production activities may apply for exploration and production licenses for onshore and off-shore oil and natural gas resources without geographical restrictions. We have exploration and production licenses for the exploration and production of both onshore and offshore crude oil and natural gas resources in China.

Exploration and production licenses do not grant the holders the right to enter upon any land for the purpose of exploration and production. Holders of exploration and production licenses must separately obtain the right to use the land covered by the licenses, and if permissible under applicable laws, current owners of the rights to use such land may transfer or lease the land to the license holder.

#### *Volume and Price of Natural Gas*

The NDRC formulates the annual natural gas supply guidelines which require natural gas producers to distribute specified amount of natural gas to specified fertilizer producers. The actual production level of natural gas (excluding the amount supplied to the fertilizer producers) is determined by the natural gas producers themselves.

The price of natural gas has two components:

- ex-factory price; and
- pipeline transportation fee

Since December 2005, the NDRC simplified the ex-factory price-setting mechanism by dividing natural gas prices into two tiers and setting a median guidance ex-factory price for each tier. The price for the first tier may be set within  $\pm 10\%$  of the guidance price through negotiation between the producers and their customers, while the price for the second tier may fluctuate up to 10% of the guidance price with no limitation on the minimum price. In addition, the NDRC would adjust the guidance prices once per year by up to 8% annually to reflect the price trends of crude oil and other alternative energies. On November 8, 2007, the NDRC adopted an adjusted pricing policy for natural gas, by increasing the guidance ex-factory price of the natural gas for industrial applications other than chemical fertilizers by RMB 400.0 per thousand cubic meters, deregulating the ex-factory price of the natural gas for LNG producers, fixing the minimum ratio between the base retail price of natural gas for automobiles and the base retail price of #90 gasoline at 0.75:1.

Natural gas producers submit to the NDRC for examination and approval of any proposed transportation fee for the natural gas transported by pipelines, which was based on the capital investment made in the pipeline, the depreciation period for the pipeline and the ability of end users to pay.

#### ***Regulation of Refining and Marketing of Refined Petroleum Products***

##### *Volume and Price Controls on Gasoline, Diesel and Jet Fuel*

The PRC government continues to exercise control over gasoline, diesel and jet fuel prices.

According to the Notice on Implementing Reforms on Prices of Refined Products and Tax promulgated by the State Council on December 18, 2008 and the Measures for Administration of Petroleum Products Price (Trial) issued by the NDRC on May 7, 2009, the sale price for refined petroleum products in the PRC market shall be adjusted with reference to international crude oil price fluctuations, subject to governmental control. The NDRC will set guidance sale prices for certain refined petroleum products for both wholesale and retail market. As a principle, maximum retail price for gasoline and diesel in the Chinese market shall be decided with reference to the international crude oil price plus the average domestic processing costs, tax levies, reasonable sales and marketing expenses and appropriate profit. The refined petroleum products price in the PRC market may be adjusted when the moving average price of international crude oil price fluctuates beyond 4% within a period of 22 consecutive business days. If the international crude oil prices experience sustained increase or radical fluctuation, the price of refined petroleum products, including gasoline and diesel products, will be controlled by the government to reduce the oil price fluctuation impact upon the PRC market.

### ***Regulation of Crude Oil and Refined Petroleum Products Market***

On December 4, 2006, Ministry of Commerce of the PRC promulgated the “Administrative Rules for Crude Oil Market” and “Administrative Rules for Refined Petroleum Products Market” to open the wholesale market of crude oil and refined petroleum products to new market entrants, respectively. We will face more competition in both crude oil and refined petroleum products markets. Such increased competition may have a material adverse effect on our financial conditions and results of operations.

### ***Investment***

Under the State Council's Decision on Investment System Reform, investments without the use of government funds are only subject to a licensing system or a registration system, as the case may be. Under the current system, only significant projects and the projects of restrictive nature are subject to approval so as to maintain social and public interests, and all other projects of any investment scale are only subject to a registration system.

Overseas investment project falling within the category of resources development involving investment by any Chinese party of above US\$200 million (inclusive) shall be verified and approved by the State Council, and those involving investment of above US\$30 million (inclusive) shall be verified and approved by the NDRC. Other overseas investment project shall be verified and approved by State Council if it involves investment by any Chinese party of above US\$50 million (inclusive), or by the NDRC if it involves investment by any Chinese party of above US\$10 million (inclusive). Any overseas investment projects other than the foregoing shall be filed with the NDRC and/or the MOFCOM if the investor is an enterprise managed by the central government, or approved by its local government according to applicable laws and regulations. Overseas investment projects involving domestic enterprise's establishment or acquisition of overseas enterprise to acquire ownership, control or management rights of overseas enterprise (with the exception of financial enterprises) shall be approved by the MOFCOM or relevant provincial-level commerce authorities according to applicable laws and regulations.

Pursuant to the Anti-Monopoly Law of the PRC which became effective on August 1, 2008, when market concentration by business carriers through merger, acquisition of control through shares or assets acquisition, or acquisition of control or the ability to exercise decisive influence over other business carriers by contract or by other means reaches a threshold of declaration level prescribed by the State Council, the business carriers shall declare in advance to the Anti-monopoly Law Enforcement Agency, otherwise, the business carriers shall not implement such market concentration.

### ***Taxation, Fees and Royalty***

Companies which operate petroleum and petrochemical businesses in China are subject to a variety of taxes, fees and royalties.

On March 26, 2006, the PRC government imposed a special oil income levy on revenues generated from the sale of domestically produced crude oil when the realized price exceeds US\$ 40 per barrel. The special oil income levy has five levels and is calculated and charged according to the progressive ad valorem rates on the excess amounts. The levy is calculated on a monthly basis and collected on a quarterly basis. The applicable rate of the levy is determined based on the weighted average crude oil sale price of the exploration and production company of a particular month.

Starting from January 1, 2008, the general enterprise income tax rate imposed on entities, other than certain enterprises defined in the new Enterprise Income Tax Law of the PRC, shall be 25%.

According to the Notice on Implementing Reforms on Prices of Refined Products and Tax, starting from January 1, 2009, consumption tax on refined petroleum products were adjusted. Applicable tax, fees and royalties on refined petroleum products and other refined products generally payable by us or by other companies in similar industries are shown below.

<b><u>Tax Item</u></b>	<b><u>Tax Base</u></b>	<b><u>Tax Rate</u></b>
Enterprise income tax	Taxable income	25% starting from January 1, 2008.
Value-added tax	Revenue	13% for liquefied petroleum gas, natural gas, and low density polyethylene for production of agricultural film and fertilizers and 17% for other items. We generally charge value-added tax to our customers at the time of settlement on top of the selling prices of our products on behalf of the taxation authority. We may directly claim refund from the value-added tax collected from our customers of any value-added tax that we paid for (i) purchasing materials consumed during the production process; (ii) charges paid for drilling and other engineering services; and (iii) labor consumed during the production process.
Business tax	Revenue from pipeline transportation services	3%.
Consumption tax	Aggregate volume sold or self-consumed	RMB 1 per liter for gasoline, naphtha, solvent oil and lubricant; RMB 0.8 per liter for diesel, fuel oil and jet fuel. Prior to December 31, 2010, the consumption tax paid for imported naphtha for the production of ethylene and aromatic hydrocarbon will be refunded, and naphtha procured from domestic sources for the production of ethylene and aromatic hydrocarbon will remain tax-free. Consumption tax on jet fuel is currently exempted.
Import tariff	CIF China price	5% for gasoline, 6% for light diesel and 9% for jet kerosene. The actual applicable tax rate in 2009 for gasoline, diesel and jet kerosene is 1%.
Resource tax	Aggregate volume sold or self-consumed	RMB 14 to RMB 30 per tonne for crude oil. RMB 7 to RMB 15 per thousand cubic meters for natural gas.
Compensatory fee for mineral resources	Revenue of crude oil and natural gas	1%.
Exploration license fee	Area	RMB 100 to 500 per square kilometer per annum.
Production license fee	Area	RMB 1,000 per square kilometer per annum.
Royalty fee <sup>(1)</sup>	Production volume	Progressive rate of 0-12.5% for crude oil and 0-3% for natural gas.
City construction tax	Total amount of value-added tax, consumption tax and business tax	1%, 5% and 7%.
Education Surcharge	Total amount of value-added tax, consumption tax and business tax	3%.
Special Oil Income Levy	Any revenue derived from sale of domestically produced crude oil when the realized crude oil price exceeds US\$ 40 per	Progressive rate of 20% to 40% for revenue derived from crude oil with realized price in excess of US\$ 40 per barrel, i.e. 20% for the portion in excess of US\$ 40 per barrel up to US\$ 45 per barrel (inclusive); 25% for the portion in excess of US\$ 45 per barrel up to US\$ 50 per

barrel.

barrel (inclusive); 30% for the portion in excess of US\$ 50 per barrel to US\$ 55 per barrel (inclusive); 35% for the portion in excess of US\$ 55 per barrel to US\$ 60 per barrel (inclusive); and 40% for the portion in excess of US\$ 60 per barrel.

- (1) Payable only by Sino-foreign oil and gas exploration and development cooperative projects, and the project companies of those cooperative projects are not subject to any other resource taxes or fees.

### **C. ORGANIZATIONAL STRUCTURE**

For a description of our relationship with Sinopec Group Company, see "Item 4. Information on the Company — A. History and Development of the Company" and "Item 7. Major Shareholders and Related Party Transactions." For a description of our significant subsidiaries, see Note 33 to our consolidated financial statements.

### **D. PROPERTY, PLANT AND EQUIPMENT**

We own substantially all of our properties, plants and equipment relating to our business activities. We hold production licenses covering all of our interests in our developed and undeveloped crude oil and natural gas fields and productive wells. See "Item 4. Information on the Company — B. Business Overview" for description of our property, plant and equipment.

### **Environmental Matters**

We are subject to various national environmental laws and regulations and also environmental regulations promulgated by the local governments in whose jurisdictions we have operations. For example, national regulations promulgated by the central government set discharge standards for emissions into air and water. They also set forth schedules of discharge fees for various waste substances. These schedules usually provide for discharge fee increases for each incremental increase of the amount of discharge up to a certain level. Above a certain level, the central regulations permit the local government to order any of our facilities to cure certain behavior causing environmental damage and subject to the central government's approval, the local government may also issue orders to close any of our facilities that fail to comply with the existing regulations. In addition, the PRC government has set certain environmental protection objective for the petroleum and chemical industry to reduce energy intensity, chemical oxygen demand, industrial water consumption and sulfur dioxide emission by certain level by 2009 compared to 2005. In light of such objective, we have increased our capital expenditure to promote energy saving and environmental protection in China.

Each of our production subsidiaries has implemented a system to control its pollutant emissions and to oversee compliance with the PRC environmental regulations. We have a central safety and environmental compliance department to set our internal environmental requirements and procedures, and to manage and supervise the environmental protection programs at the various production facilities. Each production subsidiary has an environmental compliance department which is responsible for supervising environmental matters at the subsidiary and implementing our environmental requirements and procedures. These departments report both to the management of the subsidiary and to the central environmental compliance department.

Our production facilities have their own facilities to treat waste water, solid waste and waste gases on site. Waste water first goes through preliminary treatment at our own waste water treatment facilities. Thereafter, the water is sent to nearby waste water treatment centers operated either by us or by Sinopec Group for further treatment. All solid waste materials generated by our production facilities are buried at disposal sites or burned in furnaces either operated by us or by Sinopec Group. Waste gases are generally treated and burned in furnaces before dissipation and the ash is disposed in accordance with our solid waste disposal procedures.

Environmental regulations also require companies to file an environmental impact report to the environmental bureau for approval before undertaking any construction of a new production facility or any major expansion or renovation of an existing production facility. Such an undertaking will not be permitted to operate until the environmental bureau has performed an inspection and is satisfied that environmentally sound equipment has been installed for the facility.

We believe our environmental protection systems and facilities are adequate for us to comply with current applicable national and local environmental protection regulations. The PRC government, however, may impose stricter regulations which require additional expenditure on compliance with environmental regulations.

We paid pollutant discharge fees of approximately RMB 1.6 billion in 2006, RMB 2.1 billion in 2007 and RMB 2.3 billion in 2008.

## **Insurance**

In respect of our refining, petrochemical production, and marketing and sales operations, we currently maintain with Sinopec Group Company, under the terms of its Safety Production Insurance Fund ("SPI Fund"), approximately RMB 418.9 billion of coverage on our property and plants and approximately RMB 69.6 billion of coverage on our inventory. In 2008, we paid an insurance premium of approximately RMB 1.88 billion to Sinopec Group Company for such coverage. Transportation vehicles and products in transit are not covered by Sinopec Group Company and we maintain insurance policies for those assets with insurance companies in the PRC.

The insurance coverage under SPI Fund applies to all enterprises controlled by Sinopec Group Company under regulations published by the Ministry of Finance. We believe that, in the event of a major accident, we will be able to recover most of our losses from insurance proceeds paid under the SPI Fund or by insurance companies.

Pursuant to an approval of the Ministry of Finance, Sinopec Group Company entered into an agreement with China People's Insurance Company on January 29, 2002 to purchase a property and casualty policy which would also cover our assets. The policy provides for an annual maximum cumulative claim amount of RMB 4.0 billion and a maximum of RMB 2.36 billion per occurrence.

Consistent with what we believe to be customary practice among PRC enterprises, we do not currently carry any third party liability insurance to cover claims in respect of personal injury, environmental damage arising from accidents on our property or relating to our operations other than on our transportation vehicles. We have not had a third party liability claim filed against us during the past three years. We do not carry business interruption insurance, as such coverage is not customary in the PRC.

## **ITEM 4A. UNRESOLVED STAFF COMMENTS**

None.

## **ITEM 5. OPERATING AND FINANCIAL REVIEW AND PROSPECTS**

### **A. GENERAL**

The following discussion and analysis should be read in conjunction with our audited consolidated financial statements. Our consolidated financial statements have been prepared in accordance with IFRS. Certain financial information presented in this section is derived from our audited consolidated financial statements. Unless otherwise indicated, all financial data presented on a consolidated basis or by segment, are presented net of inter-segment transactions (i.e., inter-segment and other intercompany transactions have been eliminated).

### **Critical Accounting Policies**

Our reported consolidated financial condition and consolidated results of operations are sensitive to accounting methods, assumptions and estimates that underlie the preparation of our financial statements. We base our assumptions and estimates on historical experience and on various other assumptions that we believe to be reasonable and which form the basis for making judgments about matters that are not readily apparent from other sources. On an on-going basis, our management evaluates its estimates. Actual results may differ from those estimates as facts, circumstances and conditions change.

The selection of critical accounting policies, the judgments and other uncertainties affecting application of those policies and the sensitivity of reported results to changes in conditions and assumptions are factors to be considered when reviewing our financial statements. Our principal accounting policies are set forth in Note 2 to the consolidated financial statements. We believe the following critical accounting policies involve the most significant judgments and estimates used in the preparation of our financial statements.



### *Oil and gas properties and reserves*

The accounting for our upstream oil and gas activities is subject to special accounting rules that are unique to the oil and gas business. There are two methods to account for oil and gas business activities, the successful efforts method and the full cost method. We have elected to use the successful efforts method.

The successful efforts method reflects the volatility that is inherent in exploring for mineral resources in that costs of unsuccessful exploratory efforts are charged to expense as they are incurred. These costs primarily include dry hole costs, seismic costs and other exploratory costs. Under the full cost method, these costs are capitalized and written-off (depreciation) over time.

Engineering estimates of our oil and gas reserves are inherently imprecise and represent only approximate amounts because of the subjective judgments involved in developing such information. There are authoritative guidelines regarding the engineering criteria that have to be met before estimated oil and gas reserves can be designated as "proved". Proved and proved developed reserves estimates are updated at least annually and take into account recent production and technical information about each field. In addition, as prices and cost levels change from year to year, the estimate of proved and proved developed reserves also changes. This change is considered a change in estimate for accounting purposes and is reflected on a prospective basis in related depreciation rates.

Future dismantlement costs for oil and gas properties are estimated with reference to engineering estimates after taking into consideration the anticipated method of dismantlement required in accordance with industry practices in similar geographic area, including estimation of economic life of oil and gas properties, technology and price level. The present values of these estimated future dismantlement costs are capitalized as oil and gas properties with equivalent amounts recognized as provision for dismantlement costs.

Despite the inherent imprecision in these engineering estimates, these estimates are used in determining depreciation expense, impairment expense and future dismantlement costs, and in disclosing the supplemental standardized measure of discounted future net cash flows relating to proved oil and gas properties. Depreciation rates are determined based on estimated proved developed reserve quantities (the denominator) and capitalized costs of producing properties (the numerator). Producing properties' capitalized costs are amortized based on the units of oil or gas produced. Therefore, assuming all other variables are held constant, an increase in estimated proved developed reserves decreases our depreciation, depletion and amortization expense. Also, estimated reserves are often used to calculate future cash flows from our oil and gas operations, which serve as an indicator of fair value in determining whether a property is impaired or not. The larger the estimated reserves, the less likely the property is impaired. There have been no significant changes to the original reserve estimates during any of the three years ended December 31, 2006, 2007 and 2008.

### *Impairment for long-lived assets*

If circumstances indicate that the net book value of a long-lived asset, including oil and gas properties, may not be recoverable, the asset may be "impaired", and an impairment loss may be recognized. The carrying amounts of long-lived assets are reviewed periodically in order to assess whether the recoverable amounts have declined below the carrying amounts. For goodwill, the recoverable amount is estimated annually. These assets are tested for impairment whenever events or changes in circumstances indicate that their recorded carrying amounts may not be recoverable. When such a decline has occurred, the carrying amount is reduced to recoverable amount. The recoverable amount is the greater of the net selling price and the value in use. It is difficult to precisely estimate selling price because quoted market prices for our assets or cash-generating units are not readily available. In determining the value in use, expected cash flows generated by the asset or the cash-generating unit are discounted to their present value, which requires significant judgment relating to level of sales volume, selling price and amount of operating costs. We use all readily available information in determining an amount that is a reasonable approximation of recoverable amount, including estimates based on reasonable and supportable assumptions and projections of reserve quantities, sales volume, selling price and amount of operating costs.

Impairment losses recognized for each of the three years ended December 31, 2006, 2007 and 2008 in our statement of income on long-lived assets are summarized as follows:

	Years ended December 31,		
	2006	2007	2008
	RMB	RMB (in millions)	RMB
Exploration and production	552	481	5,991
Refining	—	1,070	270
Marketing and distribution	23	1,237	709
Chemicals	250	318	1,511
Corporate and others	—	—	19
<b>Total</b>	<b>825</b>	<b>3,106</b>	<b>8,500</b>

#### *Depreciation*

Property, plant and equipment (other than oil and gas properties) are depreciated on a straight-line basis over the estimated useful lives of the assets, after taking into account the estimated residual value. We review the estimated useful lives of the assets regularly in order to determine the amount of depreciation expense to be recorded during any reporting period. The useful lives are based on our historical experience with similar assets and take into account anticipated technological changes. The depreciation expense for future periods is adjusted if there are significant changes from previous estimates. There have been no changes to the estimated useful lives and residual values during each of the three years ended December 31, 2006, 2007 and 2008.

#### *Impairment of accounts receivable for bad and doubtful debts*

We estimate impairment of accounts receivable for bad and doubtful debts resulting from the inability of our customers to make the required payments. We base our estimates on the aging of our accounts receivable balance, customer credit-worthiness, and historical write-off experience. If the financial condition of our customers were to deteriorate, actual write-offs would be higher than estimated. The changes in the impairment losses for bad and doubtful accounts are as follows:

	Years ended December 31,		
	2006	2007	2008
	RMB	RMB (in millions)	RMB
Balance as of January 1	3,151	3,345	2,882
Impairment losses recognized for the year	438	295	143
Reversal of impairment losses	(153)	(204)	(254)
Written off	(91)	(554)	(390)
<b>Balance as of December 31</b>	<b>3,345</b>	<b>2,882</b>	<b>2,381</b>

#### *Allowance for diminution in value of inventories*

If the costs of inventories fall below their net realizable values, an allowance for diminution in value of inventories is recognized. Net realizable value represents the estimated selling price in the ordinary course of business, less the estimated costs of completion and the estimated costs necessary to make the sale. We base the estimates on all available information, including the current market prices of the finished goods and raw materials, and historical operating costs. If the actual selling prices were to be lower or the costs of completion were to be higher than estimated, the actual allowance for diminution in value of inventories could be higher than estimated. Allowance for diminution in value of inventories is analyzed as follows:

	Years ended December 31,		
	2006	2007	2008
	RMB	RMB (in millions)	RMB
Balance as of January 1	897	871	4,572
Allowance for the year	419	3,962	8,527
Reversal of allowance on disposal	(317)	(131)	(64)
Written off	(128)	(130)	(4,096)
<b>Balance as of December 31</b>	<b>871</b>	<b>4,572</b>	<b>8,939</b>

#### **Recently Pronounced International Financial Reporting Standards**

Information relating to the recently pronounced IFRS is presented in Note 36 to the consolidated financial statements.

## Overview of Our Operations

We are the largest integrated petroleum and petrochemical company in China and one of the largest in Asia in terms of operating revenues. We engage in exploring for, developing and producing crude oil and natural gas, operating refineries and petrochemical facilities and marketing crude oil, natural gas, refined petroleum products and petrochemicals. We have reported our consolidated financial results according to the following four principal business segments and the corporate and others segment.

- *Exploration and Production Segment*, which consists of our activities related to exploring for and developing, producing and selling crude oil and natural gas;
- *Refining Segment*, which consists of purchasing crude oil from our exploration and production segment and from third parties, processing of crude oil into refined petroleum products, selling refined petroleum products principally to our marketing and distribution segment;
- *Marketing and Distribution Segment*, which consists of purchasing refined petroleum products from our refining segment and third parties, and marketing, selling and distributing refined petroleum products by wholesale to large customers and independent distributors and retail through our retail network;
- *Chemicals Segment*, which consists of purchasing chemical feedstock principally from the refining segment and producing, marketing, selling and distributing chemical products; and
- *Corporate and Others Segment*, which consists principally of trading activities of the import and export subsidiaries and our research and development activities.

## B. CONSOLIDATED RESULTS OF OPERATIONS

The following table sets forth certain income and expense items from our consolidated statements of income for the periods indicated.

	<b>Years Ended December 31,</b>		
	<b>2006</b>	<b>2007</b>	<b>2008</b>
	<b>RMB</b>	<b>RMB</b> <b>(in billions)</b>	<b>RMB</b>
Operating revenues			
Sales of goods	1,034.9	1,173.9	1,420.3
Other operating revenues	26.8	30.9	31.8
Total operating revenues	<u>1,061.7</u>	<u>1,204.8</u>	<u>1,452.1</u>
Other income	<u>5.2</u>	<u>4.9</u>	<u>50.3</u>
Operating expenses			
Purchased crude oil, products and operating supplies and expenses	(854.2)	(970.9)	(1,285.2)
Selling, general and administrative expenses	(37.5)	(37.9)	(46.2)
Depreciation, depletion and amortization	(33.6)	(43.3)	(45.8)
Exploration expenses, including dry holes	(8.0)	(11.1)	(8.3)
Personnel expenses	(21.0)	(22.7)	(23.3)
Taxes other than income tax	(29.3)	(34.3)	(56.8)
Other operating expenses, net	<u>(2.7)</u>	<u>(3.6)</u>	<u>(8.8)</u>
Total operating expenses	<u>(986.3)</u>	<u>(1,123.8)</u>	<u>(1,474.3)</u>
Operating income	<u>80.6</u>	<u>85.9</u>	<u>28.1</u>
Net finance costs	(5.8)	(8.1)	(4.8)
Income from investments	3.7	5.7	1.0
Earnings before income tax	78.5	83.5	24.3
Tax (expense)/benefit	<u>(23.5)</u>	<u>(24.8)</u>	<u>1.9</u>
Net income	<u>55.0</u>	<u>58.7</u>	<u>26.2</u>
Attributable to:			
Equity shareholders of the Company	53.6	56.5	29.8
Minority interests	<u>1.4</u>	<u>2.2</u>	<u>(3.6)</u>
	<u>55.0</u>	<u>58.7</u>	<u>26.2</u>

*Year Ended December 31, 2008 Compared with Year Ended December 31, 2007*

In 2008, our sales of goods, other operating revenues and other income were RMB 1,502.4 billion, representing an increase of 24.2% over 2007. Our operating income in 2008 was RMB 28.1 billion, representing a decrease of 67.2% over 2007. This was primarily due to the losses suffered by our refining segment due to the distortion of the correlation of domestic refined petroleum product prices and the international crude oil prices.

**Operating Revenues**

In 2008, our sales of goods and other operating revenues were RMB 1,452.1 billion, of which sales of goods were RMB 1,420.3 billion, representing an increase of 21.0% over 2007. The increase was primarily due to the increase in our sales of goods, which was the result of our increased average realized price and sales volume of refined oil products and the increase in volume of our trading business. In 2008, our other operating revenues were RMB 31.8 billion, representing an increase of 2.6% over 2007.

The following table sets forth our external sales volume, average realized prices and the respective rates of change from 2007 to 2008 for our major products:

	Average Realized Price		Rate of Change from 2007 to 2008 (%)	Sales Volume		Rate of Change from 2007 to 2008 (%)
	2007 (RMB)	2008 (RMB)		2007	2008	
Crude Oil	3,110 <sup>(1)</sup>	4,190 <sup>(1)</sup>	34.7	4.43 <sup>(2)</sup>	4.39 <sup>(2)</sup>	(0.8)
Natural Gas	811 <sup>(3)</sup>	911 <sup>(3)</sup>	12.3	5.82 <sup>(4)</sup>	6.28 <sup>(4)</sup>	8.0
Gasoline	5,408 <sup>(1)</sup>	6,409 <sup>(1)</sup>	18.5	35.18 <sup>(2)</sup>	37.73 <sup>(2)</sup>	7.3
Diesel	4,724 <sup>(1)</sup>	5,629 <sup>(1)</sup>	19.2	76.92 <sup>(2)</sup>	80.23 <sup>(2)</sup>	4.3
Kerosene	4,728 <sup>(1)</sup>	6,063 <sup>(1)</sup>	28.2	7.05 <sup>(2)</sup>	9.22 <sup>(2)</sup>	30.8
Basic chemical feedstock	6,200 <sup>(1)</sup>	6,261 <sup>(1)</sup>	1.0	10.23 <sup>(2)</sup>	9.64 <sup>(2)</sup>	(5.7)
Synthetic Resin	10,203 <sup>(1)</sup>	10,088 <sup>(1)</sup>	(1.1)	7.86 <sup>(2)</sup>	7.79 <sup>(2)</sup>	(0.9)
Synthetic Fiber	11,605 <sup>(1)</sup>	10,478 <sup>(1)</sup>	(9.7)	1.50 <sup>(2)</sup>	1.35 <sup>(2)</sup>	(9.9)
Synthetic Rubber	13,738 <sup>(1)</sup>	16,129 <sup>(1)</sup>	17.4	0.96 <sup>(2)</sup>	0.97 <sup>(2)</sup>	1.6
Synthetic Fiber Monomer and Polymer	9,109 <sup>(1)</sup>	8,224 <sup>(1)</sup>	(9.7)	4.05 <sup>(2)</sup>	3.71 <sup>(2)</sup>	(8.5)
Chemical fertilizer	1,659 <sup>(1)</sup>	1,729 <sup>(1)</sup>	4.2	1.57 <sup>(2)</sup>	1.66 <sup>(2)</sup>	5.3

- (1) per tonne
- (2) million tonnes
- (3) per thousand cubic meters
- (4) billion cubic meters

**Sales of crude oil and natural gas**

Most of the crude oil and a small portion of natural gas produced by us were internally used for refining and chemicals production and the remaining were sold to other customers. In 2008, the total revenue of crude oil, natural gas and other upstream products that were sold externally amounted to RMB 26.4 billion, representing an increase of 29.4% over 2007 and accounting for 1.8% of the sales of goods and other operating revenues. The increase was mainly due to the increase in the price of crude oil and the expansion of the Company's natural gas business.

### *Sales of refined petroleum products*

Our refining segment and marketing and distribution segment sell petroleum products (mainly consisting of gasoline, diesel and kerosene which are referred to as the refined oil products and other refined petroleum products) to external parties. In 2008, the external sales revenue of petroleum products by these two segments were RMB 932.5 billion, accounting for 62.1% of our sales of goods and other operating revenues, and representing an increase of 20.0% over 2007. This was primarily the result of the increased selling price of refined petroleum products, expansion of the sales volume of our petroleum products, and the optimizing of our sales structure. The sales revenue of gasoline, diesel and kerosene was RMB 749.3 billion, accounting for 80.4% of the total turnover of refined petroleum products, and representing an increase of 27.7% over 2007. The turnover of other refined petroleum products was RMB 183.2 billion, representing a decrease of 3.5% compared with 2007, and accounting for 19.6% of the total turnover of the refined petroleum products.

### *Sales of chemical products*

Our external sales revenue of chemical products was RMB 207.4 billion, accounting for 13.8% of our sales of goods and other operating revenues, and representing a decrease of 4.6% over 2007. This was primarily due to the general decrease in the selling prices and sales volume of our chemical products (other than synthetic rubber and chemical fertilizer).

### *Other income*

In 2008, we recognized grant income of RMB 50.3 billion compared to RMB 4.9 billion in 2007 for compensation of losses incurred due to the distortion of the correlation of domestic refined petroleum product prices and the international crude oil prices, and the measures we took to stabilize the supply in the PRC refined petroleum product market during the year. There are no unfulfilled conditions and other contingencies attached to the receipts of the grant. There is no assurance that we will continue to receive such grant in the future.

### *Operating expenses*

In 2008, our operating expenses were RMB 1,474.3 billion, representing an increase of 31.2% over 2007, among which:

**Purchased crude oil, products and operating supplies and expenses** were RMB 1,285.2 billion, representing an increase of 32.4% over 2007, accounting for 87.2% of the total operating expenses, of which:

Crude oil purchase expense was RMB 678.8 billion, representing an increase of 40.3% over 2007. This expense accounted for 46.0% of the total operating expense, representing an increase of 3 percentage points. With the rapid economic development in China and the expanded market demand, we increased the amount of crude oil that was purchased externally. In 2008, the total throughput of crude oil purchased externally reached 132.48 million tonnes (excluding the amounts processed for third parties), representing an increase of 6.9%. The average unit processing cost for crude oil purchased externally was RMB 5,124 per tonne, representing an increase of 31.3% over 2007.

In 2008, our other purchasing expenses reached RMB 606.4 billion, accounting for 41.1% of the total operating expenses, representing an increase of 24.5%. The increase was mainly due to the increased volume in our trading business and the increased cost for other outsourcing materials.

**Selling, general and administrative expenses** totaled were RMB 46.2 billion, representing an increase of 22.0% over 2007. This was primarily due to the RMB 3.4 billion increase in products delivering costs and other miscellaneous charges caused by the increased sales volume of our refined petroleum products as well as the increased unit transportation costs.

**Depreciation, depletion and amortization** was RMB 45.8 billion, representing an increase of 5.8% over 2007, mainly due to the increased depreciation resulted from our continuous capital expenditures on property, plant and equipment in recent years.

**Exploration expenses** reached RMB 8.3 billion, representing a decrease of 25.2%. This was mainly due to the decrease in upstream exploration activities over last year.

**Personnel expenses** were RMB 23.3 billion, representing an increase of 2.4% over 2007.

**Taxes other than income tax** were RMB 56.8 billion, representing an increase of 65.6% over 2007. The increase was mainly due to the increase of the special oil income levy in the amount of RMB 21.6 billion as a result of the high crude oil price in 2008, and the increase of the consumption tax in the amount of RMB 1.2 billion as a result of the increase in production volume.

**Other operating expenses** were RMB 8.8 billion in 2008 compared to RMB 3.6 billion in 2007, that are primarily due to impairment losses on long-lived assets, which were RMB 8.5 billion in 2008 compared with RMB 3.1 billion in 2007. The impairment losses were caused by the lower price of crude oil which led to the decrease in reserves estimated and higher production and development cost in certain field blocks.

#### ***Operating income***

In 2008, our operating income was RMB 28.1 billion, representing a decrease of 67.2% over 2007.

#### ***Net finance costs***

In 2008, our net finance costs were RMB 4.8 billion, representing a decrease of 41.0% over 2007. The decrease was mainly attributable to the increase in unrealized gain on embedded derivative component of convertible bonds by RMB 7.2 billion, partially offset by the increase in interest expense by RMB 4.0 billion.

#### ***Earnings before income taxes***

In 2008, our earnings before income tax were RMB 24.3 billion, representing a decrease of 70.9% over 2007.

#### ***Income taxes***

In 2008, we recognized an income tax benefit of RMB 1.9 billion compared to income tax expense of RMB 24.7 billion in 2007. See Note 10 to our consolidated financial statements for a reconciliation between the actual income tax benefit and the expected income tax expense at the applicable statutory tax rate.

#### ***Net income attributable to minority interests***

In 2008, loss for the year attributable to the minority interests of the Company was RMB 3.6 billion. This was primarily due to the losses incurred by our subsidiaries shared by the minority shareholders.

#### ***Net income attributable to equity shareholders of the Company***

In 2008, profit attributable to our equity shareholders was RMB 29.8 billion, representing a decrease of 47.3% compared with 2007.

#### ***Year Ended December 31, 2007 Compared with Year Ended December 31, 2006***

In 2007, our sales of goods, other operating revenues and other income were RMB 1,209.7 billion, and the operating income was RMB 85.9 billion, representing an increase of 13.4% and 6.4% over 2006, respectively. By seizing the favorable conditions provided by the steady growth of China's domestic economy, we proactively expanded the market, extended oil and gas resources, optimized crude oil mix for processing, and increased the production of chemical products and sales volume of refined oil products. In addition, we reinforced safe production, energy saving and cost efficiency. As a result of the forgoing factors, we achieved positive operating results in 2007.

#### ***Operating Revenues***

In 2007, our sales of goods and other operating revenues were RMB 1,204.8 billion, of which sales of goods was RMB 1,173.9 billion, representing an increase of 13.4% over 2006. These results were largely attributable to the increase in prices of domestic petroleum and petrochemical products and our efforts in expanding the sales volume of our petroleum and petrochemical products. In 2007, our other operating revenues were RMB 30.9 billion, representing an increase of 15.3% over 2006.

The following table sets forth our external sales volume, average realized prices and the respective rates of change from 2006 to 2007 for our major products:

	Average Realized Price		Rate of	Sales Volume		Rate of
	2006	2007	Change from	2006	2007	Change from
	(RMB)	(RMB)	2006 to 2007			2006 to 2007
			(%)			(%)
Crude Oil	3,210 <sup>(1)</sup>	3,110 <sup>(1)</sup>	(3.1)	4.03 <sup>(2)</sup>	4.43 <sup>(2)</sup>	10.0
Natural Gas	789 <sup>(3)</sup>	811 <sup>(3)</sup>	2.8	5.37 <sup>(4)</sup>	5.82 <sup>(4)</sup>	8.4
Gasoline	5,224 <sup>(1)</sup>	5,408 <sup>(1)</sup>	3.5	32.66 <sup>(2)</sup>	35.18 <sup>(2)</sup>	7.7
Diesel	4,469 <sup>(1)</sup>	4,724 <sup>(1)</sup>	5.7	72.96 <sup>(2)</sup>	76.92 <sup>(2)</sup>	5.4
Kerosene	4,525 <sup>(1)</sup>	4,728 <sup>(1)</sup>	4.5	5.46 <sup>(2)</sup>	7.05 <sup>(2)</sup>	29.0
Basic chemical Feedstock	5,831 <sup>(1)</sup>	6,200 <sup>(1)</sup>	6.3	9.69 <sup>(2)</sup>	10.23 <sup>(2)</sup>	5.5
Synthetic Resin	9,897 <sup>(1)</sup>	10,203 <sup>(1)</sup>	3.1	7.14 <sup>(2)</sup>	7.86 <sup>(2)</sup>	10.2
Synthetic Fiber	11,389 <sup>(1)</sup>	11,605 <sup>(1)</sup>	1.9	1.61 <sup>(2)</sup>	1.50 <sup>(2)</sup>	(6.9)
Synthetic Rubber	13,928 <sup>(1)</sup>	13,738 <sup>(1)</sup>	(1.4)	0.80 <sup>(2)</sup>	0.96 <sup>(2)</sup>	19.8
Synthetic Fiber Monomer and Polymer	8,821 <sup>(1)</sup>	9,109 <sup>(1)</sup>	3.3	3.68 <sup>(2)</sup>	4.05 <sup>(2)</sup>	10.0
Chemical fertilizer	1,650 <sup>(1)</sup>	1,659 <sup>(1)</sup>	0.5	1.65 <sup>(2)</sup>	1.57 <sup>(2)</sup>	(4.7)

- (1) per tonne  
(2) million tonnes  
(3) per thousand cubic meters  
(4) billion cubic meters

#### *Sales of crude oil and natural gas*

Most of the crude oil and a small portion of natural gas produced by us were internally used for refining and chemicals production and the remaining were sold to other customers. In 2007, the total revenue of crude oil, natural gas and other upstream products that were sold externally amounted to RMB 20.4 billion, representing an increase of 2.5% over 2006, accounting for 1.7% of the sales of goods and other operating revenues. The increase was mainly due to the increase in the sales volume of the crude oil and the expansion of our natural gas business.

#### *Sales of refined petroleum products*

Our refining segment and marketing and distribution segment sell petroleum products (mainly consisting of gasoline, diesel and kerosene which are referred to as the refined oil products and other refined petroleum products) to external parties. In 2007, the external sales revenue of petroleum products by these two segments were RMB 776.8 billion, accounting for 64.5% of our sales of goods and other operating revenues, and representing an increase of 10.5% over 2006. The result comes from the fact that we took advantage of the high price of petroleum products, expanded the sales volume of the petroleum products, optimized the sales structure and expanded the markets of other refined petroleum products. The sales revenue of gasoline, diesel and kerosene was RMB 586.9 billion, accounting for 75.6% of the total turnover of refined petroleum products, and representing an increase of 12.6% over 2006. The turnover of other refined petroleum products was RMB 189.9 billion, representing an increase of 6.7% compared with 2006, and accounting for 24.4% of the total turnover of petroleum products.

#### *Sales of chemical products*

Our external sales revenue of chemical products was RMB 217.5 billion, accounting for 18.1% of our sales of goods and other operating revenues, and representing an increase of 11.0% over 2006. This was mainly attributed to the fact that we took advantage of the high price level of the chemical products and expanded our sales volume accordingly.

### *Other income*

In 2007, we recognized grant income of RMB 4.9 billion compared to RMB 5.2 billion in 2006 for compensation of losses incurred due to the distortion of the correlation of domestic refined petroleum product prices and the crude oil prices, and the measures taken by the Group to stabilize the supply in the PRC refined petroleum product market during the year. There are no unfulfilled conditions and other contingencies attached to the receipts of this grant. There is no assurance that the Group will continue to receive such grant in the future.

### *Operating expenses*

In 2007, our operating expenses were RMB 1,123.8 billion, representing an increase of 13.9% over 2006, among which:

**Purchased crude oil, products and operating supplies and expenses** were RMB 970.9 billion, representing an increase of 13.7% over 2006, accounting for 86.4% of the total operating expenses, of which:

Crude oil purchase expense was RMB 483.9 billion, representing an increase of 8.9% over 2006. This expense accounted for 43.1% of the total operating expense, representing a decrease of 2 percentage points. With the rapid economic development in China and the expanded market demand, we increased our throughput of crude oil that was purchased externally. In 2007, the total throughput of crude oil purchased externally reached 123.98 million tonnes (excluding the amounts processed for third parties), representing an increase of 4.8%. The average cost for crude oil purchased externally was RMB 3,903 per tonne, representing an increase of 3.9% over 2006.

In 2007, our other purchasing expenses reached RMB 487.0 billion, accounting for 43.3% of the total operating expenses, representing an increase of 18.9%. The increase was mainly due to the increased costs of refined oil products and chemical raw materials purchased externally.

**Selling, general and administrative expenses** totaled were RMB 37.9 billion, representing an increase of 0.9% over 2006.

**Depreciation, depletion and amortization** was RMB 43.3 billion, representing an increase of 29.1%, mainly due to the increased depreciation resulted from our continuous capital expenditures on property, plant and equipment in recent two years.

**Exploration expenses** reached RMB 11.1 billion, representing an increase of 39.1%. The increase was mainly due to our increased efforts on exploration and forward looking study in the Southern marine facies blocks in the northeast and the west of Sichuan Province.

**Personnel expenses** were RMB 22.7 billion, representing an increase of 8.5%.

**Taxes other than income tax** were RMB 34.3 billion, representing an increase of 17.0% over 2006. The increase was mainly due to the increase of the special oil income levy on crude oil income in the amount of RMB 2.5 billion, and the increase of the consumption tax levied on naphtha and other refined petroleum products in the amount of RMB 1.6 billion. In addition, city construction tax and education surcharge increased by RMB 0.8 billion.

**Other operating expenses** were RMB 3.2 billion, representing an increase of 30.1%. The increase was mainly due to the increase in impairment loss on long-lived assets, which increased by RMB 2.3 billion compared with 2006.

### *Operating income*

In 2007, our operating income was RMB 85.9 billion, representing an increase of 6.5% over 2006.

### *Net finance costs*

In 2007, our net finance costs were RMB 8.1 billion, representing an increase of 39.4% over 2006. The increase was mainly attributed to the RMB 3.2 billion unrealized loss on embedded derivative component of convertible bonds.



### Earnings before income taxes

In 2007, our earnings before income tax reached RMB 83.5 billion, representing an increase of 6.3% over 2006.

### Income taxes

In 2007, our effective income tax rate was 29.6% compared with 29.9 % for 2006. See Note 10 to our consolidated financial statements for a reconciliation between the actual income tax expense and the expected income tax at applicable statutory tax rates.

### Net income attributable to minority interests

In 2007, profit for the year attributable to our minority interests reached RMB 2.2 billion, representing an increase of 57.0%. The increase was mainly due to increased profit from two of our consolidated subsidiaries Shanghai Petrochemical Company Limited and Fujian Petrochemical Company Limited.

### Net income attributable to equity shareholders of the Company

In 2007, profit attributable to our equity shareholders was RMB 56.5 billion, representing an increase of 5.5% over 2006.

## C. DISCUSSIONS ON RESULTS OF SEGMENT OPERATIONS

We divide our operations into four business segments (exploration and production segment, refining segment, marketing and distribution segment and chemicals segment) and corporate and others. Unless otherwise specified, the inter-segment transactions have not been eliminated in the financial data discussed in this section. In addition, the operating revenue data of each segment have included the “other operating revenues” of the segment.

The following table sets forth the operating revenues by each segment, the contribution of external sales and inter-segment sales as a percentage of operating revenues before elimination of inter-segment sales, and the contribution of external sales as a percentage of consolidated operating revenues (i.e. after elimination of inter-segment sales) for the periods indicated.

	Years Ended December 31,			As a Percentage of Consolidated Operating Revenues Before Elimination of Inter-segment Sales		As a Percentage of Consolidated Operating Revenues After Elimination of Inter-segment Sales	
	2006	2007	2008	2007	2008	2007	2008
	RMB	RMB (in billions)	RMB	(%)	(%)	(%)	(%)
Exploration and Production							
External sales <sup>(1)</sup>	34.1	38.2	45.1	1.8	1.6	3.2	3.1
Inter-segment sales	109.1	107.5	151.4	5.0	5.4		
Total operating revenue	143.2	145.7	196.5	6.8	7.0		
Refining							
External sales <sup>(1)</sup>	119.5	122.2	134.6	5.7	4.8	10.1	9.3
Inter-segment sales	477.8	534.7	684.0	24.7	24.5		
Total operating revenue	597.3	656.9	818.6	30.4	29.3		
Marketing and distribution							
External sales <sup>(1)</sup>	588.7	660.0	804.0	30.5	28.7	54.8	55.4
Inter-segment sales	4.8	2.8	3.2	0.1	0.1		
Total operating revenue	593.5	662.8	807.2	30.6	28.8		
Chemicals							
External sales <sup>(1)</sup>	202.6	224.7	213.6	10.4	7.6	18.7	14.7
Inter-segment sales	12.3	16.0	27.5	0.7	1.0		

Total operating revenue	<u>214.9</u>	<u>240.7</u>	<u>241.1</u>	<u>11.1</u>	<u>8.6</u>		
Corporate and others							
External sales <sup>(1)</sup>	116.8	159.7	254.8	7.4	9.1	13.2	17.5
Inter-segment sales	<u>145.3</u>	<u>297.1</u>	<u>480.0</u>	<u>13.7</u>	<u>17.2</u>		
Total operating revenue	<u>262.1</u>	<u>456.8</u>	<u>734.8</u>	<u>21.1</u>	<u>26.3</u>		
Total operating revenue before inter-segment eliminations	1,811.0	2,162.9	2,798.2	<u>100.0</u>	<u>100.0</u>		
Elimination of inter-segment sales	<u>(749.3)</u>	<u>(958.1)</u>	<u>(1,346.1)</u>				
Consolidated operating revenues	<u>1,061.7</u>	<u>1,204.8</u>	<u>1,452.1</u>			<u>100.0</u>	<u>100.0</u>

(1) include other operating revenues. See Note 32 to the consolidated financial statements for other operating revenues of each of our operating segments.

The following table sets forth the operating revenues, operating expenses and operating income/(loss) by each segment before elimination of the inter-segment transactions for the periods indicated, and the rate of changes from 2006 to 2008.

	Years Ended December 31,			Rate of Change from 2007 to 2008 (%)
	2006	2007	2008	
Exploration and Production		(RMB in billions)		
Total operating revenues	143.2	145.7	196.5	34.9
Total operating expenses	<u>(80.0)</u>	<u>(96.9)</u>	<u>(129.9)</u>	34.1
Total operating income	<u>63.2</u>	<u>48.8</u>	<u>66.6</u>	<u>36.5</u>
Refining				
Total operating revenues	597.3	656.9	818.6	24.6
Other income	<u>5.2</u>	<u>1.9</u>	<u>40.5</u>	2,031.6
Total operating expenses	<u>(628.2)</u>	<u>(669.3)</u>	<u>(920.6)</u>	37.5
Total operating loss	<u>(25.7)</u>	<u>(10.5)</u>	<u>(61.5)</u>	- -
Marketing and distribution				
Total operating revenues	593.5	662.8	807.2	21.8
Other income	<u>- -</u>	<u>2.9</u>	<u>9.8</u>	237.9
Total operating expenses	<u>(563.3)</u>	<u>(630.0)</u>	<u>(778.8)</u>	23.6
Total operating income	<u>30.2</u>	<u>35.7</u>	<u>38.2</u>	7.0
Chemicals				
Total operating revenues	214.9	240.7	241.1	0.2
Total operating expenses	<u>(200.5)</u>	<u>(227.4)</u>	<u>(254.2)</u>	11.8
Total operating income/(loss)	<u>14.4</u>	<u>13.3</u>	<u>(13.1)</u>	- -
Corporate and others				
Total operating revenues	262.1	456.8	734.8	60.8
Total operating expenses	<u>(263.6)</u>	<u>(458.4)</u>	<u>(736.8)</u>	60.7
Total operating loss	<u>(1.5)</u>	<u>(1.4)</u>	<u>(2.0)</u>	- -

### ***Exploration and Production Segment***

Most of the crude oil and a small portion of the natural gas produced by the exploration and production segment were used for our refining and chemicals operations. Most of our natural gas and a small portion of crude oil were sold to other customers.

#### *Year Ended December 31, 2008 Compared with Year Ended December 31, 2007*

In 2008, the operating revenues of this segment were RMB 196.5 billion, representing an increase of 34.9% over 2007. The increase was mainly attributable to the increase in the sales volume and sales price of crude oil and natural gas.

In 2008, this segment sold 39.41 million tonnes of crude oil and 6.9 billion cubic meters of natural gas, representing an increase of 1.4% and 9.5% respectively over 2007. The average realized price of crude oil was RMB 4,269 per tonne, representing an increase of 37.9%. The average realized price of natural gas was RMB 941 per thousand cubic meters, representing an increase of 14.4% over 2007.

In 2008, the operating expenses of this segment were RMB 129.9 billion, representing an increase of 34.1% over 2007. The increase was mainly due to the following reasons:

- The purchased raw materials, products and operating supplies and expenses increased by RMB 2 billion, which was primarily caused by the increased price of raw materials and fuels.
- The impairment losses increased by RMB 5.4 billion over 2007, attributable to the lower in price of crude oil which led to the decrease in reserves estimated and higher production and development cost in certain field blocks.
- The increase in depreciation, depletion and amortization amounted to RMB 3.9 billion was primarily due to the continuous investment in oil and gas assets.
- Special oil income levy increased by RMB 21.6 billion, primarily due to the high crude oil price in 2008.
- The exploration expense decreased by RMB 2.8 billion over 2007, due to the decrease of upstream exploration activities over last year.

In light of the high crude oil price in 2008, we developed more marginal oil reserves to increase oil and gas production. Water and electricity charges associated with oil and gas production increased due to our development of marginal oil reserves.

In 2008, the operating income of the segment was RMB 66.6 billion, representing an increase of 36.5% over 2007.

*Year Ended December 31, 2007 Compared with Year Ended December 31, 2006*

In 2007, the operating revenue of this segment were RMB 145.7 billion, representing an increase of 1.7% over 2006. The increase was mainly attributable to the increase in the sales volume of crude oil and the increase both in the sales volume and sales price of natural gas.

In 2007, this segment sold 38.85 million tonnes of crude oil and 6.3 billion cubic meters of natural gas, representing an increase of 2.4% and 10.2% respectively over 2006. The average realized price of crude oil was RMB 3,095 per tonne, representing a decrease of 3.1%. The average realized price of natural gas was RMB 823 per thousand cubic meters, representing an increase of 3.6% over 2006.

In 2007, the operating expenses of this segment were RMB 96.9 billion, representing an increase of 21.1% over 2006. The increase was mainly due to the following reasons:

- The exploration expense (including dry hole cost) increased by RMB 3.1 billion over 2006. The increase was mainly attributable to the increased efforts on exploration and forward looking study in the Southern marine facies blocks in the northeast and the west of Sichuan Province.
- The increase of RMB 5.3 billion in depreciation, depletion and amortization, which was mainly due to the increase in depreciation and depletion of the oil and gas assets.
- Special oil income levy on crude oil increased by RMB 2.5 billion over 2006.
- Other operating expenses increased by RMB 3.6 billion over 2006. The increase was mainly due to the increase in cost of materials as a result of the increase in sales of these materials.

In 2007, the operating income of the segment was RMB 48.8 billion, representing a decrease of 22.8% over 2006.

### Refining Segment

Business activities of the refining segment consist of purchasing crude oil from third parties or from our exploration and production segment, processing crude oil into refined petroleum products, selling gasoline, diesel and kerosene to the marketing and distribution segment, selling a portion of chemical feedstock to our chemicals segment, and selling other refined petroleum products to the domestic and overseas customers.

#### Year Ended December 31, 2008 Compared with Year Ended December 31, 2007

In 2008, the operating revenues of this segment were RMB 818.6 billion, representing an increase of 24.6% over 2007. The increase was mainly attributable to the increase in the price and sales volume of each refined petroleum products.

The table below sets forth sales volume and average realized prices by product for 2007 and 2008, as well as the percentage changes in sales volume and average realized prices for the periods shown.

	Sales volume		Rate of change from	Average Realized prices		Rate of change from
	2007	2008	2007 to 2008	2007	2008	2007 to 2008
	(million tonnes)		(%)	(RMB per tonne)		(%)
Gasoline	23.97	28.17	17.5	4,641	5,587	20.4
Diesel	61.54	67.78	10.1	4,057	4,934	21.6
Chemical feedstock	25.51	23.47	(8.0)	4,985	5,982	20.0
Kerosene and other refined petroleum products	42.20	41.36	(2.0)	3,884	4,388	13.0

In 2008, the sales revenues of gasoline by the segment were RMB 157.4 billion, representing an increase of 41.5% over 2007 and accounting for 18.3% of this segment's operating revenues. The sales revenues of diesel by the segment were RMB 334.4 billion, representing an increase of 34.0% over 2007 and accounting for 38.9% of this segment's operating revenues. In 2008, the sales revenues of chemical feedstock by the segment were RMB 140.4 billion, representing an increase of 10.4% over 2007 and accounting for 16.3% of this segment's operating revenues. The sales revenues of refined petroleum products other than gasoline, diesel and chemical feedstock were RMB 181.5 billion, representing an increase of 10.7% over 2007 and accounting for 21.1% of this segment's operating revenues.

In 2008, this segment's operating expenses were RMB 920.6 billion, representing an increase of 37.5% over 2007. The increase was mainly attributable to the increase of raw materials prices.

The average cost of crude oil processed was RMB 5,004 per tonne, representing an increase of 33.0% over 2007. Refining throughput were 163.26 million tonnes (excluding the volume processed for third parties), representing an increase of 5.1% over 2007. In 2008, the total costs of crude oil processed were RMB 817 billion, representing an increase of 39.8%, and accounting for 88.7% of the segment's operating expenses, up by 1.4 percentage points over 2007.

In 2008, due to the high international crude oil price and the PRC government's tight control over refined petroleum products prices, our refining segment incurred significant losses. After recognizing the subsidy of RMB 40.5 billion received by this segment, the operating losses for the segment was RMB 61.5 billion, representing an increase in loss of RMB 51.1 billion over 2007.

#### Year Ended December 31, 2007 Compared with Year Ended December 31, 2006

In 2007, the operating revenues of this segment were RMB 656.9 billion, representing an increase of 10.0% over 2006. The increase was mainly attributable to the increase in the price and sales volume of each refined petroleum products.

The table below sets forth sales volume and average realized prices by product for 2006 and 2007, as well as the percentage changes in sales volume and average realized prices for the periods shown.

	Sales volume		Rate of change from	Average Realized prices		Rate of change from
	2006	2007	2006 to 2007	2006	2007	2006 to 2007
	(million tonnes)		(%)	(RMB per tonne)		(%)
Gasoline	22.94	23.97	4.5	4,499	4,641	3.2
Diesel	59.71	61.54	3.1	3,873	4,057	4.8
Light Chemical feedstock	25.40	25.51	0.4	4,395	4,985	13.4
Other refined petroleum products	39.68	42.20	6.4	3,690	3,884	5.3

In 2007, the sales revenues of gasoline by the segment were RMB 111.2 billion, representing an increase of 7.8% over 2006 and accounting for 16.9% of this segment's operating revenues.

The sales revenues of diesel by the segment were RMB 249.6 billion, representing an increase of 8.0% over 2006 and accounting for 37.9% of this segment's operating revenues.

The sales revenues of chemical feedstock by the segment were RMB 127.2 billion, representing an increase of 13.9% over 2006 and accounting for 19.3% of this segment's operating revenues. The increase in the sales revenues of chemical feedstock was higher than the increase in the sales revenues of gasoline and diesel, which was mainly due to the fact that the extent of increase in the price of the chemical feedstock is greater than the extent of increase in the price of the gasoline and diesel oil.

In 2007, the sales revenues of refined petroleum products other than gasoline, diesel and chemical feedstock were RMB 163.9 billion, representing an increase of 11.9% over 2006 and accounting for 24.9% of this segment's operating revenues. In 2007, this segment's operating expenses were RMB 669.3 billion, representing an increase of 6.6% over the year of 2006. The increase was mainly attributable to the increase in refining throughput and crude oil price as well as the allowance for diminution in value of certain imported crude oil.

In 2007, the average cost of crude oil processed was RMB 3,762 per tonne, representing an increase of 2.2% over 2006. Refining throughput were 155.27 million tonnes (excluding the volume processed for third parties), representing an increase of 4.5% over 2006. In 2007, the total costs of crude oil processed were RMB 584.2 billion, representing an increase of 6.8%, and accounting for 87.3% of the segment's operating expenses, up by 0.2 percentage points over 2006. In 2007, due to the high international crude oil prices, and the government's tight control over refined oil products' price, our refinery segment incurred losses and an allowance for diminution in value of inventories of RMB 4.0 billion was recorded. This segment incurred an operating loss of RMB 10.5 billion, after the receipt of a cash grant of RMB 1.9 billion, representing a year-on-year loss decrease of RMB 15.2 billion.

### ***Marketing and Distribution Segment***

The business activities of the marketing and distribution segment include purchasing refined oil products from our refining segment and third parties, making wholesale and direct sales to domestic customers, and retail of the refined oil products through the segment's retail distribution network, as well as providing related services.

#### *Year Ended December 31, 2008 Compared with Year Ended December 31, 2007*

In 2008, the operating revenues of this segment were RMB 807.2 billion, up by 21.8% over 2007. The increase was mainly attributable our adjustment of sales policy and expansion in sales volume.

In 2008, the operating revenues from sales of gasoline and diesel were RMB 695.7 billion, accounting for 85.2% of the operating revenues of this segment. The percentage of retail in the total sales volume of gasoline and diesel increased to 66.5% from 63.8% in 2007. The percentage of direct sales in the total sales volume increased to 21.1% from 17.5% in 2007. The percentage of wholesale volume in the total sales volume of gasoline and diesel decreased from 18.7% in 2007 to 12.4% in 2008.

The following table sets forth the sales volumes, average realized prices and the respective rates of changes of the four major product categories in 2007 and 2008 in different forms of sales channels.

	Sales Volume		Rate of Change from	Average Realized Prices		Rate of Change from
	2007	2008	2007 to 2008	2007	2008	2007 to 2008
	(million tonnes)		(%)	(RMB per tonne)		(%)
Gasoline	35.12	37.71	7.4	5,410	6,410	18.5
Retail sale	26.73	29.83	11.6	5,542	6,524	17.7
Direct sale	2.61	2.61	0.1	5,036	6,013	19.4
Wholesale	5.79	5.27	(9.0)	4,967	5,964	20.1
Diesel	77.29	80.65	4.3	4,723	5,629	19.2
Retail sale	44.99	48.89	8.7	4,832	5,704	18.0
Direct sale	17.03	22.31	31.0	4,742	5,561	17.3
Wholesale	15.26	9.44	(38.1)	4,381	5,402	23.3
Kerosene including jet fuel	7.01	9.19	31.1	4,729	6,065	28.3
Fuel Oil	13.16	11.46	(12.9)	2,923	3,692	26.3

In 2008, the subsidy income recognized by the segment was RMB 9.8 billion.

In 2008, the operating expenses of the segment were RMB 778.8 billion, representing an increase of 23.6% compared with 2007. The increase was mainly due to the increase in the purchasing cost of refined oil products.

In 2008, the operating income of the segment was RMB 38.2 billion, representing an increase of 6.9% over 2007.

*Year Ended December 31, 2007 Compared with Year Ended December 31, 2006*

In 2007, the operating revenues of this segment were RMB 662.8 billion, up by 11.7% over 2006. The increase was mainly attributable to the improvements in sales mix and the increased proportion of the retail business and the increased domestic demand for the refined oil products.

In 2007, the operating revenues from sales of gasoline and diesel were RMB 555.1 billion, accounting for 83.4% of the operating revenues of this segment. The percentage of retail in the total sales volume of gasoline and diesel increased from 63.4% in 2006 to 63.8% in 2007, representing an increase of 0.4 percentage points. The percentage of direct sales in the total sales volume increased from 17.0% in 2006 to 17.5% in 2007, representing an increase of 0.5 percentage points. The percentage of wholesale volume in the total sales volume of gasoline and diesel decreased from 19.6% in 2006 to 18.7% in 2007, representing a decrease of 0.9 percentage points.

The following table sets forth the sales volumes, average realized prices and the respective rate of changes of the four major product categories in 2006 and 2007 in different forms of sales channels.

	Sales Volume		Rate of Change from	Average Realized Prices		Rate of Change from
	2006	2007	2006 to 2007	2006	2007	2006 to 2007
	(million tonnes)		(%)	(RMB per tonne)		(%)
Gasoline	32.72	35.12	7.4	5,224	5,410	3.6
Retail sale	23.89	26.73	11.9	5,350	5,542	3.6
Direct sale	2.81	2.61	(7.1)	4,922	5,036	2.3
Wholesale	6.02	5.79	(3.9)	4,867	4,967	2.1
Diesel	73.69	77.29	4.9	4,466	4,723	5.8
Retail sale	43.53	44.99	3.4	4,527	4,832	6.7
Direct sale	15.31	17.03	11.3	4,599	4,742	3.1
Wholesale	14.86	15.26	2.7	4,152	4,381	5.5
Kerosene including jet fuel	5.40	7.01	29.8	4,524	4,729	4.5
Fuel Oil	15.07	13.16	(12.7)	2,989	2,923	(2.2)

In 2007, the operating expenses of the segment were RMB 630.0 billion, representing an increase of 11.8% compared with that of 2006. The increase was mainly due to the increase in the purchasing cost of refined oil products.

In 2007, the operating income, after the receipt of a cash grant of RMB 2.9 billion, of the segment was RMB 35.7 billion, representing an increase of 18.2%.

### Chemicals Segment

The business activities of the chemicals segment include purchasing chemical feedstock from our refining segment and third parties, producing, marketing and distributing petrochemical and inorganic chemical products.

*Year Ended December 31, 2008 Compared with Year Ended December 31, 2007*

In 2008, operating revenues of this segment were RMB 241.1 billion, representing an increase of 0.2% over the year of 2007.

In 2008, the sales revenues of our six major categories of chemical products (namely basic organic chemicals, monomers and polymers for synthetic fiber, synthetic resin, synthetic fiber, synthetic rubber and chemical fertilizer) totaled approximately RMB 222.6 billion, representing a decrease of 2.1% over 2007, and accounting for 92.3% of the operating revenues of this segment.

The following table sets forth the sales volume, average realized price and the respective rates of changes for each of these six categories of chemical products of this segment from 2007 to 2008.

	Sales Volumes		Rate of Change from 2007 to 2008	Average Realized Prices		Rate of Change from 2007 to 2008
	2007	2008		2007	2008	
	(million tonnes)		(%)	(RMB per tonne)		(%)
Basic organic chemicals	12.89	12.59	(2.3)	5,870	6,303	7.4
Synthetic resins	7.96	7.87	(1.2)	10,163	10,075	(0.9)
Synthetic fiber monomers and polymers	4.09	3.76	(8.1)	9,116	8,237	(9.6)
Synthetic rubber	0.98	0.99	1.2	13,721	16,163	17.8
Synthetic fiber	1.50	1.35	(9.9)	11,605	10,478	(9.7)
Chemical fertilizer	1.60	1.66	3.8	1,657	1,729	4.3

In 2008, operating expenses of the chemicals segment were RMB 254.2 billion, representing an increase of 11.8% over 2007. This was primarily due to the increase in the prices of feedstock and ancillary materials, which, together, contributed to an increase of RMB 26.2 billion in operating expenses over 2007.

In 2008, operating loss of the chemicals segment was RMB 13.1 billion, compared to the operating income of RMB 13.3 billion in 2007.

*Year Ended December 31, 2007 Compared with Year Ended December 31, 2006*

In 2007, operating revenues of this segment were RMB 240.7 billion, representing an increase of 12.0% over the year of 2006. The increase was primarily due to the increase in sales volume and prices of major chemical products.

In 2007, the sales revenues of our six major categories of chemical products (namely basic organic chemicals, monomers and polymers for synthetic fiber, synthetic resin, synthetic fiber, synthetic rubber and chemical fertilizer) totaled approximately RMB 227.3 billion, representing an increase of 12.5% over 2006, and accounting for 94.4% of the operating revenues of this segment.

The following table sets forth the sales volume, average realized price and the respective rate of changes for each of these six categories of chemical products of this segment from 2006 to 2007.

	Sales Volumes		Rate of Change from 2006 to 2007	Average Realized Prices		Rate of Change from 2006 to 2007
	2006	2007		2006	2007	
	(million tonnes)		(%)	(RMB per tonne)		(%)
Basic organic chemicals	11.57	12.89	11.4	5,649	5,870	3.9
Synthetic resins	7.25	7.96	9.8	9,842	10,163	3.3
Synthetic rubber	0.83	0.98	17.3	13,885	13,721	(1.2)
Synthetic fiber	1.61	1.50	(7.0)	11,390	11,605	1.9
Synthetic fiber monomers and polymers	3.71	4.09	10.2	8,814	9,116	3.4
Chemical fertilizer	1.65	1.60	(3.3)	1,660	1,657	(0.2)

In 2007, operating expenses of the chemicals segment were RMB 227.4 billion, representing an increase of 13.4% over 2006. The increase was primarily due to:

Increase in the consumption of feedstock and ancillary materials as well as the increase in their prices, together, contributed to an increase of RMB25.8 billion over 2006.

Because of increases in production volume of the chemical products, fuel and energy costs increased by approximately RMB 1.1 billion compared with 2006.

In 2007, operating income of the chemicals segment was RMB 13.3 billion, representing a decrease of RMB 1.1 billion over 2006.

#### ***Corporate and others***

The business activities of corporate and others mainly consist of the import and export operations, international trading, research and development activities of us and managerial activities of our headquarters.

#### *Year Ended December 31, 2008 Compared with Year Ended December 31, 2007*

In 2008, the operating revenues generated from corporate and others were RMB 734.8 billion, representing an increase of 60.8% over 2007. The increase was mainly due to the increase in the trading volume of crude oil and refined oil products.

In 2008, the operating expenses of this segment were RMB 736.8 billion, representing an increase of 60.8% over 2007. This increase was mainly due to the increase in the purchasing costs of the trading business in line the increase in its operating revenue.

In 2008, the operating loss of this segment was RMB 2 billion, compared to the operating loss of RMB 1.5 billion in 2007.

#### *Year Ended December 31, 2007 Compared with Year Ended December 31, 2006*

In 2007, the operating revenues generated from corporate and others were RMB 456.8 billion, representing an increase of 74.3% over 2006. The increase was mainly due to the high crude oil price as well as the trading volume of crude oil and refined oil products.

In 2007, the operating expenses of this segment were RMB 458.4 billion, representing an increase of 73.9% over 2006. This increase was mainly due to the increase in the purchasing costs of its trading business associated with the increase in its operating revenue.

In 2007, the operating loss of this segment was RMB 1.4 billion, representing a decrease of RMB 100 million compared with 2006.

### **D. LIQUIDITY AND CAPITAL RESOURCES**

Our primary sources of funding have been cash provided by our operating activities, short-term and long-term loans. Our primary uses of cash have been for working capital, capital expenditures and repayment of short-term and long-term loans. We arrange and negotiate financing with financial institutions to finance our capital resource requirement, and maintain a certain level of standby credit facilities to reduce liquidity risk. We believe that our current cash on hand, expected cash flows from operations and available standby credit facilities from financial institutions will be sufficient to meet our working capital requirements and repay our short term debts and obligations when they become due.

The following table sets forth a summary of our consolidated cash flows for the years ended December 31, 2007 and 2008.



Cash flow data	For the Years Ended	
	December 31,	
	2007	2008
	(RMB in billions)	
Net cash generated from operating activities	119.6	67.7
Net cash used in investing activities	(113.6)	(110.2)
Net cash (used in)/generated from financing activities	(5.3)	41.8
Net increase/(decrease) in cash and cash equivalents	0.7	(0.7)

In 2008, net cash generated from operating activities was RMB 67.7 billion, representing a decrease of 43.4% over 2007. The decrease was mainly due to the lower profitability in 2008, primarily caused by the losses suffered by our refining segment due to the distortion of the correlation of domestic refined petroleum product prices and the international crude oil prices.

Net cash used in investment activities in 2008 was RMB 110.2 billion, which was mainly due to the capital expenditure of RMB 99.6 billion and exploratory wells expenditure of RMB 8.4 billion.

Net cash from financing activities was RMB 41.8 billion in 2008. This was mainly due to proceeds of issuance of bonds with detachable warrants, net of issuance costs, of RMB 29.9 billion, proceeds of issuance of corporate bonds of RMB 15.0 billion, proceeds from bank and other loans of RMB 1,147.3 billion, repayments of bank and other loans of RMB 1,125.3 billion, and the dividend paid of RMB 12.6 billion.

#### Contractual Obligations and Commercial Commitments

The following table sets forth our obligations and commitments to make future payments under contracts and commercial commitments as of December 31, 2008.

	As of December 31, 2008				
	Total	Payment due by period			
		less than 1 year	1-3 years	4-5 years	After 5 years
	(RMB in millions)				
<b>Contractual obligations<sup>(1)</sup></b>					
Short-term debt	81,005	81,005	--	--	--
Long-term debt	173,044	23,609	21,752	22,109	105,574
<b>Total contractual obligations</b>	<b>254,049</b>	<b>104,614</b>	<b>21,752</b>	<b>22,109</b>	<b>105,574</b>
<b>Other commercial commitments</b>					
Operating lease commitments	178,478	6,066	11,405	11,114	149,893
Capital commitments	168,873	120,050	48,823	--	--
Exploration and production licenses	951	123	138	39	651
Guarantees <sup>(2)</sup>	11,404	11,404	--	--	--
<b>Total commercial commitments</b>	<b>359,706</b>	<b>137,643</b>	<b>60,366</b>	<b>11,153</b>	<b>150,544</b>

(1) Contractual obligations include the contractual obligations relating to interest payments.

(2) Guarantee is not limited by time, therefore specific payment due period is not applicable. As of December 31, 2008, we have not entered into any off-balance sheet arrangements other than guarantees given to banks in respect of banking facilities granted to certain parties. As of December 31, 2008, the maximum amount of potential future payments under the guarantees was RMB 11,404 million. See Note 29 to the consolidated financial statements for further information of the guarantees.

#### Historical and Planned Capital Expenditure

The following table sets forth our capital expenditure by segment for the years ended December 31, 2006, 2007 and 2008 and the capital expenditure in each segment as a percentage of our total capital expenditure for such year.

	2006		2007		2008		Total	
	RMB	Percent	RMB	Percent	RMB	Percent	RMB	Percent
	(in billions, except percentage data)							
Exploration and production	35.2	42	54.5	50	57.7	54	147.4	49
Refining	22.6	27	22.8	21	12.5	12	57.9	19

Marketing and distribution	11.3	13	12.5	11	14.1	13	37.9	13
Chemicals	12.6	15	16.2	15	20.6	19	49.4	16
Corporate	2.2	3	3.3	3	2.4	2	7.9	3
Total	<u>83.9</u>	<u>100</u>	<u>109.3</u>	<u>100</u>	<u>107.3</u>	<u>100</u>	<u>300.5</u>	<u>100</u>

In 2008, our total capital expenditure was RMB 107.3 billion, among which,

- The capital expenditure for our exploration and development was RMB 57.7 billion. The exploration and development in Puguang Gas Field, construction of the purification plant and pipeline and market development progressed smoothly. We continued to develop the Tahe oil field in 2008. The newly-added production capacity of crude oil is 5.8 million tonnes per annum and the newly-added production capacity of natural gas is 1.33 billion cubic meters per annum.
- The capital expenditure for our refining segment was RMB 12.5 billion. Qingdao Refinery and Caofeidian crude oil dock project were completed and commenced operation in 2008. Currently undergoing projects include the revamping project in Gaoqiao to improve adaptability for low quality crude and the projects in Wuhan and Luoyang to upgrade products quality. We also started the Tahe revamping project to process heavy crude oil.
- The capital expenditure for our marketing and distribution segment was RMB 14.1 billion. We expanded our selling network by constructing, acquiring or renovating the service stations and storage facilities. We added 720 new service stations into our retail network during 2008.
- The capital expenditure for our chemicals segment was RMB 20.6 billion. Ethylene projects in Fujian, Tianjin and Zhenhai are progressing smoothly. Jinling paraxylene expansion project, Yangzi butadiene expansion project and Yanshan butyl rubber expansion project have been completed and commenced operation.
- The capital expenditure for our corporate and others segment amounted to RMB 2.4 billion, which was primarily spent on the information system improvement.

In 2009, we will continue to focus our investment on profitable and core projects. We will strictly follow management control policies and procedures regarding the investment activities, and carefully arrange and manage our constructions projects. The total planned capital expenditure for 2009 is RMB 111.8 billion, as indicated below by segment:

- Exploration and development segment: RMB 55.0 billion. We will continue to invest in Sichuan-East China Gas Project. We will also invest in Tahe and Shengli oil fields and Puguang and Erdos natural gas fields to expand the production capacity.
- Refining segment: RMB 16.8 billion. We will invest to improve the auxiliary and supporting functions in our refining segments, such as oil quality upgrade systems and our transportation, delivery and storage network.
- Marketing and distributing segment: RMB 12.0 billion. We will continue to expand and upgrade our refined oil products sales network, including construction or acquisition of oil/gas stations in highway areas or other strategic locations.
- Chemical segment: RMB 26.4 billion. We will invest primarily in our Tianjin integrated refinery and chemical project and Zhenhai ethylene project.
- Corporate and others segment: RMB 1.6 billion.

### Consumer Price Index

According to the data provided by the National Bureau of Statistics, the consumer price index in the PRC increased by 5.9% in 2008, compared with 4.8% in 2007 and 1.5% in 2006. According to China's official analysis, the

inflation in the PRC during 2008 was due to the rise in food and commodity prices. Inflation has not had a significant impact on our results of operations in recent years.

## ITEM 6. DIRECTORS, SENIOR MANAGEMENT AND EMPLOYEES

### A. DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT

#### Directors

The table and discussion below set forth certain information concerning our directors. The current term for all our directors is three years, which will expire in May 2009.

<u>Name</u>	<u>Age</u>	<u>Positions with Sinopec Corp.</u>
Su Shulin	47	Chairman
Zhou Yuan	61	Vice Chairman
Wang Tianpu	46	Director, President
Zhang Jianhua	44	Director, Senior Vice President
Wang Zhigang	51	Director, Senior Vice President
Dai Houliang	45	Director, Senior Vice President, CFO
Liu Zhongli	74	Independent Non-executive Director
Shi Wanpeng	71	Independent Non-executive Director
Li Deshui	64	Independent Non-executive Director
Yao Zhongmin	56	Director
Fan Yifei	45	Director

*Su Shulin*, 47, Chairman of the Board of Directors of Sinopec Corp. and President of Sinopec Group Company. He received his Bachelor Degree from Daqing Petroleum Institute in July 1983, and obtained a Master Degree from Harbin Engineering University in March 1999. He is a professor level senior engineer. From March 1996 to January 1997, Mr. Su acted as Assistant to the Director of CNPC Daqing Petroleum Administration Bureau. From January to November 1997, Mr. Su served as Head of the No. 1 Oil and Gas Development Department and Assistant to the Director of CNPC Daqing Petroleum Administration Bureau. From November 1997 to January 1999, Mr. Su was Deputy Director and member of the Party Committee of CNPC Daqing Petroleum Administration Bureau. From January to September 1999, Mr. Su was Director and Vice Secretary to the Party Committee of CNPC Daqing Petroleum Administration Bureau. From September 1999 to August 2000, Mr. Su Shulin was served as Vice President of PetroChina Company Limited and Chairman, General Manager and Secretary to the Party Committee of Daqing Oilfield Company Limited and Vice Secretary to Party Committee of CNPC Daqing Petroleum Administration Bureau. From August 2000 to March 2001, Mr. Su acted as Deputy General Manager and member of the Party Committee of China National Petroleum Corporation, Vice President of PetroChina Company Limited, Chairman, General Manager and Secretary to the Party Committee of Daqing Oilfield Company Limited as well as Vice Secretary to the Party Committee of CNPC Daqing Petroleum Administration Bureau. From March 2001 to December 2002, Mr. Su served as Deputy General Manager and member of the Party Committee of China National Petroleum Corporation, Vice President of PetroChina Company Limited and Chairman and General Manager of Daqing Oilfield Company Limited. From December 2002 to December 2003, Mr. Su acted as Deputy General Manager and member of the Party Committee of China National Petroleum Corporation, Director and Senior Vice President of PetroChina Company Limited as well as Chairman and General Manager of Daqing Oilfield Company Limited. From December 2003 to September 2006, Mr. Su acted as Deputy General Manager and member of the Party Committee of China National Petroleum Corporation, Director and Senior Vice President of PetroChina Company Limited. From September 2006 to October 2006, Mr. Su was elected as a member of the Standing Committee of the provincial Party Committee of Liaoning Province. In October 2006, Mr. Su was appointed as a member of the Standing Committee and Head of the Organization Department of Liaoning Provincial Committee. In June 2007 he was appointed as President and Secretary of the Party Leadership Group of Sinopec Group Company. Mr. Su was elected as Director and Chairman on Third Session of the Board of Directors of Sinopec Corp. in August 2007.

*Zhou Yuan*, 61, Vice Chairman of the Board of Directors of Sinopec Corp. and Vice President of the Sinopec Group Company. Mr. Zhou graduated from East China Petroleum Institute specializing in petroleum geology in September 1975. He is a senior economist. He has extensive experience in the management of petroleum and

petrochemical and government entities. From April 1986 to March 1989, he was the Deputy Secretary of the Party Committee of Xinjiang Petroleum Administration Bureau (Kelamayi City) as well as the Secretary of the Party Committee of South Xinjiang Petroleum Exploration Company. From March 1989 to August 1990, he was the Vice Commander, Deputy Secretary of the Party Committee and Secretary of the Disciplinary Committee of Talimu Exploration and Development Headquarter. From August 1990 to January 1992, he was the Deputy Secretary of the Party Committee of Xinjiang Petroleum Administration Bureau (Kelamayi City) and the Secretary of Politics & Law Committee. From January 1992 to December 1993, he served as Vice Minister of Organization Department of the Party Committee of Xinjiang Autonomous Region. From December 1993 to January 1998, he served as a member of the Standing Committee of Discipline Committee and the Deputy Minister of the Party Committee of the Organisation Department of Xinjiang Autonomous Region. From January 1998 to August 1999, he was a member of the Standing Committee of the Disciplinary Committee of the Xinjiang Autonomous Region and the Secretary of the Party Committee of Yili Autonomous District. From August 1999 to November 1999, he was a member of the Standing Committee of the Party Committee of the Xinjiang Autonomous Region and the Secretary of the Party Committee of Yili Autonomous District. From November 1999 to July 2004, he was a member of Standing Committee of the Party Committee of Xinjiang Autonomous Region and Minister of the Organization Department of the Party Committee of Xinjiang Autonomous Region. Since July 2004, he has been the Vice President of Sinopec Group Company. In March 2008, he was elected as a member of the 11th NPC Environment and Resources Protection Committee. In October 2008, he was appointed as Senior Advisor of Sinopec Group Company. Mr. Zhou was elected as Director and Vice Chairman of the Third Session of the Board of Directors of Sinopec Corp in May 2006.

*Wang Tianpu*, 46, Director of the Board of Directors and President of Sinopec Corp. Mr. Wang graduated from Qingdao Chemical Institute in July 1985 majoring in basic organic chemistry. He obtained his MBA degree in Dalian University of Science & Technology in July 1996 and Ph.D. degree in Zhejiang University in August 2003 majoring in chemical engineering. He is a professor level senior engineer and well-experienced in the production and management in petrochemical industry. From March 1999 to February 2000, Mr. Wang was Vice President of Qilu Petrochemical Company of Sinopec Group. From February 2000 to September 2000, he was Vice President of Sinopec Corp Qilu Company. From September 2000 to August 2001, he was President of Sinopec Corp Qilu Company. Mr. Wang was Vice President of Sinopec Corp from August 2001 to April 2003 and was Senior Vice President of Sinopec Corp from April 2003 to March 2005. Mr. Wang has been President of Sinopec Corp since March 2005; Mr. Wang was elected as Director of the Third Session of the Board of Directors of Sinopec Corp. in May 2006 and he is President of Sinopec Corp.

*Zhang Jianhua*, 44, Director of the Board of Directors and Senior Vice President of Sinopec Corp. Mr. Zhang graduated from East China Chemical Institute in July 1986 majoring in petroleum refining, and obtained a master's degree from East China University of Science and Technology in December 2000 majoring in chemical engineering. He is a professor level senior engineer. From April 1999 to February 2000, Mr. Zhang was Vice President of Shanghai Gaoqiao Petrochemical Company of Sinopec Group. From February 2000 to September 2000, he was Vice President of Sinopec Corp. Shanghai Gaoqiao Company. He was President of Sinopec Corp. Shanghai Gaoqiao Company from September 2000 to June 2003. Mr. Zhang served as Vice President of Sinopec Corp. from April 2003 to March 2005. He was also the Director General of Sinopec Production & Operation Management Dept. from November 2003 to November 2005. He has been Senior Vice President of Sinopec Corp. since March 2005; Mr. Zhang was elected as Director of the Third Session of the Board of Directors of Sinopec Corp. in May 2006 and has been Senior Vice President of Sinopec Corp.

*Wang Zhigang*, 51, Director of the Board of Directors of Sinopec Corp. and Senior Vice President of Sinopec Corp. Mr. Wang graduated from East China Petroleum Institute in January 1982, majoring in oil production, and then obtained a master's degree from University of Petroleum in June 2000, majoring in oil and gas development engineering. He obtained a Ph.D. degree from Geology and Geo-physics Research Institute of the China Academy of Sciences in September 2003 majoring in geology. He is a professor level senior engineer. From February 2000 to June 2000, he was Vice President of Sinopec Shengli Oilfield Company Limited. From June 2000 to December 2001, Mr. Wang served as Director and President of Sinopec Shengli Oilfield Company Limited. He was appointed as honorary Deputy Director-General of the Economic and Trade Committee of Ningxia Hui Autonomous Region from November 2001 to May 2003. He was Vice President of Sinopec Corp. from April 2003 to March 2005. He was also the Director General of Sinopec Exploration and Production Dept. since June 2003 to November 2005. He has been Senior Vice President of Sinopec Corp. since March 2005; Mr. Wang was elected as Director of the Third Session of the Board of Directors of Sinopec Corp. in May 2006 and has been Senior Vice President of Sinopec Corp.

*Dai Houliang*, 45, Director of the Board of Directors of Sinopec Corp., Senior Vice President and Chief Finance Officer of Sinopec Corp. Mr. Dai graduated from Jiangsu Chemical Institute in July 1985, specializing in organic chemical engineering. From September 1997 to July 1999, he participated in the MBA training program in

Nanjing University. He is a professor level senior engineer. He was Deputy Manager of Sinopec Yangzi Petrochemical Company from December 1997 to April 1998. He served as Director and Deputy General Manager of Sinopec Yangzi Petrochemical Co., Ltd. from April 1998 to July 2002. He was Vice Chairman and General Manager of Sinopec Yangzi Petrochemical Co., Ltd. and Director of Sinopec Yangzi Petrochemical Company from July 2002 to December 2003. He was Chairman and President of Sinopec Yangzi Petrochemical Co., Ltd. and Chairman of Sinopec Yangzi Petrochemical Company from December 2003 to September 2005. He also served as Chairman of BASF-YPC Company Limited from December 2004 to October 2006. He has been the Deputy CFO of Sinopec Corp. from September 2005 to May 2006. Mr. Dai has been Vice President of Sinopec Corp. from November 2005 to May 2006. In May 2006, he was elected as Director of the Third Session of the Board of Directors, Senior Vice President and CFO of Sinopec Corp.

*Liu Zhongli*, 74, Independent Non-Executive Director of Sinopec Corp. He graduated from the training course of the Training Department of Central Communist Party School (undergraduate course) in July 1982. He is a senior economist engaging in treasury finance administration and government work for a long time, and has extensive experience in macro-economics, financial and treasury administration. He was working in Commerce Bureau of Heilongjiang Province in 1952 and in Planning Commission of Heilongjiang Provincial Government in 1963. He had served as Deputy Division Director of the General Affairs Office of Planning Commission of Heilongjiang Provincial Government and Deputy Secretary General of Planning Commission of Heilongjiang Provincial Government since September 1973. He was Deputy Director General of Planning Commission of Heilongjiang Provincial Government and a member of Party Committee of Planning Commission of Heilongjiang Provincial Government from July 1982 to May 1983. From May 1983 to May 1985, he was Director General of Planning Commission (Planning & Economics Department) of Heilongjiang Provincial Government and Secretary of Party Committee of Planning Commission (Planning & Economics Department) of Heilongjiang Provincial Government. He served as Deputy Governor of Heilongjiang Province from May 1985 to January 1988. He was Vice Minister of the Ministry of Finance and Deputy Secretary of Party Committee of the Ministry of Finance from February 1988 to July 1990. He served as Deputy Secretary General of the State Council and Deputy Secretary of Party Committee of the State Council from July 1990 to September 1992. From September 1992 to March 1998, he was Minister of the Ministry of Finance and Secretary of Party Committee of the Ministry of Finance and, from February 1994, concurrently Director-General of State Administration of Taxation. From March 1998 to November 2000, he was Head of Economic System Reform Office of the State Council and Secretary of Party Committee of the Economic System Reform Office of the State Council. From August 2000 to March 2003, he was Chairman of National Council for Social Security Fund and Secretary of Party Committee of the National Council for Social Security Fund. He has been a member of the Standing Committee of the Tenth Session of the Chinese People's Political Consultative Conference (CPPCC) and Director-General of the Economics Committee of CPPCC since March 2003. Since October 2004, he has concurrently been Chairman of the Chinese Institute of Certified Public Accountants. Mr. Liu was elected as Independent Non-Executive Director of the Third Session of the Board of Directors of Sinopec Corp. in May 2006.

*Shi Wanpeng*, 71, Independent Non-Executive Director of Sinopec Corp., a member of the Standing Committee of the National Committee of the Tenth session of the Chinese People's Political Consultative Conference and Deputy Director of its Economic Committee. Mr. Shi graduated from Northern Jiaotong University in August 1960 specializing in railway transportation administration. He is a professor level senior engineer. He has long been engaged in economic management work, and has extensive experience in macro-economic management. From January 1983 to January 1987, he served as Deputy Director of the Transport Bureau of the State Economic Commission. From January 1987 to May 1988, he was the Director of the Economic and Technical Co-operation Bureau of the State Economic Commission. From May 1988 to July 1991, he was Director of the Production and Dispatch Bureau of the State Planning Commission. From July 1991 to July 1992, he served as Deputy Secretary General of the Production Office of the State Council. From July 1992 to April 1993, he served as Deputy Director of the Economic and Trade Office of the State Council. From April 1993 to July 1997, he was Vice Minister of the State Economic and Trade Commission. From July 1997 to March 1998, he was Chairman (minister level) of the China Textiles Association. From March 1998 to February 2002, he served as Vice Minister of the State Economic and Trade Commission. Since January 2003, he has been Chairman of China Packaging Federation. He has been a member of the Standing Committee of the National Committee of the Tenth session of the Chinese People's Political Consultative Conference and Deputy Director of its Economic Committee since March 2003. Mr. Shi was elected as Independent Non-executive Director of the Second Session of the Board of Directors of Sinopec Corp. from April 2003 to May 2006; he was elected as Independent Non-Executive Director of the Third Session of the Board of Directors of Sinopec Corp. in May 2006.

*Li Deshui*, 64, Independent Non-Executive Director of Sinopec Corp. Mr. Li graduated from university in 1967. He is a senior engineer, researcher, part-time professor of the Economics School of Peking University and the Economics School of Renmin University of China. After graduating from university, he was assigned to work at

Maanshan Steel Company and has acted as Workshop Section Head and Dispatch Head. In 1977 he worked at the Planning Institute of the Metallurgy Department. In 1984 he worked at the Raw Materials Bureau of the State Planning Commission. In 1988 he acted as Deputy Division Director of the First Industrial Planning Division of the Long-term Planning Department of the State Planning Commission. In 1989 he was Division Director of the First Industrial Planning Division of the Long-term Planning Department and Division Director of the First Industrial Planning Division of the Long-term Planning and Industrial Policy Department. In 1992 he acted as Deputy Director of the National Economy Comprehensive Department of the State Planning Commission. In May 1996 he was Director of the National Economy Comprehensive Department of the State Planning Commission. In November 1996, he acted as Vice Mayor of Chongqing in Sichuan Province. In March 1997 he acted as Vice Mayor of Chongqing Municipality. In November 1999 he worked as Deputy Director of the Research Office of the State Council and a member of the Party Committee. In April 2002, he served as Secretary of the Party Committee and Deputy General Manager of China International Engineering Consultancy Company. In March 2003 he served as Secretary of the Party Committee and Head of the State Statistics Bureau, a member of the Monetary Policy Committee of the People's Bank of China and Chairman of China Statistics Institute. In March 2005, he was elected as Vice Chairman of the Thirty-sixth Statistics Commission of the United Nations. In March 2005 he served as a member of the Tenth Session of the Chinese People's Political Consultative Conference. In April 2006 he acted as a member of the Economic Commission. In March 2006, he was the consultant of the State Statistics Bureau. Mr. Li was elected as Independent Non-Executive Director of the Third Session of the Board of Directors of Sinopec Corp. in May 2006.

*Yao Zhongmin*, 56, Director of Sinopec Corp. Mr. Yao graduated from Dongbei University of Finance & Economics in September 1977 specializing in Infrastructure Finance & Credit and graduated as postgraduate from Zhongnan University of Finance & Economics in December 1996 specializing in Investment Economics with a master's degree. He is a senior Economist. Mr. Yao has worked for a long time in financial investment management related work and has extensive experience in finance investment management. From May 1985 to June 1989, he was a member of the Party Committee of China Construction Bank Henan Branch and its Vice-Chairman. From June 1989 to June 1992, he was leading the work of China Construction Bank Henan Branch, and was Deputy Secretary of the Party Committee and Vice Chairman of the bank. From June 1992 to April 1993, he served as Secretary of the Party Committee and Chairman of China Construction Bank Henan Branch. He served as Vice Governor of Henan Province from April 1993 to January 1994. From January 1994 to March 1998, he was a member of the Party Committee of China Development Bank and its Vice Chairman and Chairman of the Disciplinary Supervision Committee. From March 1998 to June 1998, he was Deputy Secretary of the Party Committee of China Development Bank and its Vice Chairman and Chairman of the Disciplinary and Investigation Committee. From June 1998, he was the Deputy Secretary of the Party Committee of China Development Bank and its Vice-Chairman. In December 2008, he was reappointed as the Vice Chairman of the Party Committee of China Development Bank and Chairman of the Disciplinary Supervision Committee. Mr. Yao was elected as Director of the Third Session of the Board of Directors of Sinopec Corp. in May 2006.

*Fan Yifei*, 45, Director of Sinopec Corp. Mr. Fan graduated from the treasury and finance department of Renmin University of China in July 1993 and obtained a doctoral degree in economics; He obtained a master's degree in international economics from Columbia University in 2002. He is a senior accountant. From June 1993 to September 1994, he was the Assistant to the General Manager and Manager of the Planning and Finance Department of the Trust Investment Company of China Construction Bank successively. From September 1994 to July 1996, he served as Vice General Manager of the Capital Planning Department of China Construction Bank. He was the General Manager of the Finance and Accounting Department of China Construction Bank from July 1996 to January 1998. He was the General Manager of the Planning and Finance Department of China Construction Bank from January 1998 to February 2000. Mr. Fan served as the Assistant to the Governor of China Construction Bank from February 2000 to June 2005, during which he enriched his experience by participating in the Three Gorges project, and also acted as the Assistant to the General Manager of China Changjiang Power Co., Ltd. In June 2005, Mr. Fan was appointed as Deputy Governor of China Construction Bank. Mr. Fan acted as Director of the Second Session of the Board of Directors of Sinopec Corp. from April 2003 to May 2006; he was elected as Director of the Third Session of the Board of Directors of Sinopec Corp. in May 2006.

## **Supervisors**

The table and discussion below set forth certain information concerning our supervisors. The current term of our supervisors is three years, which will expire in May 2009.

<b>Name</b>	<b>Age</b>	<b>Position with the Company</b>
Wang Zuoran	58	Chairman of the Board of Supervisors
Zhang Youcai	67	Vice Chairman, Independent Supervisor
Kang Xianzhang	60	Supervisor
Zou Huiping	48	Supervisor
Li Yonggui	68	Independent Supervisor
Su Wensheng	52	Employee Representative Supervisor
Zhang Jitian	61	Employee Representative Supervisor
Cui Guoqi	55	Employee Representative Supervisor
Li Zhonghua	57	Employee Representative Supervisor

*Wang Zuoran*, 58, Chairman of the Supervisory Board of Sinopec Corp. Mr. Wang graduated from Shandong Economic Administration Institute in September 1994 specializing in economic administration. Mr. Wang is a professor level senior economist and has extensive experience in the management of petroleum industry. From October 1994 to February 2000, Mr. Wang served as Deputy Director and Party Secretary of Shengli Petroleum Administration Bureau. From February 2000 to July 2001, Mr. Wang was the Assistant to the President of Sinopec Group Company. Mr. Wang has been Director of Disciplinary Supervision Committee of Sinopec Group Company since July 2001. Mr. Wang served as Supervisor of the First Session of the Supervisory Board of Sinopec Corp. from February 2000 to April 2003. From April 2003 to May 2006, Mr. Wang served as Supervisor and Chairman of the Second Session of the Supervisory Board of Sinopec Corp.; he was elected as Supervisor and Chairman of the Third Session of the Supervisory Board of Sinopec Corp. in May 2006.

*Zhang Youcai*, 67, Independent Supervisor and Vice Chairman of the Supervisory Board of Sinopec Corp. Mr. Zhang graduated from Nanjing Industrial University in August 1965 majoring in inorganic chemistry. He is a professor and has long been engaged in business administration, financial management and government affairs, and has extensive experience in industrial, economic, financial and accounting management. From January 1968 to August 1980, he served as a technician, Vice-President, Deputy Secretary of the Party Committee and President of Nantong Chemical Fertilizer Plant. From August 1980 to January 1982, he was Deputy Director-General and member of the Party Committee of the Industrial Bureau of Nantong Region. From January 1982 to February 1983, he served as Deputy Director - General of Planning Commission of Nantong Region. From February 1983 to November 1989, he served as Deputy Mayor, Deputy Secretary of the Party Committee and Mayor of Nantong City. He was Vice Minister and member of the Party Committee of Ministry of Finance from December 1989 to July 2002 (from May 1994 to March 1998, he served concurrently as Director-General of State-owned Assets Administration Bureau). He has been Chairman of the Chinese Institute of Chief Accountants since November 2002. He has been a member of the Standing Committee of the Tenth National People's Congress (NPC) and Deputy Director of its Financial and Economic Committee of NPC from March 2003. Mr. Zhang served as an Independent Non-Executive Director of the Second Session of Board of Directors of Sinopec Corp. from April 2003 to May 2006; he was elected as Independent Supervisor and Vice Chairman of the Third Session of the Supervisory Board of Sinopec Corp. in May 2006.

*Kang Xianzhang*, 60, Supervisor of Sinopec Corp. Mr. Kang graduated from the Correspondence Teaching Department of the Party School of the Beijing Municipal Party Committee in March 1988 specializing in ideology politics (undergraduate course). He also graduated from the Correspondence Teaching College of the Party School of the Central Committee of the Communist Party of China in December 1992 specializing in party and political affairs management (bachelor course). He is a senior political engineer. From June 1995 to August 1996, he was the Deputy Director of the Organization Department of the Communist Party Committee of the Tibet Autonomous Region. From August 1996 to May 1997, he was a senior researcher of the deputy director level in the Cadre Allocation Bureau of the Organization Department of the Central Committee of the Communist Party of China. He acted as the Deputy Secretary of the Communist Party Committee of the Coal Scientific Research Institute of the Ministry of Coal Industry from May 1997 to October 1998. From October 1998 to May 1999, he was Supervisor of the deputy director level in the Discipline Inspection Group and the Supervisory Bureau of Sinopec Group Company, and acted as a Deputy Director of the Supervisory Bureau of the same company from May 1999 to March 2001. He was the Deputy Director of the Supervisory Department of Sinopec Corp. from February 2000 to March 2001. He has been a Deputy Head of the Discipline Inspection Group of the Leading Party Group and Director of the Supervisory Bureau of Sinopec Group Company, as well as Director of the Supervisory Department of Sinopec Corp. from March 2001 to August 2008. Mr. Kang served as Supervisor of the Second Session of the Supervisory Board of Sinopec Corp. from April 2003 to May 2006; he was elected as Supervisor of the Third Session of the Supervisory Board of Sinopec Corp. in May 2006.

*Zou Huiping*, 48, Supervisor of Sinopec Corp. Mr. Zou graduated from Jiangxi Institute of Finance and Economics in July 1986 specializing in trade economics. He is a professor level senior accountant. From November 1998 to February 2000, he served as Chief Accountant of Sinopec Group Guangzhou Petrochemical Company. From February 2000 to December 2001, he was Deputy Director General of Financial Assets Department of Sinopec Group

Company. From December 2001 to March 2006, he was Deputy Director General of Finance Planning Department of Sinopec Group Company. In March 2006, he was Director General of Financial Assets Department of Sinopec Assets Management Co., Ltd. Since March 2006, he has been Director General of Audit Department of Sinopec Corp. Mr. Zou was elected as Supervisor of the Third Session of the Supervisory Board of Sinopec Corp. in May 2006.

*Li Yonggui*, 68, Independent Supervisor of Sinopec Corp. Mr. Li graduated from Shandong Institute of Finance and Economics in July 1965, majoring in treasury finance. He is a senior economist and CPA, and has long been engaged in tax management with extensive management experience in taxation. From February 1985 to December 1988, he was Deputy Director-General of Taxation Bureau of Ministry of Finance. He served as Chief Economist of State Administration of Taxation from December 1988 to April 1991. From April 1991 to February 1995, he served as Deputy Director-General of State Administration of Taxation. He was Chief Economist of State Administration of Taxation from February 1995 to September 2001. Mr. Li has been Chairman of Chinese Association of Certified Public Taxation Experts since April 2000. He has served as Vice Chairman of Chinese Association of Certified Accountants since November 2004. In July 2008, he was appointed as consultant of Chinese Association of Certified Public Taxation Experts. Mr. Li served as Independent Supervisor of the Second Session of Supervisory Board of Sinopec Corp. from April 2003 to May 2006; he was elected as Independent Supervisor of the Third Session of Supervisory Board of Sinopec Corp. in May 2006.

*Su Wensheng*, 52, Employee Representative Supervisor of Sinopec Corp. Mr. Su graduated from the General Section of Tsinghua University in December 1980 majoring in environmental engineering. He obtained a master's degree in management science and engineering from Petroleum University (Beijing) in June 2000. He is a senior engineer. From September 1986 to November 1996, he was Deputy Secretary of Party Committee and Secretary of Disciplinary Committee of Beijing Designing Institute of the former Sinopec Group Company. From November 1996 to December 1998, he was Secretary of Party Committee of Beijing Designing Institute. Mr. Su has been Director-General of Ideology & Politics Department and Deputy Secretary of the Affiliated Party Committee of Sinopec Group Company since December 1998. He has been Managing Deputy Secretary of the Party Working Committee of the Western New Region Exploration Headquarter of Sinopec Group since December 2001. He was appointed as the Party Secretary and Vice Chairman of Beijing Yanshan Petrochemical Corporation in October 2007. Mr. Su served as an Employee Representative Supervisor of the Second Session of Supervisory Board of Sinopec Corp. from April 2003 to May 2006; he was elected as Employee Representative Supervisor of the Third Session of Supervisory Board of Sinopec Corp. in May 2006.

*Zhang Jitian*, 61, Employee Representative Supervisor of Sinopec Corp. Mr. Zhang graduated from Hohhot Transportation Institute in July 1968 specializing in road and bridge construction, and he also graduated from Sinopec Management Institute in July 1986 specializing in enterprise management (undergraduate course). He is a senior political engineer. From August 1996 to December 1998, he was Deputy Director of Personnel and Educational Department of the former Sinopec Group Company; from December 1998 to September 2005, he was Deputy Director of Personnel and Educational Department of Sinopec Group Company; he has been Deputy Director (remunerate as Director) of Personnel Department of Sinopec Corp. from September 2005 to August 2008. Mr. Zhang was elected as Employee Representative Supervisor of the Third Session of Supervisory Board of Sinopec Corp. in May 2006.

*Cui Guoqi*, 55, Employee Representative Supervisor of Sinopec Corp. Mr. Cui graduated from the Correspondence Teaching College of Renmin University of China in December 1985 majoring in industrial business management. In January 1997, he obtained a MBA degree from the Business Management School of Renmin University of China. He is a professor level senior political engineer. Mr. Cui has served as Director and Trade Union Chairman of Sinopec Yanshan Petrochemical Company since February 2000. He served as a member of the Executive Committee of All China Federation of Trade Unions in December 2000, and a member of the Standing Committee of the National Committee of the Union of Chinese Energy and Chemical Industries since December 2001. He was Deputy Secretary of Party Committee of Sinopec Yanshan Petrochemical Company from August 2005 to November 2006. Mr. Cui has been the Deputy Secretary (remunerate as Secretary) of Party Committee of Sinopec Yanshan Petrochemical Company since November 2006. He was appointed as President, Deputy Secretary of Party Committee and Director General of Headquarter Services Department of Sinopec Baichuan Economical and Trading Company. Mr. Cui served as Employee Representative Supervisor of the Second Session of Supervisory Board of Sinopec Corp. from April 2003 to May 2006; he was elected as Employee Representative Supervisor of the Third Session of Supervisory Board of Sinopec Corp. in May 2006.

*Li Zhonghua*, 57, Employee Representative Supervisor of Sinopec Corp. Mr. Li graduated from the Correspondence Teaching Department of the Party School of Shengli Oilfield in June 1996 specializing in party and political affairs management (undergraduate course). He also graduated from the Correspondence Teaching College of the Party School of Shandong Provincial Party Committee in December 1998 specializing in economic management.



He is a professor level senior political engineer. From March 1995 to January 2004, he had been Secretary of Party Committee and Vice General Manager of No. 2 Drilling Company of Shengli Petroleum Administration Bureau; Secretary of Party Committee, General Manager of Offshore Drilling Company of Shengli Petroleum Administration Bureau; and Deputy Party Secretary, General Manager of the Yellow River Drilling Company of Shengli Petroleum Administration Bureau successively. From January 2004 to November 2004, he was Deputy Chief Engineer, Deputy Secretary of Party Committee and General Manager of the Yellow River Drilling Company of Shengli Petroleum Administration Bureau; he has been member of the Standing Committee of Party Committee and Chairman of the Trade Union of Shengli Petroleum Administration Bureau since November 2004. He was Deputy Secretary of Party Committee of Shengli Petroleum Administration Bureau since April 2006. Mr. Li was elected as Employee Representative Supervisor of the Third Session of Supervisory Board of Sinopec Corp. in May 2006.

#### **Other Executive Officers**

<b>Name</b>	<b>Age</b>	<b>Positions with Sinopec Corp.</b>
Cai Xiyou	47	Senior Vice President
Zhang Kehua	55	Vice President
Zhang Haichao	51	Vice President
Jiao Fangzheng	46	Vice President
Chen Ge	46	Secretary of the Board of Directors

*Cai Xiyou*, 47, Senior Vice President of Sinopec Corp. Mr. Cai graduated from Fushun Petroleum Institute in August 1982 majoring in petroleum refining automation, and obtained a MBA degree from China Industry and Science Dalian Training Center in October 1990. He is a senior economist. From June 1995 to May 1996, he was Deputy General Manager of Jinzhou Petrochemical Company of the former Sinopec Group Company. From May 1996 to December 1998, he was Deputy General Manager of Dalian Western Pacific Petrochemical Co., Ltd (WEPEC). From December 1998 to June 2001, he was Deputy General Manager of Sinopec Sales Co., Ltd, and from June 2001 to December 2001, he was Executive Deputy Manager of Sinopec Sales Co., Ltd. He has been Director and General Manager of China International United Petrochemical Company Limited (UNIPEC) from December 2001 to December 2005. He was Vice President of Sinopec Corp. from April 2003 to November 2005. Mr. Cai has been Senior Vice President of Sinopec Corp. since November 2005.

*Zhang Kehua*, 55, Vice President of Sinopec Corp. Mr. Zhang graduated from Shanghai Chemical Engineering University in January 1980 majoring in chemical and mechanical engineering. He is a senior engineer and had his master's degree from University of Petroleum majoring in management science and engineering in December 2000. He was Deputy Manager of No. 3 Construction Company of the former Sinopec Group Company from February 1994 to April 1996. From April 1996 to December 1998, he was Deputy Director General (Deputy Manager of Sinopec Engineering Incorporation) of the Engineering Department of the former Sinopec Group Company. He was Deputy Director General of the former Engineering Department of Sinopec Group Company from December 1998 to December 2001 and was Deputy Director General of Engineering Department of Sinopec Group Company from December 2001 to September 2002. Mr. Zhang was Director General of Engineering Department of Sinopec Group Company from September 2002 to October 2004. Mr. Zhang has served as the Assistant to the President of Sinopec Group Company and Director General of Engineering Department since October 2004. Mr. Zhang has been Vice President of Sinopec Corp. since May 2006. From June 2007 to Present, he has been Director General of Engineering Dept. of Sinopec Corp.

*Zhang Haichao*, 51, Vice President of Sinopec Corp. Mr. Zhang graduated from Zhoushan Commercial and Technical School in December 1979, specializing in oil storage and transportation. He also graduated from Jilin Petrochemical Institute in July 1985 specializing in recycling of lubricating oil. From January 2001 to June 2002, he participated in the business administration program at Macau Science & Technology University. He is an economist. He served as Deputy General Manager of Zhejiang Petroleum Company from March 1998 to September 1999. He served as General Manager of Zhejiang Petroleum Company from September 1999 to February 2000, and has served as Manager of Sinopec Zhejiang Petroleum Company from February 2000 to September 2005. He has been Chairman of Sinopec-BP Zhejiang Petroleum Sales Co., Ltd. since April 2004. He was Secretary of the Party Committee, Vice Chairman and Deputy General Manager of Sinopec Sales Co., Ltd. from October 2004 to November 2005. He was Secretary of Party Committee, Chairman and General Manager of Sinopec Sales Co., Ltd. from November 2005 to June 2006. He has been Chairman and General Manager of Sinopec Sales Co., Ltd. since June 2006. From December 2008, he acted as Chairman and President of Sinopec Sales Co., Ltd. He served as Employee Representative Supervisor of the Second Session of the Supervisory Board of Sinopec Corp. from April 2003 to November 2005. Mr. Zhang has been Vice President of Sinopec Corp. since November 2005.

*Jiao Fangzheng*, 46, Vice President of Sinopec Corp. Mr. Jiao won his bachelor's degree in petroleum exploration and won his doctoral degree in natural gas engineering from Southwest Petroleum Institute respectively in July 1983 and November 2000. Mr. Jiao is a professor level senior engineer. From January 1999 to February 2000, he was Chief Geologist of Zhongyuan Petroleum Exploration Bureau of Sinopec Group Company. He then served as Deputy Manager and Chief Geologist of Zhongyuan Oilfield Company of Sinopec Group Company from February 2000 to February 2001. He was Vice President of Sinopec Exploration and Production Research Institute from July 2000 to March 2001. He then served as Deputy Director General of Sinopec Oilfield E & P Department from March 2001 to June 2004. Since June 2004, he served as Manager of the Northwest Company of Sinopec Group Company. Mr. Jiao has served as Vice President of Sinopec Corp. since October 2006.

*Chen Ge*, 46, Secretary to the Board of Directors of Sinopec Corp. Mr. Chen graduated from Daqing Petroleum Institute in July 1983 majoring in petroleum refining, and then obtained his MBA degree from Dalian University of Science and Technology in July 1996. He is a senior economist. From July 1983 to February 2000, he worked in Beijing Yanshan Petrochemical Company. From February 2000 to December 2001, he was Deputy Director General of the Board Secretariat of Sinopec Corp. Mr. Chen has been Director General of the Board Secretariat since December 2001. Mr. Chen has been the Secretary to the Board of Directors of Sinopec Corp. since April 2003.

## B. COMPENSATION

### Salaries of Directors, Supervisors and Members of the Senior Management

Our directors and supervisors who hold working posts with us and other senior management members receive their remuneration in the form of basic salary and performance rewards.

The following table sets forth the compensation on individual basis for our directors, supervisors and executive officers who receive compensation from us in 2008.

<u>Name</u>	<u>Position with the Company</u>	<u>Remuneration paid by the Company in 2007</u> (RMB in thousand)
<i><b>Directors</b></i>		
Su Shulin	Chairman	—
Zhou Yuan	Vice Chairman	—
Wang Tianpu	Director, President	844
Zhang Jianhua	Director, Senior Vice President	808
Wang Zhigang	Director, Senior Vice President	808
Dai Houliang	Director, Senior Vice President, CFO	808
Liu Zhongli	Independent Non-executive Director	240
Shi Wanpeng	Independent Non-executive Director	240
Li Deshui	Independent Non-executive Director	240
Yao Zhongmin	Director	48
Fan Yifei	Director	48
<i><b>Supervisors</b></i>		
Wang Zuoran	Chairman of Supervisory Committee	—
Zhang Youcai	Vice Chairman, Independent Supervisor	240
Kang Xianzhang	Supervisor	—
Zou Huiping	Supervisor	436
Li Yonggui	Independent Supervisor	240
Su Wensheng	Employee Representative Supervisor	428

Zhang Jitian	Employee Representative Supervisor	429
Cui Guoqi	Employee Representative Supervisor	448
Li Zhonghua	Employee Representative Supervisor	424

***Other Executive officers***

Cao Xiyou	Senior Vice President	808
Zhang Kehua	Vice President	528
Zhang Haichao	Vice President	513
Jiao Fangzheng	Vice President	518
Chen Ge	Secretary to the Board of Directors	438

**C. BOARD PRACTICE**

We have three special board committees, namely, the audit committee, the strategy committee and the remuneration and evaluation committee. The majority of the members of the strategy committee and the remuneration and evaluation committee, and all members of the audit committee, are independent directors. In addition, the audit committee shall have at least one independent director who is a financial expert.

The main responsibilities of the audit committee include:

- to propose the appointment or replacement of the independent auditor;
- to oversee the internal auditing system and its implementation;
- to coordinate the communication between the internal auditing department and the independent auditor;
- to examine and approve financial information and its disclosure; and
- to examine the internal control system.

The main responsibilities of the strategy committee are to conduct research and put forward proposals on the long-term development strategy and significant investments.

The main responsibilities of the remuneration and evaluation committee include:

- to research on evaluation criteria for directors and the president, to conduct their evaluations and make necessary suggestions; and
- to research on and review the policies and proposals in respect of the remuneration of directors, supervisors, president, vice-president, Chief Financial Officer and secretary of the board of directors.

The members of our audit committee are Liu Zhongli, Shi Wanpeng and Li Deshui, all of whom are our Independent Non-executive Directors. Our Board has determined that Liu Zhongli qualifies as an audit committee financial expert. The members of our strategy committee are Wang Tianpu, Zhang Jianhua, Wang Zhigang, Li Deshui, Yao Zhongmin and Fan Yifei. The members of our remuneration and evaluation committee are Liu Zhongli, Shi Wanpeng, Li Deshui and Dai Houliang.

Our directors have entered into directors service contracts with us and under such contracts, there is no severance pay arrangements for our directors.

## D. EMPLOYEES

As of December 31, 2006, 2007 and 2008, we had approximately 340,886, 334,377 and 358,304 employees, respectively. The following table sets forth the number of our employees by our business segments, their scope of work and their education as of December 31, 2008.

<b>By Segment</b>	<b>Number of Employees</b>	<b>Percentage of Total Number of Employees (%)</b>
Exploration and Production	140,048	39.1
Refining	82,004	22.9
Marketing and Distribution	58,260	16.2
Chemicals	69,066	19.3
Corporate and Others	8,926	2.5
<b>Total</b>	<b>358,304</b>	<b>100.0</b>

<b>By Employee's Scope of Work</b>	<b>Number of Employees</b>	<b>Percentage of Total Number of Employees (%)</b>
Production	184,800	51.6
Sales	57,651	16.1
Technical	46,936	13.1
Finance	9,957	2.8
Administration	28,664	8.0
Others	30,296	8.4
<b>Total</b>	<b>358,304</b>	<b>100.0</b>

<b>By Education</b>	<b>Number of Employees</b>	<b>Percentage of Total Number of Employees (%)</b>
Master's degree and above	6,327	1.8
University	67,318	18.8
Tertiary education	75,274	21.0
Technical/polytechnic school	33,159	9.2
Secondary, technical/polytechnic school or below	176,226	49.2
<b>Total</b>	<b>358,304</b>	<b>100.0</b>

We have trade unions that protect employee rights, organize educational programs, assist in the fulfillment of economic objectives, encourage employee participation in management decisions, and assist in mediating disputes between us and individual employees. We have not been subject to any strikes or other labor disturbances that have interfered with our operation, and we believe that our relations with our employees are good.

The total remuneration of our employees includes salary, performance bonuses and allowances. Employees also receive certain subsidies in housing, health services, education and other miscellaneous items.

Since 2001, we have implemented an employee reduction plan by means of retirement, voluntary resignation and/or redundancy to enhance our efficiency and operating profit, and by December 31, 2008, a total of 142,269 employees have retired.

## E. SHARE OWNERSHIP

Our directors, supervisors and senior officers do not have share ownership in us.

## ITEM 7. MAJOR SHAREHOLDERS AND RELATED PARTY TRANSACTIONS

### A. MAJOR SHAREHOLDERS

The following table sets forth information regarding our 5% or more shareholders as of May 15, 2009.

<b>Shareholder</b>	<b>Number of Shares Owned (in millions)</b>	<b>Percentage of Ownership (%)</b>
Sinopec Group Company .	65,758.04	75.84

As of May 15, 2009, 1,018,973,200 H shares were registered in the name of a nominee of Citibank, N.A., the depository under our ADS deposit agreement. Citibank, N.A. has advised us that, as of May 15, 2009, 10,189,732 ADSs, representing 1,018,973,200 H shares, were held of record by Cede & Co. and 54 other registered shareholders domiciled in and outside of the United States. We have no further information as to our shares held, or beneficially owned, by U.S. persons.

## **B. RELATED PARTY TRANSACTIONS**

Sinopec Group Company owns 75.84% of our outstanding equity as of May 15, 2009. Sinopec Group Company will be able to exercise all the rights of a controlling shareholder, including the election of directors and voting in respect of amendments to our articles of association. Sinopec Group Company, as our controlling shareholder, will be subject to certain minority shareholder protection provisions under our articles of association.

We have engaged from time to time and will continue to engage in a variety of transactions with Sinopec Group Company, which provide a number of services to us, including ancillary supply, transport, educational and community services. The nature of our transactions with Sinopec Group Company is governed by a number of service and other contracts between Sinopec Group Company and us. A discussion of these agreements and arrangements is set forth under the heading "Item 7 - Major Shareholders and Related Party Transactions-Related Party Transactions" in our annual report on Form 20-F filed with the Securities and Exchange Commission on April 17, 2001, and under the heading "Item 7 - Major Shareholders and Related Party Transactions-Related Party Transactions" in our annual report on Form 20-F filed with the Securities and Exchange Commission on April 13, 2007.

On June 26, 2008, we entered into a series of assets acquisition agreements with Shengli Oilfields Administrative Bureau, Zhongyuan Petroleum Exploration Bureau, Henan Petroleum Exploration Bureau, Jiangnan Oilfield Administrative Bureau, Jiangsu Petroleum Exploration Bureau and Huadong Petroleum Bureau, each of which is the wholly-owned entity of Sinopec Group Company, to acquire all the downhole operation assets in maintenance nature. The consideration for the acquisition is RMB1,624 million. We used our internal resources to fund the acquisition. The acquisition was completed on June 30, 2008.

In addition, on August 22, 2008, we entered into the Memorandum on Adjustment of Rent of Land Use Rights with Sinopec Group Company. Pursuant to the memorandum, the annual total rent payable under the original Land Use Rights Leasing Contract dated June 3, 2000, as amended, was adjusted to approximately RMB 4.2 billion and the area of land use rights subject to leasing shall be revised to approximately 416.7 million square meters.

Our aggregate amount of connected transactions actually occurred during 2008 was RMB 318.6 billion, of which, incoming trade whereby we purchased products or services amounted to RMB 121.5 billion, and outgoing trade whereby we provided products or services amounted to RMB 197.13 billion (including, RMB 197.0 billion of sales of products and services, RMB 19 million of interest earned, RMB 78 million of income from agency fee). In 2008, the products and services provided by Sinopec Group Company (procurement, storage, transportation, exploration and production services, production-related services) to us were RMB 91.9 billion, representing 6.23% of our operating expenses for year 2008, and a decrease of 2.47% compared with 2007. The auxiliary and community services provided by Sinopec Group Company to us were RMB 1.6 billion, representing 0.11% of the operating expenses, and a decrease by 0.62% compared with 2007. The product sales from us to Sinopec Group Company amounted to RMB 80.3 billion, representing 5.53% of our operating revenue. We also paid approximately RMB 368 million as rent in 2008 under the Leasing Agreement for Properties. In 2008, we paid an insurance premium of approximately RMB 1.4 billion to Sinopec Group Company under the terms of its SPI Fund. The amount of rental payable by us to Sinopec Group Company was approximately RMB 4.2 billion in 2008. Please see Note 30 of our consolidated financial statements included elsewhere in this annual report for a detailed discussion of our related party transactions.

## **C. INTERESTS OF EXPERTS AND COUNSEL**

Not applicable.

## **ITEM 8. FINANCIAL INFORMATION**

### **A. CONSOLIDATED STATEMENTS AND OTHER FINANCIAL INFORMATION**

See F-pages following Item 19.

#### **Legal Proceedings**

We are involved in certain judicial and arbitral proceedings before Chinese courts or arbitral bodies concerning matters arising in connection with the conduct of our businesses. We believe, based on currently available information, that the results of such proceedings, in the aggregate, will not have a material adverse effect on our financial condition or results of operations.

#### **Dividend Distribution Policy**

Our board of directors will determine the payment of dividends, if any, with respect to our shares on a per share basis. Any final dividend for a financial year shall be subject to shareholders' approval. The board may declare interim and special dividends at any time under general authorization by a shareholders' ordinary resolution. A decision to declare or to pay any dividends in the future, and the amount of any dividends, will depend on our results of operations, cash flows, financial condition, the payment by our subsidiaries of cash dividends to us, future prospects and other factors which our directors may determine are important.

For holders of our H shares, cash dividend payments, if any, shall be declared by our board of directors in Renminbi and paid in HK dollars. The depositary will convert the HK dollar dividend payments and distribute them to holders of ADSs in US dollars, less expenses of conversion.

In addition to cash, dividends may be distributed in the form of shares. Any distribution of shares, however, must be approved by special resolution of the shareholders. Dividends in the form of shares will be distributed to the depositary and, except as otherwise described in the Deposit Agreement, will be distributed by the depositary in the form of additional ADSs, to holders of ADSs.

Dividends may be paid only out of our distributable profits (less allocations to the statutory surplus reserve funds which are 10% of our net income determined in accordance with the PRC Accounting Standards for Business Enterprises ("ASBE") and the discretionary surplus reserve funds) and may be subject to PRC withholding tax. Our articles of association limit our distributable profits to the lower of the amount determined in accordance with the ASBE and IFRS. Subject to the above, we currently expect that we will distribute as dividends up to 40% of our distributable profits.

In accordance with the board resolution adopted on March 27, 2009, our board has proposed dividend of RMB 0.12 per ordinary share for the year ended December 31, 2008. After deducting the interim dividends distribution of RMB 0.03 per ordinary share, the year end dividend is RMB 0.09 per ordinary share. The total dividend to be paid amounted to approximately RMB 7.8 billion. The resolution is subject to the approval by the general shareholders' meeting.

### **B. SIGNIFICANT CHANGES**

None.

## **ITEM 9. THE OFFER AND LISTING**

### **A. OFFER AND LISTING DETAILS**

Not applicable, except for Item 9A (4) and Item 9C.

Our H Shares have been listed on the Hong Kong Stock Exchange (Code: 0386), and our ADSs, each representing 100 H Shares, have been listed on the New York Stock Exchange and the London Stock Exchange under the symbol "SNP", since we completed our initial public offering on October 19, 2000. Prior to that time, there was no public market for our H Shares. The Hong Kong Stock Exchange is the principal non-U.S. trading market for our H

Shares. Our publicly traded domestic shares, or A shares, are listed on the Stock Exchange of Shanghai since August 8, 2001 (Code: 600028).

The following table sets forth, for the periods indicated, the high and low closing prices per H Share, as reported on the Stock Exchange of Hong Kong, per ADS, as reported on the New York Stock Exchange and per A share, as reported on the Stock Exchange of Shanghai.

Period	The Stock Exchange of Hong Kong		The New York Stock Exchange		The Shanghai Stock Exchange		
	High	Low	High	Low	High	Low	
Past 6 months	(HK dollar per H share)		(US dollar per ADS)		(RMB per A share)		
May (up to May 15, 2009)	6.50	6.00	85.82	77.87	10.84	9.98	
April	6.19	5.15	79.77	67.45	10.06	8.78	
March	4.99	3.65	65.13	47.08	9.09	7.95	
February	4.64	4.05	60.86	52.23	9.27	7.83	
2009	January	5.26	4.17	67.7	52.41	7.94	7.06
	December	5.43	4.64	71.13	59.48	8.87	7.02
2008	November	5.15	4.25	66.53	50.87	8.42	6.67
Quarterly Data							
2009	First Quarter	5.26	3.65	67.70	47.08	9.27	7.06
2008	Fourth Quarter	6.24	3.76	78.35	50.57	10.19	6.67
	Third Quarter	8.38	5.89	110.36	73.26	11.88	8.7
	Second Quarter	8.71	6.78	112.56	86.65	13.81	9.91
	First Quarter	11.66	6.14	146.28	81.43	24.38	11.38
2007	Fourth Quarter	12.96	9.18	178.83	118.19	28.49	19.23
	Third Quarter	9.71	6.93	124.90	90.00	18.99	12.33
	Second Quarter	9.18	6.63	117.44	85.78	15.20	10.04
	First Quarter	7.32	5.67	92.23	72.92	11.20	8.37
Annual Data							
2008		11.66	3.76	146.28	50.57	24.38	6.67
2007		12.96	5.67	178.83	72.92	28.49	8.37
2006		7.20	3.775	92.64	47.40	9.15	4.58
2005		3.90	2.75	50.58	35.55	4.66	3.25
2004		3.85	2.475	49.90	32.08	5.77	4.26

Source: Bloomberg

## ITEM 10. ADDITIONAL INFORMATION

### A. SHARE CAPITAL

Not applicable.

### B. MEMORANDUM AND ARTICLES OF ASSOCIATION

*The following is a summary of certain provisions of our articles of association, as amended, the Company Law of the PRC (2006) and certain other applicable laws and regulations of the PRC. You and your advisors should refer to the text of our articles of association, as amended, and to the texts of applicable laws and regulations for further information.*

## ***Objects and Purposes***

We are a joint stock limited company established in accordance with the Company Law and certain other laws and regulations of the PRC. We are registered with the PRC State Administration of Industry and Commerce with business license number 1000001003298. Article 12 of our articles of association provides that our scope of businesses includes, among other things, exploration, exploitation, storage, pipeline transportation, land transportation, water transportation, sales of oil and natural gas; oil refining; wholesaling and retailing of gasoline, kerosene and diesel oil (for subsidiaries only); sales of lubricant, liquid gas, fuel oil, solvent naphtha and asphalt; the production, sales, storage land transportation and water transportation of ethylene, propylene, butadiene, naphtha, heavy oil, ethylene glycol, PTA, beta-lactam, dacron, nitrilon, rubber and other chemical raw materials and products; production of chemical fertilizer; production of electricity; operation of 24-hour stores; shaped packing foods, retailing of cigarettes, automobile decorations (for subsidiaries only), automobile cleaning; production, supervision of manufacturing, installation of oil and petrochemical machinery and equipment; purchase and sales of oil and petrochemical raw and auxiliary materials, equipment and parts; technology and information, research, development, application and consultation of alternative energy products; self-operation of and acting as agency for the import and export of various commodities and technologies other than those restricted or prohibited by the state from import and export; contractor of overseas mechanical, electronics, petrochemical projects and domestic international bid-inviting projects; export of equipments and materials required for the aforementioned overseas projects; dispatch of labor required for the aforementioned overseas projects.

## ***Directors***

Our directors shall be elected at our shareholders' general meeting. Cumulative voting shall be adopted for the election of directors if a controlling shareholder controls 30% or more of our shares. Details of the cumulative voting mechanism are set forth in Article 57 of the Rules and Procedures for the Shareholders' General Meetings that is an appendix to, and forms an integral part of, our articles of association. Our directors shall be elected for a term of three years and may serve consecutive terms upon re-election, except that independent directors may only serve a maximum of two terms. Our directors are not required to hold any shares in us, and there is no age limit requirement for the retirement or non-retirement of our directors.

Where a director is materially interested, directly or indirectly, in a contract, transaction or arrangement (including any proposed contract, transaction or arrangement) with us, he or she shall declare the nature and extent of his or her interests to the board of directors at the earliest opportunity, whether or not such contract, transaction or arrangement is otherwise subject to the approval of the board. A director shall not vote, and shall not be counted in the quorum of the meeting, on any resolution concerning any contract, transaction or arrangement where the director owns material rights or interests therein. A director is deemed to be interested in a contract, transaction or arrangement in which his associate (as defined by the Listing Rule of the Hong Kong Stock Exchange) is interested.

Unless the interested director discloses his interests to the board and the contract, transaction or arrangement in which the director is materially interested is approved by the board at a meeting in which the director neither votes nor is not counted in the quorum, such contract, transaction or arrangement shall be voidable by us except with respect to a bona fide party thereto who does not have notice of the director's interests.

We are prohibited from making loans or providing guarantees to our directors and their associates except where such loan or guarantee is to meet expenditure requirement incurred or to be incurred by the director for the purposes of the company or for the purpose of enabling the director to perform his or her duties properly.

The board of directors shall examine and approve the amount of the long-term loans for the current year in accordance with the annual investment plan as approved by the shareholders' general meeting. The chairman of the board may make adjustments of not more than 10% of the total amount of the long-term loans for the current year as approved by the board of directors. The board of directors shall also approve the total amount of the working capital loans for the current year. Within the total amount of the long-term or working capital loans as approved by the board of directors, the chairman of the board is authorized to approve and sign on behalf of the company any such loan contract with loan amount over RMB 1.0 billion, and the president of the company is authorized to approve and sign on behalf of the company any such loan contract with loan amount not exceeding RMB 1.0 billion.

Matters relating to the remuneration and liability insurance of our directors shall be determined by the shareholders' general meeting.



## ***Dividends***

A distribution of final dividends for any financial year is subject to shareholders' approval. Except otherwise decided by Shareholders' meeting, the board of directors may make decision on the distribution of interim dividends. Except otherwise provided by law and regulation, the sum of interim dividends shall not exceed 50 percents of the distributive profit as set out in the table for semi-year profit. Dividends may be distributed in the form of cash or shares. A distribution of shares, however, must be approved by special resolution of the shareholders.

Dividends may only be distributed after allowance has been made for:

- recovery of losses, if any;
- allocations to the statutory surplus reserve fund; and
- allocations to a discretionary surplus reserve fund if approved by the shareholders.

The allocations to the statutory surplus reserve fund shall be 10% of our after-tax profits of the current year determined in accordance with ASBE.

The articles of association require us to appoint on behalf of the holders of H shares a receiving agent which is registered as a trust corporation under the Trustee Ordinance of Hong Kong to receive dividends declared by us in respect of the H shares on behalf of such shareholders. The articles of association require that cash dividends in respect of H shares be declared in Renminbi and paid by us in HK dollars. The depository of our ADSs will convert such proceeds into US dollars and will remit such converted proceeds to our holders of ADSs. If we record no profit for the year, we may not normally distribute dividends for the year.

Dividend payments may be subject to PRC withholding tax.

## ***Voting Rights and Shareholders' Meetings***

Our board of directors shall convene a shareholders' annual general meeting once every year and within six months from the end of the preceding financial year. Our board shall convene an extraordinary general meeting within two months of the occurrence of any one of the following events:

- where the number of directors is less than the number stipulated in the PRC Company Law or two-thirds of the number specified in our articles of association;
- where our unrecovered losses reach one-third of the total amount of our share capital;
- where shareholder(s) holding 10% or more of our issued and outstanding voting shares request(s) in writing the convening of an extraordinary general meeting;
- whenever our board deems necessary or our board of supervisors so requests; or
- circumstances provided in the articles of association.

Meetings of a special class of shareholders must be called in certain enumerated situations when the rights of the holders of such class of shares may be modified or adversely affected as discussed below. Resolutions proposed by the board of supervisors or shareholder(s) holding 5% or more of the total number of voting shares shall be included in the agenda for the relevant annual general meeting if they are matters which fall within the scope of the functions and powers of shareholders in general meeting.

All shareholders' meetings must be convened by our board by written notice given to shareholders not less than 45 days before the meeting. Based on the written replies received by us 20 days before a shareholders' meeting, we shall calculate the number of voting shares represented by shareholders who have indicated that they intend to attend the meeting. Where the number of voting shares represented by those shareholders amount to more than one-half of our total voting shares, we may convene the shareholders' general meeting (regardless of the number of shareholders who actually attend). Otherwise, we shall, within five days, inform the shareholders again of the motions

to be considered and the date and venue of the meeting by way of public announcement. After the announcement is made, the shareholders' meeting may be convened. The accidental omission by us to give notice of a meeting to, or the non-receipt of notice of a meeting by, a shareholder will not invalidate the proceedings at that shareholders' meeting.

Shareholders at meetings have the power, among other things, to approve or reject our profit distribution plans, annual budget, financial statements, increase or decrease in share capital, issuance of debentures, merger or liquidation and any amendment to our articles of association. Shareholders of the shares which the Company issues to foreign investors for subscription in foreign currencies possess the same rights and undertake the same obligations as those of the shares which the Company issues to domestic investors for subscription in Renminbi. In addition, the rights of a class of shareholders may not be modified or abrogated, unless approved by a special resolution of all shareholders at a general shareholders' meeting and by a special resolution of shareholders of that class of shares at a separate meeting. Our articles of association enumerate, without limitation, certain amendments which would be deemed to be a modification or abrogation of the rights of a class of shareholders, including increasing or decreasing the number of shares of a class disproportionate to increases or decreases of other classes of shares, removing or reducing rights to receive dividends in a particular currency or creating shares with voting or equity rights superior to shares of such class.

Cumulative voting is adopted for the election of directors. For all other matters, each share is entitled to one vote on all such matters submitted to a vote of our shareholders at all shareholders' meetings, except for meetings of a special class of shareholders where only holders of shares of the affected class are entitled to vote on the basis of one vote per share of the affected class.

Shareholders are entitled to attend and vote at meetings either in person or by proxy. Proxies must be in writing and deposited at our legal address, or such other place as is specified in the meeting notice, not less than 24 hours before the time for holding the meeting at which the proxy proposes to vote or the time appointed for the passing of the relevant resolution(s). When the instrument appointing a proxy is executed by the shareholder's attorney-in-fact, such proxy when deposited must be accompanied by a notary certified copy of the relevant power of attorney or other authority under which the proxy was executed.

Except for those actions discussed below which require supermajority votes ("special resolutions"), resolutions of the shareholders are passed by a simple majority of the voting shares held by shareholders who are present in person or by proxy. Special resolutions must be passed by or more than two-thirds of the voting rights represented held by shareholders who are present in person or by proxy.

The following decisions must be adopted by special resolution:

- an increase or reduction of our share capital or the issue of shares, including stock distributions, of any class, warrants and other similar securities;
- issuance of debentures;
- our division, merger, dissolution and liquidation; (Shareholders who object to a proposed division or merger are entitled to demand that either we or the shareholders who approved the merger purchase their shares at a fair price.)
- repurchase of shares;
- amendments to our articles of association; and
- any other matters considered by the shareholders in a general meeting and which they have resolved by way of an ordinary resolution to be of a nature which may have a material impact on us and should be adopted by special resolution.

All other actions taken by the shareholders, including the appointment and removal of our directors and supervisors and the declaration of cash dividend payments, will be decided by an ordinary resolution of the shareholders. The listing agreement between us and the Hong Kong Stock Exchange (the "Listing Agreement") provided that we may not permit amendments to certain sections of the articles of association which have been mandated by the Hong Kong Stock Exchange. These sections include provisions relating to:

- varying the rights of existing classes of shares;
- voting rights;
- our power to purchase our own shares;
- rights of minority shareholders; and
- procedure on liquidation.

In addition, certain amendments to the articles of association require the approval and consent of the relevant PRC authorities.

Any shareholder resolution which is in violation of any laws or administrative regulations of the PRC will be null and void.

#### ***Liquidation Rights***

In the event of our liquidation, the H shares will rank pari passu with the domestic ordinary shares, and payment of debts out of our remaining assets shall be made in the order of priority prescribed by applicable laws and regulations or, if no such standards exist, in accordance with such procedure as the liquidation committee which has been appointed either by us or the People's Court of the PRC may consider to be fair and reasonable. After payment of debts, we shall distribute the remaining property to shareholders according to the class and proportion of their shareholders.

#### ***Further Capital Call***

Shareholders are not liable to make any further contribution to the share capital other than according to the terms, which were agreed by the subscriber of the relevant shares at the time of subscription.

#### ***Increases in Share Capital and Preemptive Rights***

The articles of association require the approval by a special resolution of the shareholders and by special resolution of holders of domestic ordinary shares and H shares at separate shareholder class meetings be obtained prior to authorizing, allotting, issuing or granting shares, securities convertible into shares or options, warrants or similar rights to subscribe for any shares or such convertible securities. No such approval is required if, but only to the extent that:

- we issue domestic ordinary shares and/or H shares, either separately or concurrently, in numbers not exceeding 20% of the number of domestic ordinary shares and H shares then in issue, respectively, in any 12-month period, as approved by a special resolution of the shareholders; or
- if our plans for issuing domestic ordinary shares and H shares upon its establishment are implemented within fifteen months of the date of approval by the China Securities Regulatory Commission.

New issues of shares must also be approved by the relevant PRC authorities.

#### ***Reduction of Share Capital and Purchase by Us of Our Shares and General Mandate to Repurchase Shares***

We may reduce our registered share capital only upon obtaining the approval of the shareholders by a special resolution and, in certain circumstances, of relevant PRC authorities. The number of H shares, which may be purchased is subject to the Hong Kong Takeovers and Share Repurchase Codes.

#### ***Restrictions on Large or Controlling Shareholders***

Our articles of association provide that, in addition to any obligation imposed by laws and administration regulations or required by the listing rules of the stock exchanges on which our H shares are listed, a controlling shareholder shall not exercise his voting rights in a manner prejudicial to the interests of the shareholders generally or of some part of the shareholders:

- to relieve a director or supervisor from his or her duty to act honestly in our best interests;
- to approve the expropriation by a director or supervisor (for his or her own benefit or for the benefit of another person) of our assets in any way, including, without limitation, opportunities which may benefit us; or
- to approve the expropriation by a director or supervisor (for his or her own benefit or for the benefit of another person) of the individual rights of other shareholders, including, without limitation, rights to distributions and voting rights (save according to a restructuring of our company which has been submitted for approval by the shareholders in a general meeting in accordance with our articles of association).

A controlling shareholder, however, will not be precluded by our articles of association or any laws and administrative regulations or the listing rules of the stock exchanges on which our H shares are listed from voting on these matters.

When a controlling shareholder intends to put forward a new motion on profit distribution at an annual general meeting, the controlling shareholder shall, at not less than ten days before the date of the annual general meeting, submit the motion to the board of directors to enable it to make an announcement, failing which the shareholder is not entitled to put forward the motion at the annual general meeting.

A controlling shareholder is defined by our articles of association as any person who acting alone or in concert with others:

- is in a position to elect more than one-half of the board of directors;
- has the power to exercise, or to control the exercise of, 30% or more of our voting rights;
- holds 30% or more of our issued and outstanding shares; or
- has de facto control of us in any other way.

As of the date of this annual report, Sinopec Group Company is and will be our only controlling shareholder.

#### ***Disclosure***

The Listing Agreement imposes a requirement on us to keep the Hong Kong Stock Exchange, our shareholders and other holders of our listed securities informed as soon as reasonably practicable of any information relating to us and our subsidiaries, including information on any major new developments which are not public knowledge, which:

- is necessary to enable them and the public to appraise the position of us and our subsidiaries;
- is necessary to avoid the establishment of a false market in its securities; and
- might be reasonably expected materially to affect market activity in and the price of its securities.

There are also requirements under the Listing Rules for us to obtain prior shareholders' approval and/or to disclose to shareholders details of certain acquisitions or disposals of assets and other transactions (including transactions with controlling shareholders).

#### ***Sources of Shareholders' Rights***

The PRC's legal system is based on written statutes and is a system in which decided legal cases have little precedent value. The PRC's legal system is similar to civil law systems in this regard. In 1979, the PRC began the process of developing its legal system by undertaking to promulgate a comprehensive system of laws. In December 1993, the Standing Committee of the 8th National People's Congress adopted the PRC Company Law. On October 27, 2005, the PRC Company law was amended by the Standing Committee of the 10<sup>th</sup> National People's Congress, and

came into force on January 1, 2006. The amended PRC Company Law enhanced the protection of shareholders' rights primarily in the following regards:

- Shareholders holding 10 percent or more of the shares of the company are entitled to petition the court to dissolve the company if (i) the company is in serious operational difficulties; (ii) its continuing existence will seriously prejudice the interests of the shareholders; and (iii) such difficulties cannot be resolved through any other means;
- Shareholders holding 1 percent or more of the shares of the company for more than 180 consecutive days are entitled to request the board of supervisors (in terms of directors and senior management) or the board of directors (in terms of supervisors) to bring legal proceedings, or bring legal proceedings in their own name on behalf of the company where it is in emergency and the company will be subject to irreparable loss if not to do so, against directors, supervisors or senior management who fail to comply with the laws and regulations or the company's articles of association in the course of performing their duties and cause loss to the company;
- Shareholders who oppose the company's decision on merger or separation are entitled to request the company to repurchase their shares; and
- Shareholders holding 10 percent or more of the voting rights of the company are entitled to convene a shareholders' meeting.

Currently, the primary sources of shareholder rights are our articles of association, as amended, the PRC Company Law and the Listing Rules of the Hong Kong Stock Exchange, which, among other things, impose certain standards of conduct, fairness and disclosure on us, our directors and our controlling shareholder, i.e., Sinopec Group Company. To facilitate the offering and listing of shares of PRC companies overseas, and to regulate the behavior of companies whose shares are listed overseas, the State Council Securities Committee and the State Commission for Restructuring the Economic System issued on August 27, 1994 the Mandatory Provisions for articles of association of Company Listing Overseas (the "Mandatory Provisions"). These Mandatory Provisions become entrenched in that, once they are incorporated into the articles of association of a PRC company, any amendment to those provisions will only become effective after approval by the State-owned Assets Supervision and Administration Commission of the State Council. The Listing Rules require a number of additional provisions to the Mandatory Provisions to be included in the articles of association of PRC companies listing H shares on the Hong Kong Stock Exchange (the "Additional Provisions"). The Mandatory Provisions and the Additional Provisions have been incorporated into our articles of association.

In addition, upon the listing of and for so long as the H shares are listed on the Hong Kong Stock Exchange, we will be subject to those relevant ordinances, rules and regulations applicable to companies listed on the Hong Kong Stock Exchange, including the Listing Rules of the Hong Kong Stock Exchange, the Securities (Disclosure of Interests) Ordinance (the "SDI Ordinance"), the Securities (Insider Dealing) Ordinance and the Hong Kong Codes on Takeovers and Mergers and Share Repurchases (the "Hong Kong Takeovers and Repurchase Codes").

Unless otherwise specified, all rights, obligations and protections discussed below derive from our articles of association and/or the PRC Company Law.

#### ***Enforceability of Shareholders' Rights***

There has not been any public disclosure in relation to the enforcement by holders of H shares of their rights under constitutive documents of joint stock limited companies or the PRC Company Law or in the application or interpretation of the PRC or Hong Kong regulatory provisions applicable to PRC joint stock limited companies.

In most states of the United States, shareholders may sue a corporation "derivatively". A derivative suit involves the commencement by a shareholder of a corporate cause of action against persons (including corporate officers, directors or controlling shareholders) who have allegedly wronged the corporation, where the corporation itself has failed to enforce such claim against such persons directly. Such action is brought based upon a primary right of the corporation, but is asserted by a shareholder on behalf of the corporation. The PRC company law as amended in October 2005 and effective in January 2006 has also granted shareholders with the rights to bring such derivative suits.

Our articles of association provide that all differences or claims:

- between a holder of H shares and us;
- between a holder of H shares and any of our directors, supervisors, general managers, deputy general managers or other senior officers; or
- between a holder of H shares and a holder of domestic ordinary shares, arising from any provision of our articles of association, any right or obligation conferred or imposed by the PRC Company Law or any other relevant law or administrative regulation which concerns our affairs

must, with certain exceptions, be referred to arbitration at either the China International Economic and Trade Arbitration Commission in the PRC or the Hong Kong International Arbitration Center. Our articles of association provide that such arbitration will be final and conclusive. In June 1999, an arrangement was made between the People's Courts of the PRC and the courts of Hong Kong to mutually enforce arbitration awards rendered in the PRC and Hong Kong according to their respective laws. This new arrangement was approved by the Supreme Court of the PRC and the Hong Kong Legislative Council and became effective on February 1, 2000. We have provided an undertaking to the United States Securities and Exchange Commission that, at such time, if any, as all applicable laws and regulations of the PRC and (unless our H shares are no longer listed on the Hong Kong Stock Exchange) all applicable regulations of the Stock Exchange of Hong Kong Ltd. shall not prohibit, and to the extent Section 14 under the United States Securities Act of 1933, as amended, so requires, our board of directors shall propose an amendment to the articles of association which would permit shareholders to adjudicate disputes arising between our shareholders and us, our directors, supervisors or officers by means of judicial proceedings.

The holders of H shares will not be able to bring actions on the basis of violations of the Listing Rules and must rely on the Hong Kong Stock Exchange to enforce its rules. The SDI Ordinance establishes certain obligations in relation to disclosure of shareholder interests in Hong Kong listed companies, the violation of which is subject to prosecution by the Securities and Futures Commission of Hong Kong. The Hong Kong Takeovers and Repurchase Codes do not have the force of law and are only standards of commercial conduct considered acceptable for takeover and merger transactions and share repurchases in Hong Kong as established by the Securities and Futures Commission and the securities and futures industry in Hong Kong.

We have appointed our subsidiary in the U.S., SINOPEC-USA Co., Ltd., 410 Park Avenue, 22nd Fl., New York, NY 10022, USA, as our agent to receive service of process with respect to any action brought against us in certain courts in New York under the United States federal and New York State's securities laws. However, as the PRC does not have treaties providing for the reciprocal recognition and enforcement of judgments of courts within the United States, the United Kingdom, Japan or most other the Organization for Economic Cooperation and Development countries, administrative actions brought by regulatory authorities, such as the Commission, and other actions which result in foreign court judgments, could (assuming such actions are not required by PRC law and the articles of association to be arbitrated) only be enforced in the PRC on a reciprocal basis or according to relevant international treaty to which China is a party if such judgments or rulings do not violate the basic principles of the law of the PRC or the sovereignty, security and public interest of the society of the PRC, as determined by a People's Court of the PRC which has the jurisdiction for recognition and enforcement of judgments. We have been advised by our PRC counsel, Haiwen & Partners, that there is certain doubt as to the enforceability in the PRC of actions to enforce judgments of United States courts arising out of or based on the ownership of H shares or ADSs, including judgments arising out of or based on the civil liability provisions of United States federal or state securities laws.

***Restrictions on Transferability and the Share Register***

H shares may be traded only among investors who are not PRC persons, and may not be sold to PRC investors. There are no restrictions on the ability of investors who are not PRC residents to hold H shares.

As provided in the articles of associations we may refuse to register a transfer of H shares unless:

- any relevant transfer fee is paid;
- the instrument of transfer is only related to H shares listed in Hong Kong;
- the instrument of transfer is accompanied by the share certificates to which it relates, or such other evidence is given as may be reasonably necessary to show the right of the transferor to make the transfer;

- the stamp duty which is chargeable on the instrument of transfer has already been paid;
- if it is intended that the shares be transferred to joint owners, the maximum number of joint owners shall not be more than four (4); and
- the Company does not have any lien on the relevant shares.

We are required to keep a register of our shareholders which shall be comprised of various parts, including one part which is to be maintained in Hong Kong in relation to H shares to be listed on the Hong Kong Stock Exchange. Shareholders have the right to inspect and, for a nominal charge, to copy the share register. No transfers of ordinary shares shall be recorded in our share register within 30 days prior to the date of a shareholders' general meeting or within 5 days prior to the record date established for the purpose of distributing a dividend.

We have appointed HKSCC Registrars Limited to act as the registrar of our H shares. This registrar maintains our register of holders of H shares at our offices in Hong Kong and enters transfers of shares in such register upon the presentation of the documents described above.

### **C. MATERIAL CONTRACTS**

We have not entered into any material contracts other than in the ordinary course of business and other than those described under Item 4. Information on the Company, Item 7 - Major Shareholders and Related Party Transactions or elsewhere in this Form 20-F.

### **D. EXCHANGE CONTROLS**

The existing foreign exchange regulations have significantly reduced government foreign exchange controls for transactions under the current account, including trade and service related foreign exchange transactions and payment of dividends. We may undertake current account foreign exchange transactions without prior approval from the State Administration of Foreign Exchange by producing commercial documents evidencing such transactions, provided that they are processed through Chinese banks licensed to engage in foreign exchange transactions. The PRC government has stated publicly that it intends to make the Renminbi freely convertible in the future. However, we cannot predict whether the PRC government will continue its existing foreign exchange policy and when the PRC government will allow free conversion of Renminbi to foreign currency.

Foreign exchange transactions under the capital account, including principal payments in respect of foreign currency-denominated obligations, continue to be subject to significant foreign exchange controls and require the approval of the State Administration of Foreign Exchange. These limitations could affect our ability to obtain foreign exchange through debt or equity financing, or to obtain foreign exchange for capital expenditures.

On July 21, 2005, the PRC government changed its policy of pegging the value of the Renminbi to the U.S. dollar. Under the new policy, the Renminbi is permitted to fluctuate within a band against a basket of certain foreign currencies. This change in policy resulted initially in an approximately 2.0% appreciation in the value of the Renminbi against the U.S. dollar. Since the adoption of this new policy, the value of Renminbi against the U.S. dollar has fluctuated on a daily basis within narrow ranges, but overall has further strengthened against the U.S. dollar. On January 14, 2006, the PBOC authorized the China Foreign Exchange Trade System to publish the exchange rate of the RMB against the US dollar, the euro, the Japanese yen, and the HK dollar at 9:15 am of each business day, which would be the medium exchange rate of RMB for transactions on the interbank spot foreign exchange market (over-the-counter transactions and automatic price-matching transactions) as well as transactions over bank counters. We cannot assure that such exchange rate would not fluctuate greatly. In addition, any significant revaluation of the Renminbi may have a material adverse effect on our revenues and financial condition, and the value of, and any dividends payable on, our ADSs in foreign currency terms. We do not currently and will not plan to hedge against the risk of exchange rate fluctuation. Information relating to the exchange risk, exchange rate and hedging activities is presented in "Item 11. Qualitative and Quantitative Disclosures about Market risk — Foreign Exchange Rate Risk".

### **E. TAXATION**

#### **PRC Taxation**

The following discussion addresses the principal PRC tax consequences of investing in the H shares or ADSs.

## ***Taxation of Dividends***

### ***Individual Investors***

According to the PRC Individual Income Tax Law, as amended, dividends paid by Chinese companies are ordinarily subject to a Chinese withholding tax levied at a flat rate of 20%. For a foreign individual who has no domicile and does not stay in the territory of China or who has no domicile but has stayed in the territory of China for less than one year, the receipt of dividends from a company in China is normally subject to a withholding tax of 20% unless reduced or exempted by an applicable tax treaty. However, the Chinese State Administration of Taxation, or the SAT, the Chinese central government tax authority which succeeded the State Tax Bureau, issued, on July 21, 1993, the Notice of the Chinese State Administration of Taxation Concerning the Taxation of Gains on Transfer and Dividends from Share (Equities) Received by Foreign Investment Enterprises, Foreign Enterprises and Foreign Individuals, or the Tax Notice, which states that dividends paid by a Chinese company to individuals with respect to overseas-listed shares, such as H shares, are temporarily not subject to Chinese withholding tax.

In a letter dated July 26, 1994 to the former State Commission for Restructuring the Economic System, the former State Council Securities Commission and the China Securities Regulatory Commission, the SAT reiterated the temporary tax exemption stated in the Tax Notice for dividends received from a Chinese company listed overseas. In the event that the exemption is withdrawn, a 20% tax may be withheld on dividends in accordance with the PRC Individual Income Tax Law and its implementation rules, as amended. The withholding tax may be reduced or exempted under an applicable double taxation treaty. To date, the relevant tax authorities have not collected withholding tax from dividend payments on the shares exempted under the Tax Notice.

### ***Foreign Enterprises***

In accordance with the new Enterprise Income Tax Law and its implementation rules that became effective on January 1, 2008, dividends derived from the revenues accumulated from January 1, 2008 and are paid by PRC companies to non-resident enterprises, which are established under the laws of non-PRC jurisdictions and have no establishment or place of business in China or whose dividends from China do not relate to their establishment or place of business in China, are generally subject to a PRC withholding tax levied at a rate of 10% unless exempted or reduced pursuant to an applicable double-taxation treaty or other exemptions. Dividends paid by PRC companies to resident enterprises, including enterprises established under the laws of non-PRC jurisdictions but whose "de facto management body" is located in the PRC, are not subject to any PRC withholding tax, unless the dividends are derived from the publicly traded shares which have been held continuously by the resident enterprises for less than twelve months. Dividends, bonuses and other return based on equity investment that a non-resident enterprise with establishment or place of business in China receives from a resident enterprise and that have actual connection with such establishment or place of business are also exempted from any PRC withholding tax, except of those derived from the publicly traded shares which have been held continuously by the non-resident enterprises for less than 12 months. According to the Notice on the Issues Concerning Withholding the Enterprise Income Tax on the Dividends Paid by Chinese Resident Enterprise to H Share Holders Which Are Overseas Non-resident Enterprises issued by the SAT on November 6, 2008, Chinese resident enterprises are required to withhold PRC enterprise income tax at the rate of 10% on dividends paid for 2008 and later years payable to their respective H Shares holders that are "non-resident enterprises".

### ***Tax Treaties***

Holders resident in countries which have entered into avoidance of double taxation treaties with the PRC may be entitled to a reduction or exemption of the withholding tax imposed on the payment of dividends. The PRC currently has avoidance of double taxation treaties with a number of other countries, which include Australia, Canada, France, Germany, Japan, Malaysia, the Netherlands, Singapore, the United Kingdom and the United States.

Under a tax treaty between United States and China, China may tax dividends paid by Sinopec Corp. to eligible US Holders up to a maximum of 10% of the gross amount of such dividend. Under the tax treaty, an eligible US Holder is a person who, by reason of domicile, residence, place of head office, place of incorporation or any other criterion of similar nature is liable to tax in the United States, subject to a detailed "treaty shopping" provision.

### ***Taxation of Capital Gains***

According to the Tax Notice, gains realized upon the sale of overseas-listed shares issued by PRC companies by foreign individual investors are not subject to tax on capital gains.



In accordance with the new Enterprise Income Tax Law and its implementation rules, capital gains realized by foreign enterprises which are non-resident enterprises in China upon the sale of overseas-listed shares are generally subject to a PRC withholding tax levied at a rate of 10%, unless exempted or reduced pursuant to an applicable double-taxation treaty or other exemptions. The capital gains realized by resident enterprises, including enterprises established under the laws of non-PRC jurisdictions but whose “de facto management body” is located in the PRC, upon the sales of overseas-listed shares are subject to the PRC enterprise income tax. Before the effectiveness of the new Enterprise Income Tax Law, gains realized by foreign enterprises that are holders of overseas-listed shares of a PRC company excluding the shares held through their PRC domestic establishment or place of business were exempted from the withholding tax according to the Tax Notice. However, the effectiveness of such exemption granted by the Tax Notice becomes uncertain in light of the provisions under the new Enterprise Income Tax Law and its implementation rules.

### ***PRC Stamp Tax Considerations***

Under the Provisional Regulations of The People's Republic of China Concerning Stamp Tax, which became effective in October, 1988, PRC stamp tax should not be imposed on the transfer of shares of H Shares or ADSs of PRC publicly traded companies..

### **United States Federal Income Tax Considerations**

The following is a summary of United States federal income tax considerations that are anticipated to be material for US Holders (as defined below) who hold H shares or ADSs. This summary is based upon existing United States federal income tax law, which is subject to change, possibly with retroactive effect. This summary does not discuss all aspects of United States federal income taxation which may be important to particular investors in light of their individual investment circumstances, such as investors subject to special tax rules including: financial institutions, insurance companies, broker-dealers, tax-exempt organizations, non-US Holders, investors who own (directly, indirectly, or constructively) 10% or more of our voting stock, investors that will hold H shares or ADSs as part of a straddle, hedge, conversion, constructive sale, or other integrated transaction for United States federal income tax purposes, or US Holders that have a functional currency other than the United States dollar, all of whom may be subject to tax rules that differ significantly from those summarized below. In addition, this summary does not discuss any foreign, state, local or alternative minimum tax considerations. This summary only addresses investors that will hold their H shares or ADSs as "capital assets" (generally, property held for investment) under the United States Internal Revenue Code (the "Code"). Each holder is urged to consult its tax advisor regarding the United States federal, state, local, and foreign income and other tax considerations of an investment in H shares or ADSs.

For purposes of this summary, a US Holder is a beneficial owner of H shares or ADSs that is for United States federal income tax purposes:

- an individual who is a citizen or resident of the United States;
- a corporation created in or organized under the laws of, the United States or any State or political subdivision thereof;
- an estate the income of which is includible in gross income for United States federal income tax purposes regardless of its source;
- a trust the administration of which is subject to the primary supervision of a United States court and which has one or more United States persons who have the authority to control all substantial decisions of the trust; or
- a trust that has elected to be treated as a United States person under the Code.

If a partnership (including any entity treated as a partnership for United States federal income tax purposes) holds H shares or ADSs, the tax treatment of a partner in such partnership will depend upon the status of the partner and the activities of the partnership. Partners in a partnership holding our H shares or ADSs are urged to consult their tax advisors as to the particular United States federal income tax consequences applicable to them.

A foreign corporation will be treated as a "passive foreign investment company" (a "PFIC"), for United States federal income tax purposes, if 75% or more of its gross income consists of certain types of "passive" income or 50%

or more of its assets are passive. Sinopec Corp. presently does not believe that it is a PFIC and does not anticipate becoming a PFIC. This is, however, a factual determination made on an annual basis and is subject to change. The following discussion is based on the belief that Sinopec Corp. will not be classified as a PFIC for United States federal income tax purposes. See the discussion below under the heading "PFIC Considerations" for a brief summary of the PFIC rules.

#### *General*

For United States federal income tax purposes, a US Holder of an ADS will be treated as the owner of the proportionate interest of the H shares held by the depository that is represented by an ADS and evidenced by such ADS. Accordingly, no gain or loss will be recognized upon the exchange of an ADS for the holder's proportionate interest in the H shares. A US Holder's tax basis in the withdrawn H shares will be the same as the tax basis in the ADS surrendered therefor, and the holding period in the withdrawn H shares will include the period during which the holder held the surrendered ADS.

#### *Dividends*

Any cash distributions paid by Sinopec Corp. out of earnings and profits, as determined under United States federal income tax principles, will be subject to tax as dividend income and will be includible in the gross income of a US Holder upon receipt. Because we do not intend to determine our earnings and profits on the basis of United States federal income tax principles, any distribution paid will generally be treated as a "dividend" for United States federal income tax purposes. A non-corporate recipient of dividend income will generally be subject to tax on dividend income from a "qualified foreign corporation" at a maximum U.S. federal tax rate of 15% rather than the marginal tax rates generally applicable to ordinary income so long as certain holding period requirements are met. A non-U.S. corporation (other than a passive foreign investment company) generally will be considered to be a qualified foreign corporation (i) if it is eligible for the benefits of a comprehensive tax treaty with the United States which the Secretary of Treasury of the United States determines is satisfactory for purposes of this provision and which includes an exchange of information program or (ii) with respect to any dividend it pays on stock which is readily tradable on an established securities market in the United States. There is currently a tax treaty in effect between the United States and the People's Republic of China which the Secretary of Treasury of the United States determined is satisfactory for these purposes and Sinopec Group, presently believes that it is eligible for the benefits of such treaty. Additionally, our ADSs trade on the New York Stock Exchange, an established securities market in the United States. Dividends paid in Hong Kong dollars will be includible in income in a United States dollar amount based on the United States dollar - Hong Kong dollar exchange rate prevailing at the time of receipt of such dividends by the depository, in the case of ADSs, or by the US Holder, in the case of H shares held directly by such US Holder. Gain or loss, if any, recognized on a subsequent sale, conversion or other disposition of Hong Kong dollars generally will be U.S. source income or loss. Dividends received on H shares or ADSs will not be eligible for the dividends received deduction allowed to corporations.

Dividends received on H shares or ADSs will be treated, for United States federal income tax purposes, as foreign source income. A US Holder may be eligible, subject to a number of complex limitations, to claim a foreign tax credit in respect of any foreign withholding taxes imposed on dividends received on H shares or ADSs. US Holders who do not elect to claim a foreign tax credit for foreign income tax withheld may instead claim a deduction, for United States federal income tax purposes, in respect of such withholdings, but only for a year in which the US Holder elects to do so for all creditable foreign income taxes.

A distribution of additional shares of Sinopec Corp.'s stock to US Holders with respect to their H shares or ADSs that is pro rata to all Sinopec Corp.'s shareholders may not be subject to United States federal income tax. The tax basis of such additional shares will be determined by allocating the US Holders' adjusted tax basis in the H shares or ADSs between the H shares or ADSs and the additional shares, based on their relative fair market values on the date of distribution.

#### *Sale or Other Disposition of H shares or ADSs*

A US Holder will recognize capital gain or loss upon the sale or other disposition of H shares or ADSs in an amount equal to the difference between the amount realized upon the disposition and the US Holder's adjusted tax basis in such H shares or ADSs, as each is determined in US dollars. Any capital gain or loss will be long-term if the H shares or ADSs have been held for more than one year and may be, under the income tax treaty between the People's Republic of China and the United States, foreign source gain or loss. The claim of a deduction in respect of a capital loss, for United States federal income tax purposes, may be subject to limitations.

## *PFIC Considerations*

If Sinopec Corp. were to be classified as a PFIC in any taxable year, a U.S. Holder would be subject to special rules generally intended to reduce or eliminate any benefits from the deferral of United States federal income tax that a U.S. Holder could derive from investing in a foreign company that does not distribute all of its earnings on a current basis. In such event, a U.S. Holder of the H shares or ADSs may be subject to tax at ordinary income tax rates on (i) any gain recognized on the sale of the H shares or ADSs and (ii) any "excess distribution" paid on the H shares or ADSs (generally, a distribution in excess of 125% of the average annual distributions paid by Sinopec Corp. in the three preceding taxable years). In addition, a U.S. Holder may be subject to an interest charge on such gain or excess distribution.

The above results may be eliminated if a "mark-to-market" election is available and a US Holder validly makes such an election. If the election is made, such holder generally will be required to take into account the difference, if any, between the fair market value and its adjusted tax basis in H shares or ADSs at the end of each taxable year as ordinary income or ordinary loss (to the extent of any net mark-to-market gain previously included in income). In addition, any gain from a sale or other disposition of H shares or ADSs will be treated as ordinary income, and any loss will be treated as ordinary loss (to the extent of any net mark-to-market gain previously included in income).

### **F. DIVIDENDS AND PAYING AGENTS**

Not applicable.

### **G. STATEMENT BY EXPERTS**

Not applicable.

### **H. DOCUMENTS ON DISPLAY**

We filed with the Securities and Exchange Commission in Washington, D.C. a Registration Statement on Form F-1 (Registration No. 333-12502) under the Securities Act in connection with the ADSs offered in the global offering. The Registration Statement contains exhibits and schedules. Any statement in this annual report about any of our contracts or other documents is not necessarily complete. If the contract or document is filed as an exhibit to the Registration Statement, the contract or document is deemed to modify the description contained in this annual report. You must review the exhibits themselves for a complete description of the contract or documents.

You may inspect and copy our registration statements, including their exhibits and schedules, and the reports and other information we file with the Securities and Exchange Commission in accordance with the Exchange Act at the public reference facilities maintained by the Securities and Exchange Commission at Judiciary Plaza, 450 Fifth Street, Room 1024, N.W., Washington, D.C. 20549 and at the regional offices of the Securities and Exchange Commission located at 233 Broadway, New York, NY 10279 and at Citicorp Center, 500 West Madison Street, Suite 1400, Chicago, Illinois 60661. You may also inspect the registration statements, including their exhibits and schedules, at the office of the New York Stock Exchange, Wall Street, New York, New York 10005. Copies of such material may also be obtained from the Public Reference Section of the Securities and Exchange Commission at 450 Fifth Street, N.W., Washington, D.C. 20549, at prescribed rates. You may obtain information regarding the Washington D.C. Public Reference Room by calling the Securities and Exchange Commission at 1-800-SEC-0330 or by contacting the Securities and Exchange Commission over the internet at its website at <http://www.sec.gov>.

### **I. SUBSIDIARY INFORMATION**

Not applicable.

## **ITEM 11. QUALITATIVE AND QUANTITATIVE DISCLOSURES ABOUT MARKET RISK**

Our primary market risk exposures are to fluctuations in exchange rates and interest rates.

## Foreign Exchange Rate Risk

The Renminbi is not a freely convertible currency. With the authorization from the PRC government, the PBOC announced that the PRC government reformed the exchange rate regime by moving into a managed floating exchange rate regime based on market supply and demand with reference to a basket of currencies on July 21, 2005. Actions taken by the PRC government could cause future exchange rates to vary significantly from current or historical exchange rates. Fluctuations in exchange rates may adversely affect the value, translated or converted into US dollars or Hong Kong dollars, of our net assets, earnings and any declared dividends. We cannot give any assurance that any future movements in the exchange rate of the Renminbi against the US dollar and other foreign currencies will not adversely affect our results of operations and financial condition.

The following presents various market risk information regarding market-sensitive financial instruments that we held or issued as of December 31, 2008 and 2007. We conduct our business primarily in Renminbi, which is also our functional and reporting currency.

The following tables provide information regarding instruments that are sensitive to foreign exchange rates as of December 31, 2008 and 2007. For debt obligations, the table presents cash flows and related weighted average rates by expected maturity dates.

As of December 31, 2008:

	Expected maturity					thereafter	Total	Fair value
	2009	2010	2011	2012	2013			
	(RMB equivalent in millions, except interest rates)							
<b>Assets</b>								
Cash and cash equivalents								
In United States dollar	1,259	-	-	-	-	-	1,259	1,259
In Hong Kong dollar	109	-	-	-	-	-	109	109
In Japanese yen	5	-	-	-	-	-	5	5
In Euro	43	-	-	-	-	-	43	43
Time deposits with financial institutions								
In United States dollar	91	-	-	-	-	-	91	91
<b>Liabilities</b>								
Debts in United States dollar								
Fixed rate	3,074	114	71	57	57	336	3,709	3,702
Average interest rate	4.0%	2.0%	1.5%	1.4%	1.4%	1.4%		
Variable rate	4,948	3	3	4	4	7	4,969	4,969
Average interest rate (1)	4.5%	4.9%	4.9%	4.9%	4.9%	4.9%		
Debts in Japanese yen								
Fixed rate	110	110	79	79	79	734	1,191	1,233
Average interest rate	2.6%	2.6%	2.6%	2.6%	2.6%	2.6%		
Variable rate	309	207	207	207	-	-	930	930
Average interest rate (1)	2.8%	2.9%	2.9%	2.9%	-	-		
Debts in Hong Kong dollar								
Fixed rate	-	-	-	-	-	9,870	9,870	9,870
Average interest rate	-	-	-	-	-	4.2%		
Variable rate	265	-	-	-	-	-	265	265
Average interest rate (1)	0.9%	-	-	-	-	-		
Debts in Euro								
Fixed rate	84	84	29	-	-	-	197	206
Average interest rate	6.6%	6.6%	6.6%	-	-	-		

(1) The average interest rates for variable rate loans are calculated based on the rates reported as of December 31, 2008.

As of December 31, 2007:

	Expected maturity						Total	Fair value
	2008	2009	2010	2011	2012	thereafter		
	(RMB equivalent in millions, except interest rates)							
<b>Assets</b>								
Cash and cash equivalents								
In United States dollar	754	-	-	-	-	-	754	754
In Hong Kong dollar	302	-	-	-	-	-	302	302
In Japanese yen	11	-	-	-	-	-	11	11
In Euro	5	-	-	-	-	-	5	5
<b>Liabilities</b>								
Debts in United States dollar								
Fixed rate	7,960	179	188	125	63	420	8,935	8,877
<i>Average interest rate</i>	5.2%	3.1%	2.8%	2.3%	2.0%	2.0%		
Variable rate	1,518	7	3	3	4	11	1,546	1,546
<i>Average interest rate (1)</i>	5.0%	7.3%	7.4%	7.2%	7.0%	6.7%		
Debts in Japanese yen								
Fixed rate	94	93	92	67	67	689	1,102	1,206
<i>Average interest rate</i>	2.6%	2.6%	2.6%	2.6%	2.6%	2.6%		
Variable rate	262	255	176	176	176	-	1,045	1,045
<i>Average interest rate (1)</i>	2.7%	2.8%	2.9%	2.9%	2.9%	-		
Debts in Hong Kong dollar								
Fixed rate	25	-	-	-	-	14,106	14,131	14,131
<i>Average interest rate</i>	5.5%	-	-	-	-	4.2%		
Variable rate	347	375	-	-	-	-	722	722
<i>Average interest rate (1)</i>	3.9%	4.0%	-	-	-	-		
Debts in Euro								
Fixed rate	26	26	26	-	-	-	78	81
<i>Average interest rate</i>	6.7%	6.7%	6.7%	-	-	-		

(1) The average interest rates for variable rate loans are calculated based on the rates reported as of December 31, 2007.

**Interest Rate Risk**

We are exposed to interest rate risk resulting from fluctuations in interest rates on our short- and long-term debts. Upward fluctuations in interest rates increase the cost of new debt and the interest cost of outstanding floating rate borrowings.

Our debts consist of fixed and variable rate debt obligations with original maturities ranging from 1 to 25 years. Fluctuations in interest rates can lead to significant fluctuations in the fair values of our debt obligations.

The following tables present principal cash flows and related weighted average interest rates by expected maturity dates of our interest rate sensitive financial instruments as of December 31, 2008 and 2007.

As of December 31, 2008:

	Expected maturity						Total	Fair value
	2009	2010	2011	2012	2013	thereafter		
	(RMB equivalent in millions, except interest rates)							
<b>Assets</b>								
Cash and cash equivalents								
In Renminbi	5,532	-	-	-	-	-	5,532	5,532
In United States dollar	1,259	-	-	-	-	-	1,259	1,259
In Hong Kong dollar	109	-	-	-	-	-	109	109
In Japanese yen	5	-	-	-	-	-	5	5
In Euro	43	-	-	-	-	-	43	23
Time deposits with financial institutions								
In Renminbi	661	-	-	-	-	-	661	661
In United States dollar	91	-	-	-	-	-	91	91
<b>Liabilities</b>								
Debts in Renminbi								
Fixed rate	78,395	1,550	382	8,580	60	79,705	168,672	172,273 (1)
<i>Average interest rate</i>	3.7%	3.0%	3.0%	2.9%	2.5%	1.5%		
Variable rate	11,300	7,923	5,034	2,974	6,139	2,454	35,824	35,824
<i>Average interest rate (2)</i>	6.3%	6.7%	6.7%	6.7%	6.7%	6.8%		
Debts in United States dollar								
Fixed rate	3,074	114	71	57	57	336	3,709	3,702
<i>Average interest rate</i>	4.0%	2.0%	1.5%	1.4%	1.4%	1.4%		
Variable rate	4,948	3	3	4	4	7	4,969	4,969
<i>Average interest rate (2)</i>	4.5%	4.9%	4.9%	4.9%	4.9%	4.9%		
Debts in Japanese yen								
Fixed rate	110	110	79	79	79	734	1,191	1,233
<i>Average interest rate</i>	2.6%	2.6%	2.6%	2.6%	2.6%	2.6%		
Variable rate	309	207	207	207	-	-	930	930
<i>Average interest rate (2)</i>	2.8%	2.9%	2.9%	2.9%	-	-		
Debts in Hong Kong dollar								
Fixed rate	-	-	-	-	-	9,870	9,870	9,870
<i>Average interest rate</i>	-	-	-	-	-	4.2%		
Variable rate	265	-	-	-	-	-	265	265
<i>Average interest rate (2)</i>	0.9%	-	-	-	-	-		
Debts in Euro								
Fixed rate	84	84	29	-	-	-	197	206
<i>Average interest rate</i>	6.6%	6.6%	6.6%	-	-	-		

(1) Carrying amounts are used for loans from Sinopec Group Company and its affiliates as it is not practicable to estimate their fair values because the cost of obtaining discount and borrowing rates for comparable borrowings would be excessive.

(2) The average interest rates for variable rate loans are calculated based on the rates reported as of December 31, 2008.



As of December 31, 2007:

	Expected maturity						Total	Fair value
	2008	2009	2010	2011	2012	thereafter		
	(RMB equivalent in millions, except interest rates)							
<b>Assets</b>								
Cash and cash equivalents								
In Renminbi	6,624	-	-	-	-	-	6,624	6,624
In United States dollar	754	-	-	-	-	-	754	754
In Hong Kong dollar	302	-	-	-	-	-	302	302
In Japanese yen	11	-	-	-	-	-	11	11
In Euro	5	-	-	-	-	-	5	5
Time deposits with financial institutions								
In Renminbi	668	-	-	-	-	-	668	668
<b>Liabilities</b>								
Debts in Renminbi								
Fixed rate	49,399	7,554	3,661	82	8,580	55,915	125,191	124,322 (1)
Average interest rate	5.4%	5.2%	5.0%	4.9%	4.9%	0.4%		
Variable rate	863	11,115	7,201	4,001	2,101	2,777	28,058	28,058
Average interest rate (2)	6.5%	6.5%	6.8%	6.9%	7.0%	7.0%		
Debts in United States dollar								
Fixed rate	7,960	179	188	125	63	420	8,935	8,877
Average interest rate	5.2%	3.1%	2.8%	2.3%	2.0%	2.0%		
Variable rate	1,518	7	3	3	4	11	1,546	1,546
Average interest rate (2)	5.0%	7.3%	7.4%	7.2%	7.0%	6.7%		
Debts in Japanese yen								
Fixed rate	94	93	92	67	67	689	1,102	1,206
Average interest rate	2.6%	2.6%	2.6%	2.6%	2.6%	2.6%		
Variable rate	262	255	176	176	176	-	1,045	1,045
Average interest rate (2)	2.7%	2.8%	2.9%	2.9%	2.9%	-		
Debts in Hong Kong dollar								
Fixed rate	25	-	-	-	-	14,106	14,131	14,131
Average interest rate	5.5%	-	-	-	-	4.2%		
Variable rate	347	375	-	-	-	-	722	722
Average interest rate (2)	3.9%	4.0%						
Debts in Euro								
Fixed rate	26	26	26	-	-	-	78	81
Average interest rate	6.7%	6.7%	6.7%	-	-	-		

(1) Carrying amounts are used for loans from Sinopec Group Company and its affiliates as it is not practicable to estimate their fair values because the cost of obtaining discount and borrowing rates for comparable borrowings would be excessive.

(2) The average interest rates for variable rate loans are calculated based on the rates reported as of December 31, 2007.

**ITEM 12. DESCRIPTION OF SECURITIES OTHER THAN EQUITY SECURITIES**

Not applicable

**ITEM 13. DEFAULTS, DIVIDEND ARREARAGES AND DELINQUENCIES**

None.

**ITEM 14. MATERIAL MODIFICATIONS TO THE RIGHTS OF SECURITY HOLDERS AND USE OF PROCEEDS**

**A. MATERIAL MODIFICATIONS TO THE RIGHTS TO SECURITIES HOLDERS**

None.

**B. USE OF PROCEEDS**

Not applicable.

**ITEM 15. CONTROLS AND PROCEDURES**

**Disclosure Controls and Procedures**

Our management, with the participation of our principal executive officer and principal financial officer, has evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the U.S. Securities Exchange Act of 1934, as amended (the "Exchange Act")) as of December 31, 2008 (the "Evaluation Date"), the end of the fiscal year covered by this annual report. Based on this evaluation, our principal executive officer and principal financial officer have concluded that, as of the Evaluation Date, our disclosure controls and procedures were effective.

**Management's Report on Internal Control over Financial Reporting**

Our management is responsible for establishing and maintaining adequate internal control over financial reporting (as defined in Rules 13a-15(f) of the Securities Exchange Act of 1934). The Company's internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with International Financial Reporting Standards.

Internal control over financial reporting cannot provide absolute assurance of achieving financial reporting objectives because of its inherent limitations. Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Our management assessed the effectiveness of our internal control over financial reporting based upon the criteria established in *Internal Control-Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission as of December 31, 2008. Based on that evaluation, our management has concluded that our internal control over financial reporting was effective as of December 31, 2008 based on these criteria.

KPMG, an independent registered public accounting firm, has audited the consolidated financial statements included in this annual report on Form 20-F and, as part of the audit, has issued a report, included herein, on the effectiveness of our internal control over financial reporting.

**Report of Independent Registered Public Accounting Firm**

The Board of Directors and Shareholders of China Petroleum & Chemical Corporation:

We have audited China Petroleum & Chemical Corporation and subsidiaries (the “Group”)’ s internal control over financial reporting as of December 31, 2008, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Group’s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management’s Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Group’s internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company’s internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company’s internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company’s assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the Group maintained, in all material respects, effective internal control over financial reporting as of December 31, 2007, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of the Group as of December 31, 2007 and 2008, and the related consolidated statements of income, cash flows and equity for each of the years in the three-year period ended December 31, 2008, and our report dated March 27, 2009 expressed an unqualified opinion on those consolidated financial statements.

**/S/ KPMG**  
Hong Kong, China  
March 27, 2009

#### **Changes in Internal Control over Financial Reporting**

During the year ended December 31, 2008, there have been no changes in our internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

#### **ITEM 16. RESERVED**

#### **ITEM 16A. AUDIT COMMITTEE FINANCIAL EXPERT**

The board of directors has determined that Mr. Liu Zhongli qualifies as an audit committee financial expert in accordance with the terms of Item 16.A of Form 20-F. Mr. Liu was appointed as an independent non-executive director and a member of the audit committee of the third board of our company in May 2006. For Mr. Liu's biographical information, see "Item 6 Directors, Senior Management and Employees – A. Directors, members of the supervisory committee and senior management."

**ITEM 16B. CODE OF ETHICS**

As of the date of this annual report, we do not have, in form, a code of ethics that applies to our principal executive officer, principal financial officer and principal accounting officer. Our principal executive officers, Mr. Su Shulin (Chairman) and Mr. Wang Tianpu (President), and our principal financial officer, Mr. Dai Houliang (CFO), currently also serve as our directors and are thus subject to the director service contracts that they have with us. Under the director service contracts, each of them agrees that he owes a fiduciary and diligence obligation to our company and that he shall not engage in any activities in competition with our business or carry any activities detrimental to the interests of our company. Each of them also agrees to perform his respective duties as a director and senior officer in accordance with the Company Law of the PRC, relevant rules and regulations promulgated by China Securities Regulatory Commission and the Mandatory Provisions of Articles of Association of Overseas Listed Companies.

**ITEM 16C. PRINCIPAL ACCOUNTANT FEES AND SERVICES**

The following table sets forth the aggregate audit fees, audit-related fees, tax fees of our principal accountants and all other fees billed for products and services provided by our principal accountants other than the audit fees, audit-related fees and tax fees for each of the fiscal years 2007 and 2008:

	<u>Audit Fees</u>	<u>Audit-Related Fees</u>	<u>Tax Fees</u>	<u>Other Fees</u>
2007	RMB 85 million	—	—	—
2008	RMB 81 million	—	—	—

Before our principal accountants were engaged by our company or our subsidiaries to render audit or non-audit services, the engagement has been approved by our audit committee.

**ITEM 16D. EXEMPTIONS FROM THE LISTING STANDARDS FOR AUDIT COMMITTEES**

Not applicable.

**ITEM 16E. PURCHASES OF EQUITY SECURITIES BY THE ISSUER AND AFFILIATED PURCHASERS**

None.

**ITEM 16F. CHANGE IN REGISTRANT'S CERTIFYING ACCOUNTANT**

Not applicable.

**ITEM 16G. COMPARISON OF NEW YORK STOCK EXCHANGE CORPORATE GOVERNANCE RULES AND CHINA CORPORATE GOVERNANCE RULES FOR LISTED COMPANIES**

Under the amended Corporate Governance Rules of New York Stock Exchange (NYSE), foreign issuers (including the Company) listed on the NYSE are required to disclose a summary of the significant differences between their domestic corporate governance rules and NYSE corporate governance rules that would apply to a U.S. domestic issuer. A summary of such differences is listed below:

<u>NYSE corporate governance rules</u>	<u>Corporate governance rules applicable to the domestically listed companies in China and the Company's governance practices</u>
Corporate governance guidelines	

Listed companies must adopt and disclose corporate governance guidelines, involving director qualification standards, director compensation, director continuing education, annual performance evaluation of the board of directors, etc.

### **Director Independence**

A listed company must have a majority of independent directors on its board of directors. No director qualifies as “independent” unless the board of directors affirmatively determines that the director has no material relationship with the listed company (either directly or as a partner, shareholder or officer of an organization that has a relationship with the company). In addition, a director must meet certain standards to be deemed independent. For example, a director is not independent if the director is, or has been within the last three years, an employee of the listed company, or if the director has received, during any twelve-month period within the last three years, more than US\$120,000 in direct compensation from the listed company.

To empower non-management directors to serve as a more effective check on management, the non-management directors of each listed company must meet at regularly scheduled executive sessions without management.

### **Nominating/Corporate Governance Committee**

Listed companies must have a nominating/corporate governance committee composed entirely of independent directors.

The nominating/corporate governance committee must have a written charter that addresses the committee’s purposes and responsibilities which, at minimum, must be to: search for eligible people for the board of directors, select and nominate directors for the next session of the shareholders’ annual meeting, study and propose corporate governance guidelines, supervise the evaluation of the board of directors and management, and evaluate the performance of the committee every year.

### **Compensation Committee**

Listed companies must have a compensation committee composed entirely of independent directors.

CSRC (China Securities Regulatory Commission) has issued the Corporate Governance Rules, prescribing detailed guidelines on directors of the listed companies, including director selection, the structure of the board of directors and director performance evaluation etc. The Company Law of PRC has specific regulations on the directors’ qualification. Furthermore, CSRC promulgates the guidelines on the senior management training and organizes the relevant training. The Company has complied with the above mentioned laws or rules.

It is required in China that any listed company must establish an independent director system and set forth specific requirements for the qualification of independent directors. For example, an independent director shall not hold any other position in the listed company other than being a director and shall not be influenced by the main shareholders or the controlling persons of the listed company, or by any other entities or persons with whom the listed company has a significant relationship. The Company has complied with the relevant Chinese corporate governance rules and has implemented internal rules governing the independence and responsibilities of independent directors. The Company determines the independence of independent directors every year.

No similar requirements.

It is stipulated in China that the board of directors of a listed company may, through the resolution of the shareholders’ meeting, establish a nominating committee composed entirely of directors, of which the independent directors shall be the majority and the convener. Up to now, the Company has not set up any nominating committee.

Relevant responsibilities of the nominating/corporate governance committee are similar to those stipulated by the NYSE rules, but the main responsibilities do not include the research and recommendation of corporate governance guidelines, the supervision of the evaluation of the board of directors and management, or the annual evaluation of the committee.

It is stipulated in China that the board of directors of a listed company should, through the resolution of shareholders’ meeting, have a compensation and

The written charter of the compensation committee must state, at least, the following purposes and responsibilities:

- (1) review and approve the corporate goals associated with CEO's compensation, evaluate the performance of the CEO in fulfilling these goals, and based on such evaluation determine and approve the CEO's compensation level;
- (2) make recommendations to the board with respect to non-CEO executive officer compensation, and incentive-compensation and equity-based plans that are subject to board approval;
- (3) produce a committee report on executive compensation as required by the SEC to be included in the annual proxy statement or annual report filed with the SEC.

The charter must also include the requirement for an annual performance evaluation of the compensation committee.

### **Audit Committee**

Listed companies must have an audit committee that satisfies the requirements of Rule 10A-3 of Securities Exchange Act of 1934 (the "Exchange Act"). It must have a minimum of three members, and all audit committee members must satisfy the requirements for independence set forth in Section 303A.02 of NYSE Corporate Governance Rules as well as the requirements of Rule 10A-3b (1) of the Exchange Act.

The written charter of the audit committee must specify that the purpose of the audit committee is to assist the board oversight of the integrity of financial statements, the company's compliance with legal and regulatory requirements, qualifications and independence of independent auditors and the performance of the listed company's internal audit function and independent auditors.

The written charter must also require the audit committee to prepare an audit committee report as required by the SEC to be included in the listed company's annual proxy statement as well as an annual performance evaluation of the audit committee.

Each listed company must have an internal audit department.

Shareholders must be given the opportunity to vote on equity-compensation plans and material revisions thereto, except for employment incentive plans, certain awards and plans in the context of mergers and acquisitions.

assessment committee composed entirely of directors, of whom the independent directors are the majority and act as the convener.

It is stipulated in China that the responsibilities of the compensation committee are:

- (1) to study evaluation standards on the performance of directors and the senior management and submit suggestion to the board of directors;
- (2) to study and review the compensation policies on the directors and the senior management.

It is also stipulated that the committee shall produce a report about the committee's performance in the annual report.

But the committee is not required to produce a report on the executive compensation or make an annual performance evaluation of the committee.

The board of directors of the Company has established a compensation and performance evaluation committee composed mainly of independent directors who act as the convener, and the committee has established a written charter complying with the domestic corporate governance rules.

It is stipulated in China that the board of directors of a listed company should, through the resolution of the shareholders' meeting, establish an audit committee composed entirely of directors, of which the independent directors are the majority and act as the convener, and, at minimum, one independent director is an accounting professional.

The responsibilities of the audit committee are similar to those stipulated by the NYSE rules. It is also stipulated that the committee shall produce a report about the committee's performance in the annual report.

But according to the domestic practices, the company is not required to make an annual performance evaluation of the audit committee, and the audit committee is not required to prepare an audit report to be included in the company's annual proxy statement.

The Board of Directors of the Company has established an audit committee that satisfies relevant domestic and overseas requirements and the audit committee has a written charter.

China has a similar regulatory provision, and the Company has an internal audit department.

The relevant regulations of China require the board of directors propose plans on the amount and types of director compensation for the shareholders' meeting to approve. The compensation plan of executive officers shall be approved by the board and announced at the shareholders' meeting and disclosed to the public upon

the approval of the board of directors.

### **Code of ethics for directors, officers and employees**

Listed companies must adopt and disclose a code of business conduct and ethics for directors, officers and employees, and promptly disclose any waivers of the code for directors or executive officers.

China does not have such requirement for a code for ethics. But, since the directors and officers of the Company have all signed the Director Service Agreement, they are bound by their fiduciary duties to the Company. In addition, the directors and officers must perform their legal responsibilities in accordance with the Company Law of PRC, relative requirements of CSRS and Mandatory Provisions to the Charter of Companies Listed Overseas. Meanwhile, the Company establishes The Model Code of Securities Transactions by Corporate Employees and The Rules of The Company's Shares Transactions by Corporate Directors, Superiors and Senior Managements to regulate the above mentioned people when transacting related securities. In 2008, the Company promulgated the Code for Employees of the Company as the standards of business conduct and ethics of the employees.

Each listed company CEO must certify to the NYSE each year that he or she is not aware of any violation by the company of NYSE corporate governance listing standards and he or she must promptly notify the NYSE on writing of any material non-compliance with any applicable provisions of Section 303A.

No similar requirements.

### **ITEM 17. FINANCIAL STATEMENTS**

Not applicable.

### **ITEM 18. FINANCIAL STATEMENTS**

See F-pages following Item 19.

### **ITEM 19. EXHIBITS**

- 1 \*\* Articles of Association of the Registrant, amended and adopted by the shareholders' meeting on May 24, 2006 (English translation), incorporated by reference to Exhibit 1 to our Annual Report on Form 20-F filed with the Securities and Exchange Commission on April 13, 2007 (File Number: 001-15138).
- 1.1 \* Amendment to the Articles of Association of China Petroleum & Chemical Corporation, adopted by the shareholders' meeting on May 26, 2008 (English translation).
- 4.1\*\* Forms of Director Service Contracts dated May 24, 2006 (English translation), incorporated by reference to Exhibit 4.1 to our Annual Report on Form 20-F filed with the Securities and Exchange Commission on April 13, 2007 (File Number: 001-15138).
- 4.2\*\* Forms of Supervisor Service Contracts dated May 24, 2006 (English translation), incorporated by reference to Exhibit 4.2 to our Annual Report on Form 20-F filed with the Securities and Exchange Commission on April 13, 2007 (File Number: 001-15138).
- 4.3\*\* Reorganization Agreement between China Petrochemical Corporation and China Petroleum & Chemical Corporation dated June 3, 2000 (including English translation), incorporated by reference to Exhibit 10.1 to our Registration Statement on Form F-1 filed with the Securities and Exchange Commission on October 10, 2000 (File Number: 333-12502).

- 4.4\*\* Agreement for Mutual Provision of Products and Ancillary Services between China Petrochemical Corporation and China Petroleum & Chemical Corporation dated June 3, 2000 (including English translation), incorporated by reference to Exhibit 10.3 to our Registration Statement on Form F-1 filed with the Securities and Exchange Commission on October 10, 2000 (File Number: 333-12502).
- 4.5\*\* Agreement for Provision of Cultural, Educational, Hygiene and Community Services between China Petrochemical Corporation and China Petroleum & Chemical Corporation dated June 3, 2000 (including English translation), incorporated by reference to Exhibit 10.4 to our Registration Statement on Form F-1 filed with the Securities and Exchange Commission on October 10, 2000 (File Number: 333-12502).
- 4.6\*\* Trademark License Agreement between China Petrochemical Corporation and China Petroleum & Chemical Corporation dated June 3, 2000 (including English translation), incorporated by reference to Exhibit 10.6 to our Registration Statement on Form F-1 filed with the Securities and Exchange Commission on October 10, 2000 (File Number: 333-12502).
- 4.7\*\* Patents and Proprietary Technology License Contract between China Petrochemical Corporation and China Petroleum & Chemical Corporation dated June 3, 2000 (including English translation), incorporated by reference to Exhibit 10.7 to our Registration Statement on Form F-1 filed with the Securities and Exchange Commission on October 10, 2000 (File Number: 333-12502).
- 4.8\*\* Computer Software License Contract between China Petrochemical Corporation and China Petroleum & Chemical Corporation dated June 3, 2000 (including English translation), incorporated by reference to Exhibit 10.8 to our Registration Statement on Form F-1 filed with the Securities and Exchange Commission on October 10, 2000 (File Number: 333-12502).
- 4.9\*\* Assets Swap Contract between China Petrochemical Corporation and China Petroleum & Chemical Corporation dated June 3, 2000 (including English translation), incorporated by reference to Exhibit 10.9 to our Registration Statement on Form F-1 filed with the Securities and Exchange Commission on October 10, 2000 (File Number: 333-12502).
- 4.10\*\* Land Use Rights Leasing Contract between China Petrochemical Corporation and China Petroleum & Chemical Corporation dated June 3, 2000 (including English translation), incorporated by reference to Exhibit 10.10 to our Registration Statement on Form F-1 filed with the Securities and Exchange Commission on October 10, 2000 (File Number: 333-12502).
- 4.12\*\* Property Leasing Contract between China Petrochemical Corporation and China Petroleum & Chemical Corporation dated June 3, 2000 (including English translation), incorporated by reference to Exhibit 10.11 to our Registration Statement on Form F-1 filed with the Securities and Exchange Commission on October 10, 2000 (File Number: 333-12502).
- 4.13\*\* Accounts Collectable Contract between China Petrochemical Corporation and China Petroleum & Chemical Corporation dated August 16, 2000 (including English translation), incorporated by reference to Exhibit 10.17 to our Registration Statement on Form F-1 filed with the Securities and Exchange Commission on October 10, 2000 (File Number: 333-12502).
- 4.14\*\* Loan Transfer and Adjustment Contract between China Petrochemical Corporation and China Petroleum & Chemical Corporation dated August 16, 2000 (including English translation), incorporated by reference to Exhibit 10.18 to our Registration Statement on Form F-1 filed with the Securities and Exchange Commission on October 10, 2000 (File Number: 333-12502).
- 4.15\*\* Agreement on Adjustment to Related Party Transactions between China Petrochemical Corporation and China Petroleum & Chemical Corporation dated June 11, 2001 (English translation), incorporated by reference to Exhibit 4.15 to our Annual Report on Form 20-F filed with the Securities and Exchange Commission on April 13, 2007 (File Number: 001-15138).
- 4.16\*\* Land Use Right Leasing Agreement between China Petrochemical Corporation and China Petroleum & Chemical Corporation dated August 22, 2003 (English translation), incorporated by reference to Exhibit 4.16 to our Annual Report on Form 20-F filed with the Securities and Exchange Commission on April 13, 2007 (File Number: 001-15138).



- 4.17\*\* 2004 Agreement on Adjustment to Related Party Transactions between China Petrochemical Corporation and China Petroleum & Chemical Corporation dated October 31, 2004 (English translation) , incorporated by reference to Exhibit 4.17 to our Annual Report on Form 20-F filed with the Securities and Exchange Commission on April 13, 2007 (File Number: 001-15138).
- 4.18\*\* Memorandum on Adjustment of Rent of Land Use Rights between China Petrochemical Corporation and China Petroleum & Chemical Corporation dated March 31, 2006 (English translation) , incorporated by reference to Exhibit 4.18 to our Annual Report on Form 20-F filed with the Securities and Exchange Commission on April 13, 2007 (File Number: 001-15138).
- 4.19\*\* Supplemental Agreement on Related Party Transactions between China Petrochemical Corporation and China Petroleum & Chemical Corporation dated March 31, 2006 (English translation) , incorporated by reference to Exhibit 4.19 to our Annual Report on Form 20-F filed with the Securities and Exchange Commission on April 13, 2007 (File Number: 001-15138).
- 4.20\* Memorandum on Adjustment of Rent of Land Use Rights between China Petrochemical Corporation and China Petroleum & Chemical Corporation dated August 22, 2008 (English Translation).
- 8\* A list of the Registrant's subsidiaries.
- 12.1\* Certification of Chairman pursuant to Rule 13a-14(a).
- 12.2\* Certification of President pursuant to Rule 13a-14(a).
- 12.3\* Certification of CFO pursuant to Rule 13a-14(a).
- 13\* Certification of CEO and CFO pursuant to 18 U.S.C. §1350, and Rule 13a-14(b).

\* Filed herewith.

\*\* Incorporated by reference.

**CHINA PETROLEUM & CHEMICAL CORPORATION AND SUBSIDIARIES**

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## REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Shareholders of  
China Petroleum & Chemical Corporation:

We have audited the accompanying consolidated balance sheets of China Petroleum & Chemical Corporation and subsidiaries (the ‘ ‘Group’’) as of December 31, 2007 and 2008, and the related consolidated statements of income, cash flows and equity for each of the years in the three-year period ended December 31, 2008. These consolidated financial statements are the responsibility of the Group’s management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Group as of December 31, 2007 and 2008, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2008, in conformity with International Financial Reporting Standards as issued by the International Accounting Standards Board.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of the Group’s internal control over financial reporting as of December 31, 2008, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated March 27, 2009 expressed an unqualified opinion on the effectiveness of the Group’s internal control over financial reporting.

**KPMG**  
Hong Kong, China  
March 27, 2009

CHINA PETROLEUM & CHEMICAL CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME  
FOR THE YEARS ENDED DECEMBER 31, 2006, 2007 AND 2008  
(Amounts in millions, except per share data)

	Note	Years ended December 31,		
		2006	2007	2008
		RMB	RMB	RMB
<b>Operating revenues</b>				
Sales of goods		1,034,888	1,173,869	1,420,321
Other operating revenues	3	26,853	30,974	31,780
		<u>1,061,741</u>	<u>1,204,843</u>	<u>1,452,101</u>
<b>Other income</b>	4	5,161	4,863	50,342
<b>Operating expenses</b>				
Purchased crude oil, products and operating supplies and expenses		(854,236)	(970,929)	(1,285,155)
Selling, general and administrative expenses	5	(37,514)	(37,843)	(46,175)
Depreciation, depletion and amortization		(33,554)	(43,315)	(45,823)
Exploration expenses, including dry holes		(7,983)	(11,105)	(8,310)
Personnel expenses	6	(20,956)	(22,745)	(23,285)
Taxes other than income tax	7	(29,330)	(34,304)	(56,799)
Other operating expenses, net	8	(2,697)	(3,601)	(8,773)
<b>Total operating expenses</b>		<u>(986,270)</u>	<u>(1,123,842)</u>	<u>(1,474,320)</u>
<b>Operating income</b>		<u>80,632</u>	<u>85,864</u>	<u>28,123</u>
<b>Finance costs</b>				
Interest expense	9	(7,101)	(7,314)	(11,326)
Interest income		538	405	445
Unrealized (loss) / gain on embedded derivative component of the Convertible Bonds	23(f)	—	(3,211)	3,947
Foreign currency exchange losses		(140)	(311)	(954)
Foreign currency exchange gains		890	2,330	3,112
<b>Net finance costs</b>		<u>(5,813)</u>	<u>(8,101)</u>	<u>(4,776)</u>
Investment income		289	1,657	390
Income from associates and jointly controlled entities		3,434	4,044	580
<b>Earnings before tax</b>		<u>78,542</u>	<u>83,464</u>	<u>24,317</u>
Tax (expense) / benefit	10	(23,504)	(24,721)	1,883
<b>Net income</b>		<u>55,038</u>	<u>58,743</u>	<u>26,200</u>
<b>Attributable to:</b>				
Equity shareholders of the Company		53,603	56,533	29,769
Minority interests		1,435	2,210	(3,569)
<b>Net income</b>		<u>55,038</u>	<u>58,743</u>	<u>26,200</u>
<b>Earnings per share:</b>				
Basic	11	<u>0.62</u>	<u>0.65</u>	<u>0.34</u>
Diluted	11	<u>0.62</u>	<u>0.65</u>	<u>0.30</u>
<b>Weighted average number of shares</b>	11	<u>86,702</u>	<u>86,702</u>	<u>86,702</u>

See accompanying notes to consolidated financial statements.

**CHINA PETROLEUM & CHEMICAL CORPORATION AND SUBSIDIARIES**

**CONSOLIDATED BALANCE SHEETS  
AS OF DECEMBER 31, 2007 AND 2008  
(Amounts in millions)**

	Note	December 31,	
		2007 RMB	2008 RMB
<b>ASSETS</b>			
<b>Current assets</b>			
Cash and cash equivalents		7,696	6,948
Time deposits with financial institutions		668	752
Trade accounts receivable, net	12	22,947	12,989
Bills receivable		12,851	3,659
Inventories	13	116,032	95,255
Prepaid expenses and other current assets	14	24,922	34,924
Income tax receivable		—	9,784
Total current assets		<u>185,116</u>	<u>164,311</u>
<b>Non-current assets</b>			
Property, plant and equipment, net	15	375,142	403,265
Construction in progress	16	95,408	121,886
Goodwill	17	15,490	14,237
Interest in associates	18	16,865	15,595
Interest in jointly controlled entities	19	12,723	11,781
Investments	20	3,194	1,483
Deferred income tax assets	22	10,439	12,810
Lease prepayments		8,224	10,817
Long-term prepayments and other assets	21	10,124	11,642
Total non-current assets		<u>547,609</u>	<u>603,516</u>
Total assets		<u>732,725</u>	<u>767,827</u>
<b>LIABILITIES AND EQUITY</b>			
<b>Current liabilities</b>			
Short-term debts	23	44,654	74,896
Loans from Sinopec Group Company and its affiliates	23	15,840	23,587
Trade accounts payable	24	93,049	56,667
Bills payable	24	12,162	17,493
Accrued expenses and other payables	25	89,171	101,878
Income tax payable		10,479	16
Total current liabilities		<u>265,355</u>	<u>274,537</u>
<b>Non-current liabilities</b>			
Long-term debts	23	83,134	90,254
Loans from Sinopec Group Company and its affiliates	23	37,180	36,890
Deferred income tax liabilities	22	5,636	5,235
Other liabilities	26	8,662	11,589
Total non-current liabilities		<u>134,612</u>	<u>143,968</u>
Total liabilities		<u>399,967</u>	<u>418,505</u>
<b>Equity</b>			
Share capital	27	86,702	86,702
Reserves	28	220,731	241,967
Total equity attributable to equity shareholders of the Company		<u>307,433</u>	<u>328,669</u>
Minority interests		25,325	20,653
Total equity		<u>332,758</u>	<u>349,322</u>
Total liabilities and equity		<u>732,725</u>	<u>767,827</u>

See accompanying notes to consolidated financial statements.

CHINA PETROLEUM & CHEMICAL CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF EQUITY  
(Amounts in millions)

	Share capital	Capital reserve	Share premium	Re-valuation reserve	Statutory surplus reserve	Statutory public welfare fund	Discretionary surplus reserve	Other reserves	Retained earnings	Total equity attributable to equity shareholders of the Company	Minority interests	Total equity
	RMB	RMB	RMB	RMB	RMB	RMB	RMB	RMB	RMB	RMB	RMB	RMB
Balance as of January 1, 2006	86,702	(19,217)	18,072	26,342	13,514	13,514	7,000	2,785	77,387	226,099	31,174	257,273
Net income recognized directly in equity:												
Unrealized gain for the change in fair value of available-for-sale financial assets, net of deferred tax	—	—	—	—	—	—	—	34	—	34	—	34
Net income	—	—	—	—	—	—	—	—	53,603	53,603	1,435	55,038
Total recognized income for the year	—	—	—	—	—	—	—	34	53,603	53,637	1,435	55,072
Final dividend for 2005	—	—	—	—	—	—	—	—	(7,803)	(7,803)	—	(7,803)
Interim dividend for 2006	—	—	—	—	—	—	—	—	(3,468)	(3,468)	—	(3,468)
Appropriation (Note 28 (d) and (f))	—	—	—	—	5,066	—	20,000	—	(25,066)	—	—	—
Statutory public welfare fund transferred to statutory surplus reserve (Note 28 (e))	—	—	—	—	13,514	(13,514)	—	—	—	—	—	—
Revaluation surplus realized	—	—	—	(1,590)	—	—	—	—	1,590	—	—	—
Realization of deferred tax on lease prepayments	—	—	—	—	—	—	—	(7)	7	—	—	—
Transfer from retained earnings to other reserves	—	—	—	—	—	—	—	704	(704)	—	—	—
Transfer from other reserves to capital reserve	—	(2,373)	—	—	—	—	—	2,373	—	—	—	—
Distribution to Sinopec Group Company (Note 28 (g))	—	—	—	—	—	—	—	(631)	—	(631)	—	(631)
Consideration for the Acquisition of Oil Production Plants (Note 1)	—	—	—	—	—	—	—	(3,500)	—	(3,500)	—	(3,500)
Acquisitions of non-controlling interests of subsidiaries	—	—	—	—	—	—	—	—	—	—	(9,730)	(9,730)
Contributions from minority interests net of distributions	—	—	—	—	—	—	—	—	—	—	187	187
Disposal of a subsidiary	—	—	—	—	—	—	—	—	—	—	(743)	(743)
Balance as of December 31, 2006	<u>86,702</u>	<u>(21,590)</u>	<u>18,072</u>	<u>24,752</u>	<u>32,094</u>	<u>—</u>	<u>27,000</u>	<u>1,758</u>	<u>95,546</u>	<u>264,334</u>	<u>22,323</u>	<u>286,657</u>

See accompanying notes to consolidated financial statements.

CHINA PETROLEUM & CHEMICAL CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF EQUITY (CONTINUED)

(Amounts in millions)

	<u>Share capital</u>	<u>Capital reserve</u>	<u>Share premium</u>	<u>Re-valuation reserve</u>	<u>Statutory surplus reserve</u>	<u>Discretionary surplus reserve</u>	<u>Other reserves</u>	<u>Retained earnings</u>	<u>Total equity attributable to equity shareholders of the Company</u>	<u>Minority interests</u>	<u>Total equity</u>
	RMB	RMB	RMB	RMB	RMB	RMB	RMB	RMB	RMB	RMB	RMB
Balance as of January 1, 2007	86,702	(21,590)	18,072	24,752	32,094	27,000	1,758	95,546	264,334	22,323	286,657
Net income recognized directly in equity:											
Unrealized gain for the change in fair value of available-for-sale financial assets, net of deferred tax (Note 28 (k))	—	—	—	—	—	—	2,892	—	2,892	145	3,037
Effect of change in tax rate (Note 22 (ii))	—	—	—	—	—	—	(54)	—	(54)	17	(37)
Net income	—	—	—	—	—	—	—	56,533	56,533	2,210	58,743
Total recognized income for the year	—	—	—	—	—	—	2,838	56,533	59,371	2,372	61,743
Final dividend for 2006	—	—	—	—	—	—	—	(9,537)	(9,537)	—	(9,537)
Interim dividend for 2007	—	—	—	—	—	—	—	(4,335)	(4,335)	—	(4,335)
Adjustment to statutory surplus reserve (Note 28 (d))	—	—	—	—	235	—	—	(235)	—	—	—
Appropriation (Note 28 (d))	—	—	—	—	5,468	—	—	(5,468)	—	—	—
Revaluation surplus realized	—	—	—	(638)	—	—	—	638	—	—	—
Realization of deferred tax on lease prepayments	—	—	—	—	—	—	(7)	7	—	—	—
Transfer from retained earnings to other reserves	—	—	—	—	—	—	(151)	151	—	—	—
Transfer from other reserves to capital reserve	—	(1,062)	—	—	—	—	1,062	—	—	—	—
Contribution from Sinopec Group Company (Note 28 (g))	—	—	—	—	—	—	68	—	68	—	68
Consideration for the Acquisition of Refinery Plants (Note 1)	—	—	—	—	—	—	(2,468)	—	(2,468)	—	(2,468)
Contributions from minority interests net of distributions	—	—	—	—	—	—	—	—	—	630	630
Balance as of December 31, 2007	<u>86,702</u>	<u>(22,652)</u>	<u>18,072</u>	<u>24,114</u>	<u>37,797</u>	<u>27,000</u>	<u>3,100</u>	<u>133,300</u>	<u>307,433</u>	<u>25,325</u>	<u>332,758</u>

See accompanying notes to consolidated financial statements.

CHINA PETROLEUM & CHEMICAL CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF EQUITY (CONTINUED)  
(Amounts in millions)

	<u>Share capital</u>	<u>Capital reserve</u>	<u>Share premium</u>	<u>Re-valuation reserve</u>	<u>Statutory surplus reserve</u>	<u>Discretionary surplus reserve</u>	<u>Other reserves</u>	<u>Retained earnings</u>	<u>Total equity attributable to equity shareholders of the Company</u>	<u>Minority interests</u>	<u>Total equity</u>
	RMB	RMB	RMB	RMB	RMB	RMB	RMB	RMB	RMB	RMB	RMB
Balance as of January 1, 2008	86,702	(22,652)	18,072	24,114	37,797	27,000	3,100	133,300	307,433	25,325	332,758
Net loss recognized directly in equity:											
Unrealized loss for the change in fair value of available-for-sale financial assets, net of deferred tax (Note 28 (k))	—	—	—	—	—	—	(2,320)	—	(2,320)	(118)	(2,438)
Net income	—	—	—	—	—	—	—	29,769	29,769	(3,569)	26,200
Total recognized income / (loss) for the year	—	—	—	—	—	—	(2,320)	29,769	27,449	(3,687)	23,762
Issuance of the Bonds with Warrants (Note 23 (g))	—	6,879	—	—	—	—	—	—	6,879	—	6,879
Final dividend for 2007	—	—	—	—	—	—	—	(9,971)	(9,971)	—	(9,971)
Interim dividend for 2008	—	—	—	—	—	—	—	(2,601)	(2,601)	—	(2,601)
Adjustment to the statutory surplus reserve (Note 28 (d))	—	—	—	—	1,189	—	—	(1,189)	—	—	—
Appropriation (Note 28 (d) and (f))	—	—	—	—	4,092	20,000	—	(24,092)	—	—	—
Revaluation surplus realized	—	—	—	(347)	—	—	—	347	—	—	—
Realization of deferred tax on lease prepayments	—	—	—	—	—	—	(6)	6	—	—	—
Acquisitions of non-controlling interests of subsidiaries	—	(318)	—	—	—	—	—	—	(318)	(617)	(935)
Distribution to Sinopec Group Company (Note 28 (b))	—	(202)	—	—	—	—	—	—	(202)	—	(202)
Distributions to minority interests net of contributions	—	—	—	—	—	—	—	—	—	(368)	(368)
Balance as of December 31, 2008	<u>86,702</u>	<u>(16,293)</u>	<u>18,072</u>	<u>23,767</u>	<u>43,078</u>	<u>47,000</u>	<u>774</u>	<u>125,569</u>	<u>328,669</u>	<u>20,653</u>	<u>349,322</u>

See accompanying notes to consolidated financial statements.



**CHINA PETROLEUM & CHEMICAL CORPORATION AND SUBSIDIARIES**

**CONSOLIDATED STATEMENTS OF CASH FLOWS  
FOR THE YEARS ENDED DECEMBER 31, 2006, 2007 AND 2008  
(Amounts in millions)**

	Note	Years ended December 31,		
		2006	2007	2008
		RMB	RMB	RMB
<b>Net cash generated from operating activities</b>	(a)	92,507	119,594	67,712
<b>Investing activities</b>				
Capital expenditure		(71,278)	(99,946)	(99,636)
Exploratory wells expenditure		(7,985)	(9,913)	(8,380)
Purchase of investments and investments in associates		(3,763)	(1,581)	(3,089)
Purchase of subsidiaries, net of cash acquired		(1,361)	(3,968)	—
Proceeds from disposal of investments and investments in associates		776	1,441	1,366
Proceeds from disposal of property, plant and equipment		415	413	263
Acquisitions of non-controlling interests of subsidiaries		(20,610)	—	(598)
Purchase of time deposits with financial institutions		(916)	(3,373)	(1,442)
Proceeds from maturity of time deposits with financial institutions		1,337	3,340	1,358
<b>Net cash used in investing activities</b>		<u>(103,385)</u>	<u>(113,587)</u>	<u>(110,158)</u>
<b>Financing activities</b>				
Proceeds of issuance of convertible bonds, net of issuance costs		—	11,368	29,850
Proceeds of issuance of corporate bonds		22,689	35,000	15,000
Proceeds from bank and other loans		773,842	768,039	1,147,279
Repayments of corporate bonds		(21,000)	(12,000)	(10,000)
Repayments of bank and other loans		(761,569)	(788,793)	(1,125,333)
Distributions to minority interests		(852)	(593)	(1,404)
Contributions from minority interests		1,255	1,223	1,137
Dividend paid		(11,271)	(13,872)	(12,572)
Distributions to Sinopec Group Company		(216)	(5,682)	(2,180)
<b>Net cash generated from / (used in) financing activities</b>		<u>2,878</u>	<u>(5,310)</u>	<u>41,777</u>
<b>Net (decrease) / increase in cash and cash equivalents</b>		<u>(8,000)</u>	<u>697</u>	<u>(669)</u>
<b>Cash and cash equivalents as of January 1</b>		15,088	7,063	7,696
<b>Effect of foreign currency exchange rate changes</b>		<u>(25)</u>	<u>(64)</u>	<u>(79)</u>
<b>Cash and cash equivalents as of December 31</b>		<u><u>7,063</u></u>	<u><u>7,696</u></u>	<u><u>6,948</u></u>

See accompanying notes to consolidated financial statements.

CHINA PETROLEUM & CHEMICAL CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED STATEMENTS OF CASH FLOWS  
FOR THE YEARS ENDED DECEMBER 31, 2006, 2007 AND 2008  
(Amounts in millions)

(a) Reconciliation of earnings before income tax to net cash generated from operating activities

	Years ended December 31,		
	2006	2007	2008
	RMB	RMB	RMB
<b>Operating activities</b>			
<b>Earnings before income tax</b>	78,542	83,464	24,317
Adjustment for:			
Depreciation, depletion and amortization	33,554	43,315	45,823
Dry hole costs	3,960	6,060	4,236
Income from associates and jointly controlled entities	(3,434)	(4,044)	(580)
Investment income	(289)	(1,657)	(390)
Interest income	(538)	(405)	(445)
Interest expense	7,101	7,314	11,326
Unrealized gain on foreign currency exchange rate changes and derivative financial instruments	(657)	(1,463)	(2,228)
Loss / (gain) on disposal of property, plant and equipment, net impairment losses on long-lived assets	1,647	549	(248)
Gain on non-monetary contribution to a jointly controlled entity	—	(1,315)	—
Unrealized loss / (gain) on embedded derivative component of the convertible bonds	—	3,211	(3,947)
	120,711	138,135	86,364
(Increase) / decrease in trade accounts receivable	(2,187)	(6,613)	10,817
(Increase) / decrease in bills receivable	(1,729)	(4,130)	9,193
(Increase) / decrease in inventories	(2,901)	(20,493)	20,799
Decrease / (increase) in prepaid expenses and other current assets	583	(2,536)	(10,581)
Increase in lease prepayments	(577)	(4,128)	(2,593)
(Increase) / decrease in long-term prepayments and other assets	(1,111)	3,288	1,928
(Decrease) / increase in trade accounts payable	(1,278)	39,176	(37,234)
(Decrease) / increase in bills payable	(1,511)	(9,710)	5,331
Increase in accrued expenses and other payables	10,148	18,396	11,269
Increase / (decrease) in other liabilities	36	(207)	442
	120,184	151,178	95,735
Interest received	541	404	446
Interest paid	(8,525)	(6,971)	(11,079)
Investment and dividend income received	649	2,657	3,682
Income tax paid	(20,342)	(27,674)	(21,072)
<b>Net cash generated from operating activities</b>	<u>92,507</u>	<u>119,594</u>	<u>67,712</u>

See accompanying notes to consolidated financial statements.

# CHINA PETROLEUM & CHEMICAL CORPORATION AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Amounts in millions, except per share data and except otherwise stated)

### 1. PRINCIPAL ACTIVITIES, ORGANIZATION AND BASIS OF PRESENTATION

#### *Principal activities*

China Petroleum & Chemical Corporation (the “Company”) is an energy and chemical company that, through its subsidiaries (hereinafter collectively referred to as the “Group”), engages in oil and gas and chemical operations in the People’s Republic of China (the “PRC”). Oil and gas operations consist of exploring for, developing and producing crude oil and natural gas; transporting crude oil and natural gas by pipelines; refining crude oil into finished petroleum products; and marketing crude oil, natural gas and refined petroleum products. Chemical operations include the manufacture and marketing of a wide range of chemicals for industrial uses.

#### *Organization*

The Company was established in the PRC on February 25, 2000 as a joint stock limited company as part of the reorganization (the “Reorganization”) of China Petrochemical Corporation (“Sinopec Group Company”), the ultimate holding company of the Group and a ministry-level enterprise under the direct supervision of the State Council of the PRC. Prior to the incorporation of the Company, the oil and gas and chemical operations of the Group were carried on by oil administration bureau, petrochemical and refining production enterprises and sales and marketing companies of Sinopec Group Company.

As part of the Reorganization, certain of Sinopec Group Company’s core oil and gas and chemical operations and businesses together with the related assets and liabilities were transferred to the Company. On February 25, 2000, in consideration for Sinopec Group Company transferring such oil and gas and chemical operations and businesses and the related assets and liabilities to the Company, the Company issued 68.8 billion domestic state-owned ordinary shares with a par value of RMB 1.00 each to Sinopec Group Company. The shares issued to Sinopec Group Company on February 25, 2000 represented the entire registered and issued share capital of the Company as of that date. The oil and gas and chemical operations and businesses transferred to the Company related to (i) the exploration, development and production of crude oil and natural gas, (ii) the refining, transportation, storage and marketing of crude oil and petroleum products, and (iii) the production and sale of chemicals.

#### *Basis of preparation*

Pursuant to the resolution passed at the Directors’ meeting on October 10, 2006, the Group acquired equity interests in Sinopec Hainan Refining and Chemical Company Limited (“Sinopec Hainan”) for cash of RMB 2,990 (hereinafter referred to as the “Acquisition of Sinopec Hainan”). Sinopec Hainan was previously wholly owned by Sinopec Group Company.

Pursuant to the resolution passed at the Directors’ meeting on December 6, 2006, the Group acquired the equity interests in certain oil and gas production companies (“Oil Production Plants”) from Sinopec Group Company, for cash of RMB 3,500 (hereinafter referred to as the “Acquisition of Oil Production Plants”).

Pursuant to the resolution passed at the Directors’ meeting on December 28, 2007, the Group acquired the controlling equity interests of Zhanjiang Dongxing Petrochemical Company Limited, Sinopec Hangzhou Oil Refinery Plant, Yangzhou Petrochemical Plant, Jiangsu Taizhou Petrochemical Plant and Sinopec Qingjiang Petrochemical Company Limited (collectively “Refinery Plants”) from Sinopec Group Company (hereinafter referred to as the “Acquisition of Refinery Plants”). In accordance with the acquisition agreement with Sinopec Group Company, the Group paid a cash consideration of RMB 2,468 to Sinopec Group Company during the year ended December 31, 2007, which is subject to further adjustment, if any, made by State-owned Assets Supervision and Administration Commission of the State Council (“SASAC”). During the year ended December 31, 2008, the consideration was adjusted by SASAC and the Group paid an additional cash consideration of RMB 96 to Sinopec Group Company.

As the Group, Sinopec Hainan, Oil Production Plants and Refinery Plants are under the common control of Sinopec Group Company, the Acquisitions of Sinopec Hainan, Oil Production Plants and Refinery Plants (collectively the “Acquired Group”) have been reflected in the accompanying consolidated financial statements as combination of entities under common control in a manner similar to a pooling-of-interests. Accordingly, the assets and liabilities of the Acquired Group have been accounted for at historical cost and the consolidated financial statements of the Company prior to these acquisitions have been restated to include the results of operations and the assets and liabilities of the Acquired Group on a combined basis. The differences between the total consideration paid over the amount of the net assets of the Acquired Group were accounted for as equity transactions.

## CHINA PETROLEUM & CHEMICAL CORPORATION AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued) (Amounts in millions, except per share data and except otherwise stated)

The accompanying financial statements have been prepared in accordance with International Financial Reporting Standards (“IFRS”) as issued by the International Accounting Standards Board (“IASB”). IFRS includes International Accounting Standards (“IAS”) and related interpretations. A summary of the principal accounting policies adopted by the Group are set out in Note 2.

The IASB has issued certain new and revised IFRS that are first effective or available for early adoption for the current accounting period of the Group. There have been no significant changes to the accounting policies applied in these financial statements for the years presented as a result of these developments, except for the early adoption of revised IFRS 3 “Business Combinations” ( “revised IFRS 3”) and the amended IAS 27 “Consolidated and Separate Financial Statements” ( “amended IAS 27”). The impact of the early adoptions of revised IFRS 3 and amended IAS 27, which have been applied prospectively, is that any changes in the Company’s ownership interests in a subsidiary on or after January 1, 2008 that do not result in a loss of control are recognized as equity transactions. The early adoptions of revised IFRS 3 and amended IAS 27 did not have a significant impact to the Group’s consolidated financial statements for the year ended December 31, 2008.

The Group has not adopted any other new standard or interpretation that is not yet effective for the current accounting period (Note 36).

The accompanying financial statements are prepared on the historical cost basis as modified by the revaluation of certain property, plant and equipment (Note 2(f)) and by the remeasurement of available-for-sale securities (Note 2(k)), derivative financial instruments (Note 2(p)) and derivative component of the convertible bonds (Note 2(o)) to their fair values.

The preparation of the financial statements in accordance with IFRS requires management to make judgments, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the year. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results could differ from those estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

Key assumptions and estimation made by management in the application of IFRS that have significant effect on the financial statements and have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities in the following financial year are disclosed in Note 35.

## 2. PRINCIPAL ACCOUNTING POLICIES

### (a) Basis of consolidation

The consolidated financial statements comprise the Company and its subsidiaries, and the Group’s interest in associates and jointly controlled entities.

### (i) Subsidiaries

Subsidiaries are those entities controlled by the Group. Control exists when the Group has the power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

The financial statements of subsidiaries are included in the consolidated financial statements from the date that control effectively commences until the date that control effectively ceases.

## CHINA PETROLEUM & CHEMICAL CORPORATION AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued) (Amounts in millions, except per share data and except otherwise stated)

Minority interests at the balance sheet date, being the portion of the net assets of subsidiaries attributable to equity interests that are not owned by the Company, whether directly or indirectly through subsidiaries, are presented in the consolidated balance sheet and consolidated statements of equity within equity, separately from equity attributable to the equity shareholders of the Company. Minority interests in the results of the Group are presented on the face of the consolidated statements of income as an allocation of the total net income or loss for the period between minority interests and the equity shareholders of the Company.

The particulars of the Group's principal subsidiaries are set out in Note 33.

#### (ii) Associates and jointly controlled entities

An associate is an entity, not being a subsidiary, in which the Group exercises significant influence over its management. Significant influence is the power to participate in the financial and operating policy decisions of the investee but is not control or joint control over those policies.

A jointly controlled entity is an entity which operates under a contractual arrangement between the Group and other parties, where the contractual arrangement establishes that the Group and one or more of the other parties share joint control over the economic activity of the entity.

Investments in associates and jointly controlled entities are accounted for in the consolidated financial statements using the equity method from the date that significant influence or joint control commences until the date that significant influence or joint control ceases.

#### (iii) Transactions eliminated on consolidation

Inter-company balances and transactions and any unrealized gains arising from inter-company transactions are eliminated on consolidation. Unrealized gains arising from transactions with associates and jointly controlled entities are eliminated to the extent of the Group's interest in the entity. Unrealized losses are eliminated in the same way as unrealized gains, but only to the extent that there is no evidence of impairment.

#### (b) Translation of foreign currencies

The presentation currency of the Group is Renminbi. Foreign currency transactions during the year are translated into Renminbi at the applicable rates of exchange quoted by the People's Bank of China ("PBOC") prevailing on the transaction dates. Foreign currency monetary assets and liabilities are translated into Renminbi at the PBOC's rates at the balance sheet date.

Exchange differences, other than those capitalized as construction in progress, are recognized as income or expenses in the "finance costs" section of the consolidated statements of income.

#### (c) Cash and cash equivalents

Cash equivalents consist of time deposits with financial institutions with an initial term of less than three months when purchased. Cash equivalents are stated at cost, which approximates fair value.

#### (d) Trade, bills and other receivables

Trade, bills and other receivables are initially recognized at fair value and thereafter stated at amortized cost less impairment losses for bad and doubtful debts (Note 2(1)). Trade, bills and other receivables are derecognized if the Group's contractual rights to the cash flows from these financial assets expire or if the Group transfers these financial asset to another party without retaining control or substantially all risks and rewards of the assets.

#### (e) Inventories

Inventories, other than spare parts and consumables, are stated at the lower of cost and net realizable value. Cost includes the cost of purchase computed using the weighted average method and, in the case of work in progress and finished goods, direct labor and an appropriate proportion of production overheads. Net realizable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and the estimated costs necessary to make the sale.

Spare parts and consumables are stated at cost less any provision for obsolescence.

## CHINA PETROLEUM & CHEMICAL CORPORATION AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued) (Amounts in millions, except per share data and except otherwise stated)

#### (f) Property, plant and equipment

An item of property, plant and equipment is initially recorded at cost, less accumulated depreciation and impairment losses (Note 2(1)). The cost of an asset comprises its purchase price, any directly attributable costs of bringing the asset to working condition and location for its intended use. Subsequent to the revaluation, which was based on depreciated replacement costs, property, plant and equipment are carried at revalued amount, being the fair value at the date of the revaluation less any subsequent accumulated depreciation and impairment losses. Revaluations are performed periodically to ensure that the carrying amount does not differ materially from that which would be determined using fair value at the balance sheet date. The Group recognizes in the carrying amount of an item of property, plant and equipment the cost of replacing part of such an item when that cost is incurred if it is probable that the future economic benefits embodied with the item will flow to the Group and the cost of the item can be measured reliably. All other expenditure is recognized as an expense in the consolidated statements of income in the year in which it is incurred.

Gains or losses arising from the retirement or disposal of an item of property, plant and equipment, other than oil and gas properties, are determined as the difference between the net disposal proceeds and the carrying amount of the item and are recognized as income or expense in the consolidated statements of income on the date of retirement or disposal. On disposal of a revalued asset, the related revaluation surplus is transferred from the revaluation reserve to retained earnings.

Depreciation is provided to write off the cost / revalued amount of items of property, plant and equipment, other than oil and gas properties, over its estimated useful life on a straight-line basis, after taking into account its estimated residual value, as follows:

Buildings	15 to 45 years
Plant, machinery, equipment, and others	4 to 18 years
Oil depots, storage tanks and service stations	8 to 25 years

Where parts of an item of property, plant and equipment have different useful lives, the cost or valuation of the item is allocated on a reasonable basis between the parts and each part is depreciated separately. Both the useful life of an asset and its residual value, if any, are reassessed annually.

#### (g) Oil and gas properties

The Group uses the successful efforts method of accounting for its oil and gas producing activities. Under this method, costs of development wells and the related support equipment are capitalized. The cost of exploratory wells is initially capitalized as construction in progress pending determination of whether the well has found proved reserves. The impairment of exploratory well costs occurs upon the determination that the well has not found proved reserves. Exploratory wells that find oil and gas reserves in any area requiring major capital expenditure are expensed unless the well has found a sufficient quantity of reserves to justify its completion as a producing well if the required capital expenditure is made, and drilling of the additional exploratory wells is under way or firmly planned for the near future. However, in the absence of a determination of the discovery of proved reserves, exploratory well costs are not carried as an asset for more than one year following completion of drilling. If, after one year has passed, a determination of the discovery of proved reserves cannot be made, the exploratory well costs are impaired and charged to expense. All other exploration costs, including geological and geophysical costs, other dry hole costs and annual lease rentals, are expensed as incurred. Capitalized costs relating to proved properties are amortized at the field level on a unit-of-production method. The amortization rates are determined based on oil and gas reserves estimated to be recoverable from existing facilities over the shorter of the economic lives of crude oil and natural gas reservoirs and the terms of the relevant production licenses.

Gains and losses on the disposal of proved oil and gas properties are not recognized unless the disposal encompasses an entire property. The proceeds on such disposals are credited to the carrying amounts of oil and gas properties.

Management estimates future dismantlement costs for oil and gas properties with reference to engineering estimates after taking into consideration the anticipated method of dismantlement required in accordance with the industry practices. These estimated future dismantlement costs are discounted at a credit-adjusted risk-free rate and are capitalized as oil and gas properties, which are subsequently amortized as part of the costs of the oil and gas properties.

## CHINA PETROLEUM & CHEMICAL CORPORATION AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued) (Amounts in millions, except per share data and except otherwise stated)

#### (h) Lease prepayments

Lease prepayments represent land use rights paid to the relevant government authorities. Land use rights are carried at cost less the accumulated amount charged to expense and impairment losses (Note 2(l)). The cost of lease prepayments are charged to expense on a straight-line basis over the respective periods of the rights.

#### (i) Construction in progress

Construction in progress represents buildings, oil and gas properties, various plant and equipment under construction and pending installation, and is stated at cost less impairment losses (Note 2(l)). Cost comprises direct costs of construction as well as interest charges, and foreign exchange differences on related borrowed funds to the extent that they are regarded as an adjustment to interest charges, during the periods of construction.

Construction in progress is transferred to property, plant and equipment when the asset is substantially ready for its intended use.

No depreciation is provided in respect of construction in progress.

#### (j) Goodwill

Goodwill represents amounts arising on acquisition of subsidiaries, associates or jointly controlled entities. Goodwill represents the difference between the cost of acquisition and the fair value of the net identifiable assets acquired.

Prior to January 1, 2008, the acquisition of the minority interests (or non-controlling interests) of a consolidated subsidiary was accounted using the acquisition method whereby the difference between the cost of acquisition and the fair value of the net identifiable assets acquired (on a proportionate share) was recognized as goodwill. From January 1, 2008, any difference between the amount by which the non-controlling interest is adjusted (such as through an acquisition of the non-controlling interests) and the cash or other considerations paid is recognized in equity.

Goodwill is stated at cost less accumulated impairment losses. Goodwill is allocated to cash-generating units and is tested annually for impairment (Note 2(l)). In respect of associates and jointly controlled entities, the carrying amount of goodwill is included in the carrying amount of the interest in the associates or jointly controlled entities.

#### (k) Investments

Investment in available-for-sale financial assets are carried at fair value with any change in fair value recognized directly in equity. When these investments are derecognized or impaired, the cumulative gain or loss previously recognized directly in equity is recognized in the consolidated statements of income. Investments in equity securities, other than investments in associates and jointly controlled entities, that do not have a quoted market price in an active market and whose fair value cannot be reliably measured are recognized in the balance sheet at cost less impairment losses (Note 2(l)).

#### (l) Impairment of assets

(i) Trade accounts receivable, other receivables and investment in equity securities that do not have an quoted market price in an active market, other than investments in associates and jointly controlled entities, are reviewed at each balance sheet date to determine whether there is objective evidence of impairment. If any such evidence exists, an impairment loss is determined and recognized.

The impairment loss is measured as the difference between the asset's carrying amount and the estimated future cash flows, discounted at the current market rate of return for a similar financial asset where the effect of discounting is material, and is recognized as an expense in the consolidated statements of income. Impairment losses for trade and other receivables are reversed through the consolidated statements of income if in a subsequent period the amount of the impairment losses decreases. Impairment losses for equity securities are not reversed.

## CHINA PETROLEUM & CHEMICAL CORPORATION AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued) (Amounts in millions, except per share data and except otherwise stated)

(ii) Impairment of other long-lived assets is accounted for as follows:

The carrying amounts of other long-lived assets, including property, plant and equipment, construction in progress, lease prepayment and investments in associates and jointly controlled entities, are reviewed at each balance sheet date to identify indicators that the assets may be impaired. These assets are tested for impairment whenever events or changes in circumstances indicate that their recorded carrying amounts may not be recoverable. When such a decline has occurred, the carrying amount is reduced to the recoverable amount. For goodwill, the recoverable amount is estimated at each balance sheet date.

The recoverable amount is the greater of the fair value less costs to sell and the value in use. In determining the value in use, expected future cash flows generated by the asset are discounted to their present value using a pre-tax discount rate that reflects current market assessments of time value of money and the risks specific to the asset. Where an asset does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the smallest group of assets that generates cash inflows independently (i.e. a cash-generating unit).

The amount of the reduction is recognized as an expense in the consolidated statements of income unless the asset is carried at revalued amount for which an impairment loss is recognized directly against any related revaluation reserve to the extent that the impairment loss does not exceed the amount held in the revaluation reserve for that same asset. Impairment losses recognized in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to the cash-generating unit and then, to reduce the carrying amount of the other assets in the unit on a pro rata basis, except that the carrying value of an asset will not be reduced below its individual fair value less costs to sell, or value in use, if determinable.

Management assesses at each balance sheet date whether there is any indication that an impairment loss recognized for an asset, except in the case of goodwill, in prior years may no longer exist. An impairment loss is reversed if there has been a favorable change in the estimates used to determine the recoverable amount. A subsequent increase in the recoverable amount of an asset, when the circumstances and events that led to the write-down or write-off cease to exist, is recognized as an income unless the asset is carried at revalued amount. Reversal of an impairment loss on a revalued asset is credited to the revaluation reserve except for impairment loss which was previously recognized as an expense in the consolidated statements of income; a reversal of such impairment loss is recognized as an income. The reversal is reduced by the amount that would have been recognized as depreciation had the write-down or write-off not occurred. An impairment loss in respect of goodwill is not reversed.

#### **(m) Trade, bills and other payables**

Trade, bills and other payables are initially recognized at fair value and thereafter stated at amortized cost unless the effect of discounting would be immaterial, in which case they are stated at cost.

#### **(n) Interest-bearing borrowings**

Interest bearing borrowings are recognized initially at fair value less attributable transaction costs. Subsequent to initial recognition, interest-bearing borrowings are stated at amortized cost with any difference between cost and redemption value being recognized in the consolidated statements of income over the period of borrowings using the effective interest method.

#### **(o) Convertible bonds**

(i) Convertible bonds that contain an equity component

Convertible bonds that can be converted to equity share capital at the option of the holder, where the number of shares that would be issued on conversion and the value of the consideration that would be received at that time do not vary, are accounted for as compound financial instruments that contain both a liability component and an equity component.

At initial recognition, the liability component of the convertible bonds is measured as the present value of the future interest and principal payments, discounted at the market rate of interest applicable at the time of initial recognition to similar liabilities that do not have a conversion option. Any excess of proceeds over the amount initially recognized as the liability component is recognized as the equity component. Transaction costs that relate to the issuance of the convertible bonds are allocated to the liability and equity components in proportion to the allocation of proceeds.



## CHINA PETROLEUM & CHEMICAL CORPORATION AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued) (Amounts in millions, except per share data and except otherwise stated)

The liability component is subsequently carried at amortized cost. The interest expense on the liability component is calculated using the effective interest method. The equity component is recognized in the capital reserve until the bond is converted or redeemed.

If the bond is converted, the capital reserve, together with the carrying amount of the liability component at the time of conversion, is transferred to share capital and share premium as consideration for the shares issued. If the bond is redeemed, the capital reserve is transferred to retained earnings.

#### (ii) Other convertible bonds

Convertible bonds issued with a cash settlement option and other embedded derivative features are accounted for as compound financial instruments that contain a liability component and a derivative component.

At initial recognition, the derivative component of the convertible bonds is measured at fair value. Any excess of proceeds over the amount initially recognized as the derivative component is recognized as the liability component. Transaction costs that relate to the issuance of the convertible bonds are allocated to the liability and derivative components in proportion to the allocation of proceeds. The portion of the transaction costs relating to the liability component is recognized initially as part of the liability. The portion relating to the derivative component is recognized immediately as an expense in the consolidated statements of income.

The derivative component is subsequently remeasured at each balance sheet date and any gains or losses arising from change in the fair value are recognized in the consolidated statements of income. The liability component is subsequently carried at amortized cost until extinguished on conversion or redemption. The interest expense recognized in the consolidated statements of income on the liability component is calculated using the effective interest method. Both the liability and the related derivative components are presented together for financial statements reporting purposes.

If the convertible bonds are converted, the carrying amounts of the derivative and liability components are transferred to share capital and share premium as consideration for the shares issued. If the convertible bonds are redeemed, any difference between the amount paid and the carrying amounts of both components is recognized in the consolidated statements of income.

#### (p) Derivative financial instruments

Derivative financial instruments are recognized initially at fair value. At each balance sheet date the fair value is remeasured. The gain or loss on remeasurement of derivative financial instruments to fair value, except where the derivatives qualify for cash flow hedge accounting or hedge the net investment in a foreign operation, is recognized in the consolidated statements of income.

#### (q) Provisions and contingent liability

A provision is recognized for liability of uncertain timing or amount when the Group has a legal or constructive obligation arising as a result of a past event, it is probable that an outflow of economic benefits will be required to settle the obligation and a reliable estimate can be made.

## CHINA PETROLEUM & CHEMICAL CORPORATION AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued) (Amounts in millions, except per share data and except otherwise stated)

When it is not probable that an outflow of economic benefits will be required, or the amount cannot be estimated reliably, the obligation is disclosed as a contingent liability, unless the probability of outflow of economic benefits is remote. Possible obligations, whose existence will only be confirmed by the occurrence or non-occurrence of one or more future events are also disclosed as contingent liabilities unless the probability of outflow of economic benefits is remote.

Provisions for future dismantlement costs are initially recognized based on the present value of the future costs expected to be incurred in respect of the Group's expected dismantlement and abandonment costs at the end of related oil and gas exploration and development activities. Any subsequent change in the present value of the estimated costs, other than the change due to passage of time which is regarded as interest cost, is reflected as an adjustment to the provision and oil and gas properties.

A provision for onerous contracts is recognized when the expected economic benefits to be derived by the Group from a contract are lower than the unavoidable cost of meeting its obligations under the contract. The provision is measured at the present value of the lower of the expected cost of terminating the contract and the expected net cost of continuing with the contract.

#### **(r) Revenue recognition**

Revenues associated with the sale of crude oil, natural gas, petroleum and chemical products and ancillary materials are recorded when the customer accepts the goods and the significant risks and rewards of ownership and title have been transferred to the buyer. Revenue from the rendering of services is recognized in the consolidated statements of income upon performance of the services. No revenue is recognized if there are significant uncertainties regarding recovery of the consideration due, the possible return of goods, or when the amount of revenue and the costs incurred or to be incurred in respect of the transaction cannot be measured reliably.

Interest income is recognized on a time apportioned basis that takes into account the effective yield on the asset.

A government grant that becomes receivable as compensation for expenses or losses already incurred with no future related costs is recognized as income in the period in which it becomes receivable.

#### **(s) Borrowing costs**

Borrowing costs are expensed in the consolidated statements of income in the period in which they are incurred, except to the extent that they are capitalized as being attributable to the construction of an asset which necessarily takes a period of time to get ready for its intended use.

#### **(t) Repairs and maintenance expenditure**

Repairs and maintenance expenditure is expensed as incurred.

#### **(u) Environmental expenditures**

Environmental expenditures that relate to current ongoing operations or to conditions caused by past operations are expensed as incurred.

Liabilities related to future remediation costs are recorded when environmental assessments and / or cleanups are probable and the costs can be reasonably estimated. As facts concerning environmental contingencies become known to the Group, the Group reassesses its position both with respect to accrued liabilities and other potential exposures.

#### **(v) Research and development expense**

Research and development expenditures are expensed in the period in which they are incurred. Research and development expense amounted to RMB 2,902, RMB 3,419 and RMB 3,427 for the years ended December 31, 2006, 2007 and 2008, respectively.

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### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued) (Amounts in millions, except per share data and except otherwise stated)

#### (w) Operating leases

Operating lease payments are charged to the consolidated statements of income on a straight-line basis over the period of the respective leases.

#### (x) Employee benefits

The contributions payable under the Group's retirement plans are recognized as an expense in the consolidated statements of income as incurred and according to the contribution determined by the plans. Further information is set out in Note 31.

Termination benefits, such as employee reduction expenses, are recognized when, and only when, the Group demonstrably commits itself to terminate employment or to provide benefits as a result of voluntary redundancy by having a detailed formal plan which is without realistic possibility of withdrawal.

#### (y) Income tax

Income tax comprises current and deferred tax. Current tax is calculated on taxable income by applying the applicable tax rates. Deferred tax is provided using the balance sheet liability method on all temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes only to the extent that it is probable that future taxable income will be available against which the assets can be utilized. Deferred tax is calculated on the basis of the enacted tax rates that are expected to apply in the period when the asset is realized or the liability is settled. The effect on deferred tax of any changes in tax rates is charged or credited to the consolidated statements of income, except for the effect of a change in tax rate on the carrying amount of deferred tax assets and liabilities which were previously charged or credited to equity.

The tax value of losses expected to be available for utilization against future taxable income is set off against the deferred tax liability within the same legal tax unit and jurisdiction to the extent appropriate, and is not available for set off against the taxable profit of another legal tax unit. The carrying amount of a deferred tax asset is reviewed at each balance sheet date and is reduced to the extent that it is no longer probable that the related tax benefit will be realized.

#### (z) Dividends

Dividends are recognized as a liability in the period in which they are declared.

#### (aa) Segmental reporting

A business segment is a distinguishable component of the Group that is engaged in providing products or services and is subject to risks and rewards that are different from those of other segments.

The segments were determined primarily because the Group manages its exploration and production, refining, marketing and distribution, chemicals, and corporate and others businesses separately. The reportable segments are each managed separately because they manufacture and / or distribute distinct products with different production processes and due to their distinct operating and gross margin characteristics. In view of the fact that the Company and its subsidiaries operate mainly in the PRC, no geographical segment information is presented.

Management evaluates the performance and allocates resources to its operating segments on an operating income basis, without considering the effects of finance costs or investment income. Corporate administrative costs and assets are not allocated to the operating segments; instead, operating segments are billed for direct corporate services. Inter-segment transfer pricing is based on cost plus an appropriate margin, as specified by the Group's policy.

Assets and liabilities dedicated to a particular segment's operations are included in that segment's total assets and liabilities. Assets which benefit more than one segment or are considered to be corporate assets are not allocated. "Unallocated assets" consists primarily of cash and cash equivalents, time deposits with financial institutions, investments, deferred tax assets and other non-current assets. "Unallocated liabilities" consists

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primarily of short-term and long-term debts, loans from Sinopec Group Company and its affiliates, income tax payable and deferred tax liabilities.

Interest in and share of income from associates and jointly controlled entities are included in the segments in which the associates and jointly controlled entities operate.

**3. OTHER OPERATING REVENUES**

	<b>Years ended December 31,</b>		
	<b>2006</b>	<b>2007</b>	<b>2008</b>
	<b>RMB</b>	<b>RMB</b>	<b>RMB</b>
Sale of materials, service and others	26,469	30,604	31,289
Rental income	384	370	491
	<u>26,853</u>	<u>30,974</u>	<u>31,780</u>

**4. OTHER INCOME**

During the years ended December 31, 2006, 2007 and 2008, the Group recognized grant income of RMB 5,161, RMB 4,863 and RMB 50,342, respectively. These government grants were for compensation of losses incurred due to the distortion of the correlation of domestic refined petroleum product prices and the crude oil prices, and the measures taken by the Group to stabilize the supply in the PRC refined petroleum product market during the respective years. There are no unfulfilled conditions and other contingencies attached to the receipts of these grants. There is no assurance that the Group will continue to receive such grant in the future.

**5. SELLING, GENERAL AND ADMINISTRATIVE EXPENSES**

The following items are included in selling, general and administrative expenses:

	<b>Years ended December 31,</b>		
	<b>2006</b>	<b>2007</b>	<b>2008</b>
	<b>RMB</b>	<b>RMB</b>	<b>RMB</b>
Operating lease charges	6,116	5,897	6,986
Impairment losses			
- trade accounts receivable	438	295	143
- other receivables	107	143	85
	<u>6,661</u>	<u>6,335</u>	<u>7,214</u>

**6. PERSONNEL EXPENSES**

	<b>Years ended December 31,</b>		
	<b>2006</b>	<b>2007</b>	<b>2008</b>
	<b>RMB</b>	<b>RMB</b>	<b>RMB</b>
Wages and salaries	15,679	17,763	17,669
Staff welfare	2,012	885	1,271
Contributions to retirement schemes (Note 31)	2,394	2,806	2,861
Social security contributions	871	1,291	1,484
	<u>20,956</u>	<u>22,745</u>	<u>23,285</u>

**7. TAXES OTHER THAN INCOME TAX**

	<b>Years ended December 31,</b>		
	<b>2006</b>	<b>2007</b>	<b>2008</b>
	<b>RMB</b>	<b>RMB</b>	<b>RMB</b>
Consumption tax	14,718	16,324	17,524
Special oil income levy	8,747	11,208	32,823
City construction tax	3,096	3,670	3,340
Education surcharge	1,651	1,922	1,828
Resources tax	854	882	857
Business tax	264	298	427
	<u>29,330</u>	<u>34,304</u>	<u>56,799</u>

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Consumption tax is levied on producers of gasoline, diesel, naphtha, fuel oil, jet fuel, lubricant oil and solvent oil based on a tariff rate applied to the volume of sales. Special oil income levy is levied on oil exploration and production entities based on the progressive rates ranging from 20% to 40% on the portion of the monthly weighted average sales price of the crude oil produced in the PRC exceeding USD 40 per barrel. City construction tax is levied on an entity based on its total amount of value-added tax, consumption tax and business tax.

**8. OTHER OPERATING EXPENSES, NET**

	<b>Years ended December 31,</b>		
	<b>2006</b>	<b>2007</b>	<b>2008</b>
	<b>RMB</b>	<b>RMB</b>	<b>RMB</b>
Fines, penalties and compensations	65	73	105
Donations	98	158	104
Employee reduction expenses (i)	236	399	306
Loss / (gain) on disposal of property, plant and equipment, net	1,647	549	(248)
Impairment losses on long-lived assets			
(ii)	825	3,106	8,500
Gain on non-monetary contribution to a jointly controlled entity			
(iii)	—	(1,315)	—
Gain from debt extinguishment (iv)	(486)	—	—
Others	312	631	6
	<u>2,697</u>	<u>3,601</u>	<u>8,773</u>

Note:

(i) During the year ended December 31, 2006, in accordance with the Group's voluntary employee reduction plan, the Group recorded employee reduction expenses of RMB 236 in respect of the voluntary termination of approximately 4,000 employees.

During the year ended December 31, 2007, in accordance with the Group's voluntary employee reduction plan, the Group recorded employee reduction expenses of RMB 399 in respect of the voluntary termination of approximately 5,000 employees.

During the year ended December 31, 2008, in accordance with the Group's voluntary employee reduction plan, the Group recorded employee reduction expenses of RMB 306 in respect of the voluntary termination of approximately 4,900 employees.

(ii) The primary factor resulting in the exploration and production ("E&P") segment impairment losses of RMB 552, RMB 481 and RMB 5,991 for the years ended December 31, 2006, 2007 and 2008, respectively, that comprised of impairment losses of RMB 552, RMB 481 and RMB 4,600 of property, plant and equipment in the E&P segment (Note 15) for the years ended December 31, 2006, 2007 and 2008, respectively, and RMB 1,391 of goodwill in respect of Sinopec Zhongyuan (Note 17) for the year ended December 31, 2008, was downward reserves estimation for certain oil fields resulting from lower oil and gas pricing. The carrying values of these E&P properties and associated goodwill were written down to respective recoverable amounts which were determined based on the present values of the expected future cash flows of the assets. The oil and gas pricing was a factor used in the determination of the present values of the expected future cash flows of the assets and had an impact on the recognition of the asset and goodwill impairment.

Impairment losses recognized on long-lived assets of the refining segment were RMB nil, RMB 1,070 and RMB 270 for the years ended December 31, 2006, 2007 and 2008, respectively, that comprised of impairment losses of RMB 916 and RMB 270 of property, plant and equipment for the years ended December 31, 2007 and 2008, respectively, and an impairment loss of RMB 154 of construction in progress for the year ended December 31, 2007. Impairment losses recognized on property, plant and equipment of the chemicals segment were RMB 250, RMB 318 and RMB 1,511 for the years ended December 31, 2006, 2007 and 2008, respectively. These impairment losses relate to certain refining and chemicals production facilities that are held for use and a refining construction in progress. The carrying values of these facilities were written down to their recoverable amounts that were primarily determined based on the asset held for use model using the present value of estimated future cash flows of the production facilities. The primary factor resulting in the impairment losses on long-lived assets of the refining and chemicals segments was due to the drop in profit margin caused by the adverse changes in the business environment.

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Impairment losses recognized on long-lived assets of the marketing and distribution segment of RMB 23, RMB 1,237 and RMB 709 for the years ended December 31, 2006, 2007 and 2008, respectively, that comprised of impairment losses of RMB 23, RMB 1,194 and RMB 698 of property, plant and equipment for the years ended December 31, 2006, 2007 and 2008, respectively, and impairment losses of RMB 43 and RMB 11 of construction in progress for the years ended December 31, 2007 and 2008, respectively, primarily relate to certain service stations and certain construction in progress that were closed or abandoned during respective years. In measuring the amounts of impairment charges, the carrying amounts of these assets were compared to the present value of the expected future cash flows of the assets, as well as information about sales and purchases of similar properties in the same geographic area.

- (iii) During the year ended December 31, 2007, the Group contributed certain property, plant and equipment and construction in progress with carrying amounts of RMB 1,239 and RMB 601, respectively, in exchange for a 50% equity interest in a newly set up jointly controlled entity and recognized a gain of RMB 1,315, representing the portion of the difference between the carrying amount of these assets and their fair value attributable to the equity interests of the other venturer. The other venturer contributed the other 50% equity interest in cash representing the fair values of the property, plant and equipment and construction in progress as determined by a valuation performed by an independent valuer.
- (iv) During the year ended December 31, 2006, a subsidiary of the Group reached an agreement with a bank to waive loan principal balance and related interest payable totaling RMB 486.

**9. INTEREST EXPENSE**

	<b>Years ended December 31,</b>		
	<b>2006</b>	<b>2007</b>	<b>2008</b>
	<b>RMB</b>	<b>RMB</b>	<b>RMB</b>
Interest expense incurred	8,595	7,927	12,465
Less: Interest expense capitalized*	(1,494)	(966)	(1,569)
	<u>7,101</u>	<u>6,961</u>	<u>10,896</u>
Accretion expenses (Note 26)	—	353	430
Interest expense	<u>7,101</u>	<u>7,314</u>	<u>11,326</u>
* Interest rates per annum at which borrowing costs were	3.6% to	3.6% to	3.8% to
Capitalized for construction in progress	<u>6.1%</u>	<u>7.1%</u>	<u>7.1%</u>

**10. INCOME TAX**

Income tax in the consolidated statements of income represents:

	<b>Years ended December 31,</b>		
	<b>2006</b>	<b>2007</b>	<b>2008</b>
	<b>RMB</b>	<b>RMB</b>	<b>RMB</b>
Current tax			
- Provision for the year	23,980	28,628	609
- Under-provision in prior years	260	249	216
Deferred taxation (Note 22)	<u>(736)</u>	<u>(4,156)</u>	<u>(2,708)</u>
	<u>23,504</u>	<u>24,721</u>	<u>(1,883)</u>

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Reconciliation between actual income tax expense / (benefit) and the expected income tax at applicable statutory tax rates is as follows:

	<b>Years ended December 31,</b>		
	<b>2006</b>	<b>2007</b>	<b>2008</b>
	<b>RMB</b>	<b>RMB</b>	<b>RMB</b>
Earnings before income tax	78,542	83,464	24,317
Expected PRC income tax expense at statutory tax rates of 33%, 33% and 25% in 2006, 2007 and 2008, respectively	25,919	27,543	6,079
Tax effect of differential tax rate			
(i)	(2,047)	(1,959)	1,213
Tax effect of non-deductible expenses	535	1,400	864
Tax effect of non-taxable income			
(iii)	(1,438)	(3,767)	(11,203)
Tax effect of tax losses not recognized	324	103	948
Under-provision in prior years	260	249	216
Tax credit for domestic equipment purchases	(49)	(500)	—
Effect of change in tax rate on deferred tax			
(ii)	—	1,652	—
Actual income tax expense / (benefit) .	<u>23,504</u>	<u>24,721</u>	<u>(1,883)</u>

Substantially all earnings before income tax and related tax expense / (benefit) is from PRC sources.

Notes:

- (i) During the years ended December 31, 2006, 2007 and 2008, the provision for PRC current income tax is based on statutory rates of 33%, 33% and 25%, respectively, of the assessable income of the Group as determined in accordance with the relevant income tax rules and regulations of the PRC, except for certain entities of the Group, which are taxed at a preferential rate of 15% or 18%.
- (ii) On March 16, 2007, the Fifth Plenary Session of the Tenth National People's Congress passed the Corporate Income Tax Law of the People's Republic of China ("new tax law"), which took effect on January 1, 2008. According to the new tax law, a unified corporate income tax rate of 25% is applied to PRC entities; however certain entities previously taxed at a preferential rate are subject to a transition period during which their tax rate will gradually be increased to the unified rate of 25% over a five-year period starting from January 1, 2008.

Based on the new tax law, the income tax rate applicable to the Group, except for certain entities of the Group, is reduced from 33% to 25% from January 1, 2008. Based on a tax notice issued by the State Council on December 26, 2007, the applicable tax rates for entities operating in special economic zones, which were previously taxed at the preferential rate of 15%, are 18%, 20%, 22%, 24% and 25% in 2008, 2009, 2010, 2011 and 2012 onward, respectively. According to the same notice, the applicable tax rate for entities operating in the western region of the PRC which were granted a preferential tax rate of 15% from 2004 to 2010, remains at 15% in 2008, 2009 and 2010 and will be increased to 25% from January 1, 2011.

- (iii) The tax effect of non-taxable income for the year ended December 31, 2008 primarily related to the grant income.

**11. BASIC AND DILUTED EARNINGS PER SHARE**

The calculation of basic and diluted earnings per share is based on the net income attributable to ordinary equity shareholders of the Company of RMB 53,603 and RMB 56,533 for the years ended December 31, 2006 and 2007, respectively, and the weighted average number of shares of 86,702,439,000 for each of the years ended December 31, 2006 and 2007. For the year ended December 31, 2007, diluted earnings per share is calculated on the same basis as basic earnings per share, since the effect of the Convertible Bonds (Note 23(f)) was anti-dilutive for that year.

The calculation of basic earnings per share for the year ended December 31, 2008 is based on the net income attributable to ordinary equity shareholders of the Company of RMB 29,769 and the weighted average number of the shares of 86,702,439,000. The calculation of diluted earnings per share for the year ended December 31, 2008 is based on the net income attributable to ordinary equity shareholders of the Company of RMB 26,592 and the weighted average number of the shares of 87,789,799,595 calculated as follows:

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(i) Net income attributable to ordinary equity shareholders of the Company (diluted)

	<b>2008</b>
	<b>RMB</b>
Net income attributable to ordinary equity shareholders of the Company	29,769
After tax effect of exchange gain net of interest expense of the Convertible Bonds	(217)
After tax effect of unrealized gain on embedded derivative component of the Convertible Bonds	(2,960)
Net income attributable to ordinary equity shareholders of the Company (diluted)	<u>26,592</u>

(ii) Weighted average number of shares (diluted)

	<b>2008</b>
	<b>Number of</b>
	<b>shares</b>
Weighted average number of shares as of December 31	86,702,439,000
Effect of conversion of the Convertible Bonds	1,087,360,595
Weighted average number of shares (diluted) as of December 31	<u>87,789,799,595</u>

The calculation of diluted earnings per share for the year ended December 31, 2008 excludes the effect of the Warrants (Note 23 (g)), since it did not have any dilutive effect.

**12. TRADE ACCOUNTS RECEIVABLE, NET**

	<b>December 31,</b>	
	<b>2007</b>	<b>2008</b>
	<b>RMB</b>	<b>RMB</b>
Amounts due from third parties	21,839	11,289
Amounts due from Sinopec Group Company and its affiliates	2,240	2,673
Amounts due from associates and jointly controlled entities	1,750	1,408
	<u>25,829</u>	<u>15,370</u>
Less: Impairment losses for bad and doubtful debts	(2,882)	(2,381)
	<u>22,947</u>	<u>12,989</u>

Impairment losses for bad and doubtful debts are analyzed as follows:

	<b>2006</b>	<b>2007</b>	<b>2008</b>
	<b>RMB</b>	<b>RMB</b>	<b>RMB</b>
Balance as of January 1	3,151	3,345	2,882
Impairment losses recognized for the year	438	295	143
Reversal of impairment losses	(153)	(204)	(254)
Written off	(91)	(554)	(390)
Balance as of December 31	<u>3,345</u>	<u>2,882</u>	<u>2,381</u>

Sales are generally on a cash term. Credit is generally only available for major customers with well-established trading records. Amounts due from Sinopec Group Company and its affiliates are repayable under the same terms.



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**13. INVENTORIES**

	<b>December 31,</b>	
	<b>2007</b>	<b>2008</b>
	<b>RMB</b>	<b>RMB</b>
Crude oil and other raw materials	70,739	53,258
Work in progress	11,823	10,713
Finished goods	35,040	35,759
Spare parts and consumables	3,002	4,464
	<u>120,604</u>	<u>104,194</u>
Less: Allowance for diminution in value of inventories	(4,572)	(8,939)
	<u>116,032</u>	<u>95,255</u>

Allowance for diminution in value of inventories is analyzed as follows:

	<b>2006</b>	<b>2007</b>	<b>2008</b>
	<b>RMB</b>	<b>RMB</b>	<b>RMB</b>
Balance as of January 1	897	871	4,572
Allowance for the year	419	3,962	8,527
Reversal of allowance on disposal	(317)	(131)	(64)
Written off	(128)	(130)	(4,096)
Balance as of December 31	<u>871</u>	<u>4,572</u>	<u>8,939</u>

During the years ended December 31, 2006, 2007 and 2008, the cost of inventories recognized as an expense in the consolidated statements of income of RMB 887,319, RMB 1,008,384 and RMB 1,327,970, respectively, which includes the write-down of inventories, that primarily related to the refining and chemicals segment, of RMB 419, RMB 3,962 and RMB 8,527, respectively, and the reversal of write-down of inventories made in prior years of RMB 445, RMB 261 and RMB 4,160, respectively, that mainly was due to the sales of inventories. The write-down of inventories and the reversal of write-down of inventories were recorded in purchased crude oil, products and operating supplies and expenses in the consolidated statements of income.

**14. PREPAID EXPENSES AND OTHER CURRENT ASSETS**

	<b>December 31,</b>	
	<b>2007</b>	<b>2008</b>
	<b>RMB</b>	<b>RMB</b>
Advances to third parties	1,418	1,242
Amounts due from Sinopec Group Company and its affiliates	6,719	3,896
Other receivables	1,597	3,566
Purchase deposits and other assets	3,817	4,819
Prepayments in connection with construction work and equipment purchases	4,683	3,176
Prepaid value-added tax and customs duty	6,325	17,457
Amounts due from associates and jointly controlled entities	363	654
Derivative financial instruments – foreign exchange contracts	—	114
	<u>24,922</u>	<u>34,924</u>

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15. PROPERTY, PLANT AND EQUIPMENT

By segment:

	<u>Exploration and production</u>	<u>Refining</u>	<u>Marketing and distribution</u>	<u>Chemicals</u>	<u>Corporate and others</u>	<u>Total</u>
	RMB	RMB	RMB	RMB	RMB	RMB
<b>Cost / valuation:</b>						
Balance as of January 1, 2007	241,364	151,956	86,108	176,717	4,869	661,014
Additions	7,367	506	289	269	247	8,678
Transferred from construction in progress	35,851	10,768	5,726	6,244	1,316	59,905
Acquisitions (ii)	—	—	2,474	—	—	2,474
Reclassification	(7)	(78)	94	(9)	—	—
Contributed to a jointly controlled entity (Note 8 (iii))	—	(4,317)	—	—	—	(4,317)
Reclassification to lease prepayments and other assets	—	(322)	(1,345)	(672)	(27)	(2,366)
Disposals	(392)	(1,027)	(2,191)	(1,425)	(207)	(5,242)
Balance as of December 31, 2007	<u>284,183</u>	<u>157,486</u>	<u>91,155</u>	<u>181,124</u>	<u>6,198</u>	<u>720,146</u>
Balance as of January 1, 2008	284,183	157,486	91,155	181,124	6,198	720,146
Additions	1,598	509	588	688	162	3,545
Transferred from construction in progress	35,701	23,385	9,877	4,683	2,605	76,251
Acquisitions (ii)	17,943	—	—	—	—	17,943
Reclassification	(105)	(3,603)	(250)	3,952	6	—
Reclassification to lease prepayments and other assets	—	(247)	(314)	(41)	(202)	(804)
Disposals	(198)	(486)	(952)	(928)	(28)	(2,592)
Balance as of December 31, 2008	<u>339,122</u>	<u>177,044</u>	<u>100,104</u>	<u>189,478</u>	<u>8,741</u>	<u>814,489</u>
<b>Accumulated depreciation:</b>						
Balance as of January 1, 2007	112,050	69,257	17,154	104,959	1,837	305,257
Depreciation charge for the year	18,161	8,899	5,788	8,734	634	42,216
Acquisitions (ii)	—	—	916	—	—	916
Impairment losses for the year (Note 8 (ii))	481	916	1,194	318	—	2,909
Reclassification	131	(204)	82	(9)	—	—
Contributed to a jointly controlled entity (Note 8 (iii))	—	(3,078)	—	—	—	(3,078)
Reclassification to lease prepayments and other assets	—	—	(190)	(56)	—	(246)
Written back on disposals	(140)	(431)	(1,142)	(1,164)	(93)	(2,970)
Balance as of December 31, 2007	<u>130,683</u>	<u>75,359</u>	<u>23,802</u>	<u>112,782</u>	<u>2,378</u>	<u>345,004</u>
Balance as of January 1, 2008	130,683	75,359	23,802	112,782	2,378	345,004
Depreciation charge for the year	22,040	9,412	4,610	8,234	716	45,012
Acquisitions (ii)	16,401	—	—	—	—	16,401
Impairment losses for the year (Note 8 (ii))	4,600	270	698	1,511	19	7,098
Reclassification	(194)	(499)	13	686	(6)	—
Reclassification to lease prepayments and other assets	—	—	(73)	(1)	(16)	(90)
Written back on disposals	(182)	(421)	(766)	(809)	(23)	(2,201)
Balance as of December 31, 2008	<u>173,348</u>	<u>84,121</u>	<u>28,284</u>	<u>122,403</u>	<u>3,068</u>	<u>411,224</u>
<b>Net book value:</b>						
Balance as of January 1, 2007	<u>129,314</u>	<u>82,699</u>	<u>68,954</u>	<u>71,758</u>	<u>3,032</u>	<u>355,757</u>
Balance as of December 31, 2007	<u>153,500</u>	<u>82,127</u>	<u>67,353</u>	<u>68,342</u>	<u>3,820</u>	<u>375,142</u>
Balance as of December 31, 2008	<u>165,774</u>	<u>92,923</u>	<u>71,820</u>	<u>67,075</u>	<u>5,673</u>	<u>403,265</u>

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By asset class:

	<u>Buildings</u>	<u>Oil and gas properties</u>	<u>Oil depots, storage tanks and service stations</u>	<u>Plant, machinery, equipment and others</u>	<u>Total</u>
	RMB	RMB	RMB	RMB	RMB
<b>Cost / valuation:</b>					
Balance as of January 1, 2007	47,379	218,693	90,249	304,693	661,014
Additions	199	7,264	370	845	8,678
Transferred from construction in progress	684	33,423	7,289	18,509	59,905
Acquisitions (ii)	1,423	—	949	102	2,474
Reclassification	349	(7)	(446)	104	—
Contributed to a jointly controlled entity (Note 8 (iii))	(749)	—	—	(3,568)	(4,317)
Reclassification to lease prepayments and other assets	(1,941)	—	—	(425)	(2,366)
Disposals	(1,044)	—	(1,411)	(2,787)	(5,242)
Balance as of December 31, 2007	<u>46,300</u>	<u>259,373</u>	<u>97,000</u>	<u>317,473</u>	<u>720,146</u>
Balance as of January 1, 2008	46,300	259,373	97,000	317,473	720,146
Additions	195	1,482	319	1,549	3,545
Transferred from construction in progress	5,887	32,218	12,387	25,759	76,251
Acquisitions (ii)	548	—	—	17,395	17,943
Reclassification	49	(176)	363	(236)	—
Reclassification to lease prepayments and other assets	(543)	—	(27)	(234)	(804)
Disposals	(227)	—	(1,118)	(1,247)	(2,592)
Balance as of December 31, 2008	<u>52,209</u>	<u>292,897</u>	<u>108,924</u>	<u>360,459</u>	<u>814,489</u>
<b>Accumulated depreciation:</b>					
Balance as of January 1, 2007	22,728	102,382	17,868	162,279	305,257
Depreciation charge for the year	1,740	16,304	4,409	19,763	42,216
Acquisitions (ii)	472	—	350	94	916
Impairment losses for the year	337	437	961	1,174	2,909
Reclassification	736	(66)	471	(1,141)	—
Contributed to a jointly controlled entity (Note 8 (iii))	(448)	—	—	(2,630)	(3,078)
Reclassification to lease prepayments and other assets	(245)	—	—	(1)	(246)
Written back on disposals	(333)	—	(756)	(1,881)	(2,970)
Balance as of December 31, 2007	<u>24,987</u>	<u>119,057</u>	<u>23,303</u>	<u>177,657</u>	<u>345,004</u>
Balance as of January 1, 2008	24,987	119,057	23,303	177,657	345,004
Depreciation charge for the year	2,025	20,254	5,044	17,689	45,012
Acquisitions (ii)	236	—	—	16,165	16,401
Impairment losses for the year	522	4,530	632	1,414	7,098
Reclassification	(124)	(231)	265	90	—
Reclassification to lease prepayments and other assets	(76)	—	(6)	(8)	(90)
Written back on disposals	(169)	—	(991)	(1,041)	(2,201)
Balance as of December 31, 2008	<u>27,401</u>	<u>143,610</u>	<u>28,247</u>	<u>211,966</u>	<u>411,224</u>
<b>Net book value:</b>					
Balance as of 1 January 1, 2007	<u>24,651</u>	<u>116,311</u>	<u>72,381</u>	<u>142,414</u>	<u>355,757</u>
Balance as of December 31, 2007	<u>21,313</u>	<u>140,316</u>	<u>73,697</u>	<u>139,816</u>	<u>375,142</u>
Balance as of December 31, 2008	<u>24,808</u>	<u>149,287</u>	<u>80,677</u>	<u>148,493</u>	<u>403,265</u>

Notes:

- (i) The additions to the exploration and production segment and oil and gas properties of the Group for the years ended December 31, 2007 and 2008 included RMB 7,211 and RMB 1,482, respectively, of the estimated dismantlement costs for site restoration (Note 26).
- (ii) During the year ended December 31, 2007, the Group acquired the entire equity interests of certain service stations companies incorporated in Hong Kong (“Hong Kong service stations”). During the year ended December 31, 2008, the Group acquired Downhole Assets from Sinopec Group Company (Note 30).

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**16. CONSTRUCTION IN PROGRESS**

	<b>Exploration and production</b>	<b>Refining</b>	<b>Marketing and distribution</b>	<b>Chemicals</b>	<b>Corporate and others</b>	<b>Total</b>
	<b>RMB</b>	<b>RMB</b>	<b>RMB</b>	<b>RMB</b>	<b>RMB</b>	<b>RMB</b>
Balance as of January 1, 2007	16,420	15,439	10,288	7,025	3,699	52,871
Additions	60,135	22,209	10,448	16,025	2,873	111,690
Dry hole costs written off	(6,060)	—	—	—	—	(6,060)
Transferred to property, plant and equipment	(35,851)	(10,768)	(5,726)	(6,244)	(1,316)	(59,905)
Reclassification to lease prepayments and other assets	(203)	(144)	(1,969)	(54)	(20)	(2,390)
Impairment losses for the year (Note 8 (ii))	—	(154)	(43)	—	—	(197)
Contributed to a jointly controlled entity (Note 8 (iii))	—	(601)	—	—	—	(601)
Balance as of December 31, 2007	<u>34,441</u>	<u>25,981</u>	<u>12,998</u>	<u>16,752</u>	<u>5,236</u>	<u>95,408</u>
Balance as of January 1, 2008	34,441	25,981	12,998	16,752	5,236	95,408
Additions	61,750	12,647	12,791	20,536	2,073	109,797
Dry hole costs written off	(4,236)	—	—	—	—	(4,236)
Transferred to property, plant and equipment	(35,701)	(23,385)	(9,877)	(4,683)	(2,605)	(76,251)
Reclassification to lease prepayments and other assets	(154)	(200)	(1,340)	(108)	(1,019)	(2,821)
Reclassification	97	2,846	(292)	(2,732)	81	—
Impairment losses for the year (Note 8 (ii))	—	—	(11)	—	—	(11)
Balance as of December 31, 2008	<u>56,197</u>	<u>17,889</u>	<u>14,269</u>	<u>29,765</u>	<u>3,766</u>	<u>121,886</u>

Net changes in capitalized cost of exploratory wells included in the Group's construction in progress in the E&P segment are analyzed as follows:

	<b>2006</b>	<b>2007</b>	<b>2008</b>
	<b>RMB</b>	<b>RMB</b>	<b>RMB</b>
At beginning of year .	3,573	4,771	6,294
Additions, net of amount that were capitalized and subsequently expensed in the same year, pending the determination of proved reserves .	3,241	4,874	4,613
Transferred to oil and gas properties based on the determination of proved reserves .	(305)	(568)	(1,008)
Dry hole costs written off	<u>(1,738)</u>	<u>(2,783)</u>	<u>(2,066)</u>
At end of year .	<u>4,771</u>	<u>6,294</u>	<u>7,833</u>

Aging of capitalized exploratory well costs based on the date the drilling was completed are analyzed as follows:

	<b>December 31,</b>		
	<b>2006</b>	<b>2007</b>	<b>2008</b>
	<b>RMB</b>	<b>RMB</b>	<b>RMB</b>
One year or less	4,393	5,701	7,113
Over one year	378	593	720
	<u>4,771</u>	<u>6,294</u>	<u>7,833</u>

Capitalized exploratory wells costs aged over one year are related to wells for which the drilling results are being further evaluated or the development plans are being formulated.

The geological and geophysical costs paid during the years ended December 31, 2006, 2007 and 2008 amounted to RMB 3,878, RMB 4,640 and RMB 3,789, respectively.

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17. GOODWILL

	<u>2007</u>	<u>2008</u>
	RMB	RMB
<b>Cost:</b>		
Balance as of January 1	14,325	15,490
Net additions and exchange adjustments	<u>1,165</u>	<u>138</u>
Balance as of December 31	<u><u>15,490</u></u>	<u><u>15,628</u></u>
<b>Accumulated impairment losses:</b>		
Balance as of January 1	—	—
Impairment losses for the year	<u>—</u>	<u>(1,391)</u>
Balance as of December 31	<u><u>—</u></u>	<u><u>(1,391)</u></u>
<b>Net book value</b>		
Balance as of December 31	<u><u>15,490</u></u>	<u><u>14,237</u></u>

**Impairment tests for cash-generating units containing goodwill**

Goodwill is allocated to the following Group's cash-generating units:

	<u>December 31,</u>	
	<u>2007</u>	<u>2008</u>
	RMB	RMB
Sinopec Beijing Yanshan Branch ("Sinopec Yanshan")	1,157	1,157
Sinopec Zhenhai Refining and Chemical Branch ("Sinopec Zhenhai")	3,952	3,952
Sinopec Qilu Branch ("Sinopec Qilu")	2,159	2,159
Sinopec Yangzi Petrochemical Company Limited ("Sinopec Yangzi")	2,737	2,737
Sinopec Zhongyuan Petroleum Company Limited ("Sinopec Zhongyuan")	1,391	—
Sinopec Shengli Oil Field Dynamic Company Limited ("Dynamic")	1,361	1,361
Hong Kong service stations	1,004	924
Multiple units without individually significant goodwill	<u>1,729</u>	<u>1,947</u>
	<u><u>15,490</u></u>	<u><u>14,237</u></u>

Goodwill represents the excess of the cost of purchase over the fair value of the underlying assets and liabilities. The recoverable amounts of Sinopec Yanshan, Sinopec Zhenhai, Sinopec Qilu, Sinopec Yangzi, Sinopec Zhongyuan, Dynamic and Hong Kong service stations are determined based on value in use calculations. These calculations use cash flow projections based on financial budgets approved by management covering a one-year period and pre-tax discount rates primarily ranging from 13.9% to 16.9% and 10.0% to 12.8% for the years ended December 31, 2007 and 2008, respectively. Cash flows beyond the one-year period are maintained constant. Management believes any reasonably possible change in the key assumptions on which these entities' recoverable amounts are based would not cause these entities' carrying amounts to exceed their recoverable amounts.

Key assumptions used for the value in use calculations for these entities are the gross margin and sales volume. Management determined the budgeted gross margin based on the gross margin achieved in the period immediately before the budget period and management's expectation on the future trend of the prices of crude oil and petrochemical products. The sales volume was based on the production capacity and / or the sales volume in the period immediately before the budget period.

During the year ended December 31, 2008, the carrying amount of a cash-generating unit, Sinopec Zhongyuan, was determined to be higher than its recoverable amount. The reduction in recoverable amount was a result of the downward reserves estimation for the oil fields of this cash-generating unit resulting from lower oil and gas pricing. The oil and gas pricing was a factor used in the determination of the present values of the expected future cash flows of this cash-generating unit. The total impairment losses recognized on the goodwill of Sinopec Zhongyuan was RMB 1,391 for the year ended December 31, 2008.

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**18. INTEREST IN ASSOCIATES**

	<b>December 31,</b>	
	<b>2007</b>	<b>2008</b>
	<b>RMB</b>	<b>RMB</b>
Share of net assets	16,865	15,595

The Group's investments in associates are with companies primarily engaged in the oil and gas, petrochemical, and marketing and distribution operations in the PRC. These investments are individually and in aggregate not material to the Group's financial condition or results of operations for all periods presented. The principal investments in associates, all of which are incorporated in the PRC, are as follows:

<b>Name of company</b>	<b>Form of business structure</b>	<b>Particulars of issued and paid up capital</b>	<b>Percentage of equity held by the Company</b>	<b>Percentage of equity held by the Company's subsidiaries</b>	<b>Principal activities</b>
			%	%	
Sinopec Finance Company Limited	Incorporated	Registered capital RMB 6,000,000,000	49.00	—	Provision of non-banking financial services
China Aviation Oil Supply Company Limited	Incorporated	Registered capital RMB 3,800,000,000	—	29.00	Marketing and distribution of refined petroleum products
Shanghai Petroleum National Gas Corporation	Incorporated	Registered capital RMB 900,000,000	30.00	—	Exploration and production of crude oil and natural gas
Shanghai Chemical Industry Park Development Company Limited	Incorporated	Registered capital RMB 2,372,439,000	—	38.26	Planning, development and operation of the Chemical Industry Park in Shanghai, the PRC
China Shipping & Sinopec Suppliers Company Limited	Incorporated	Registered capital RMB 876,660,000	—	50.00	Transportation of petroleum products

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19. INTEREST IN JOINTLY CONTROLLED ENTITIES

	December 31,	
	2007	2008
	RMB	RMB
Share of net assets	12,723	11,781

The Group's principal interests in jointly controlled entities are primarily engaged in the refining and chemical operations in the PRC as follows:

Name of company	Form of business structure	Particulars of issued and paid up capital	Percentage of equity held by the Company	Percentage of equity held by the Company's subsidiaries	Principal activities
			%	%	
Shanghai Secco Petrochemical Company Limited	Incorporated	Registered capital USD 901,440,964	30.00	20.00	Manufacturing and distribution of petrochemical products
BASF-YPC Company Limited	Incorporated	Registered capital RMB 8,793,000,000	30.00	10.00	Manufacturing and distribution of petrochemical products
Fujian Refining and Petrochemical Company Limited	Incorporated	Registered capital USD 1,654,351,000	—	50.00	Manufacturing and distribution of petrochemical products

The Group's effective interest share of the jointly controlled entities' results of operation, financial condition and cash flows are as follows:

	Years ended December 31,		
	2006	2007	2008
	RMB	RMB	RMB
Results of operation:			
Operating revenue	17,323	23,085	27,417
Expenses	(14,927)	(20,378)	(28,371)
Net income / (loss)	2,396	2,707	(954)

	December 31,	
	2007	2008
	RMB	RMB
Financial condition:		
Current assets	6,736	6,691
Non-current assets	22,229	28,430
Current liabilities	(5,313)	(6,413)
Non-current liabilities	(10,929)	(16,927)
Net assets	12,723	11,781

	Years ended December 31,		
	2006	2007	2008
	RMB	RMB	RMB
Cash flows:			
Net cash generated from / (used in) operating activities	2,452	5,079	(2,046)
Net cash used in investing activities	(382)	(13,238)	(5,872)
Net cash (used in) / generated from financing activities	(939)	7,143	7,999
Net increase / (decrease) in cash and cash equivalents	1,131	(1,016)	81



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**20. INVESTMENTS**

	<b>December 31,</b>	
	<b>2007</b>	<b>2008</b>
	<b>RMB</b>	<b>RMB</b>
Available-for-sale equity securities, listed and at quoted market price	653	154
Other investments in equity securities, unlisted and at cost	2,846	1,562
	<u>3,499</u>	<u>1,716</u>
Less: Impairment losses for investments	(305)	(233)
	<u>3,194</u>	<u>1,483</u>

Unlisted investments represent the Group's interests in PRC privately owned enterprises which are mainly engaged in non-oil and gas activities and operations.

The impairment losses relating to investments for the year ended December 31, 2007 and 2008 amounted to RMB 55 and 9, respectively.

**21. LONG-TERM PREPAYMENTS AND OTHER ASSETS**

Long-term prepayments and other assets primarily represent prepaid rental expenses over one year, computer software, catalysts and operating rights of service stations.

**22. DEFERRED TAX ASSETS AND LIABILITIES**

Deferred tax assets and deferred tax liabilities are attributable to the items detailed in the table below:

	<b>Assets</b>		<b>Liabilities</b>		<b>Net balance</b>	
	<b>December 31,</b>		<b>December 31,</b>		<b>December 31,</b>	
	<b>2007</b>	<b>2008</b>	<b>2007</b>	<b>2008</b>	<b>2007</b>	<b>2008</b>
	<b>RMB</b>	<b>RMB</b>	<b>RMB</b>	<b>RMB</b>	<b>RMB</b>	<b>RMB</b>
<i>Current</i>						
Receivables and inventories	3,841	4,357	—	—	3,841	4,357
Accruals	2,613	261	—	—	2,613	261
<i>Non-current</i>						
Property, plant and equipment	2,641	3,891	(1,376)	(1,286)	1,265	2,605
Accelerated depreciation	—	—	(4,144)	(3,716)	(4,144)	(3,716)
Tax value of losses carried forward	176	3,915	—	—	176	3,915
Lease prepayments	306	300	—	—	306	300
Available-for-sale financial assets	—	—	(116)	(52)	(116)	(52)
Embedded derivative component of the						
Convertible Bonds	803	—	—	(151)	803	(151)
Others	59	86	—	(30)	59	56
Deferred tax assets / (liabilities)	<u>10,439</u>	<u>12,810</u>	<u>(5,636)</u>	<u>(5,235)</u>	<u>4,803</u>	<u>7,575</u>

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As of December 31, 2007 and 2008, certain subsidiaries of the Company did not recognize the tax value of losses carried forward of RMB 3,813 and RMB 7,975, respectively, because it was not probable that the related tax benefit will be realized. The tax value of these losses carried forward of RMB 765, RMB 1,443, RMB 1,366, RMB 639 and RMB 3,762 expire in 2009, 2010, 2011, 2012 and 2013, respectively.

Based on management's assessment of the probability that taxable profit will be available over the period which the deferred tax assets can be realized or utilized, deferred tax asset of RMB 103 and 948 were not recognized for the years ended December 31, 2007 and 2008, respectively. In assessing the probability, both positive and negative evidence was considered, including whether it is probable that the operations will have future taxable profits over the periods which the deferred tax assets are deductible or utilized and whether the tax losses result from identifiable causes which are unlikely to recur.

Movements in deferred tax assets and liabilities are as follows:

	Balance as of January 1, 2006 RMB	Recognized in consolidated statements of income RMB	Recognized in equity RMB	Balance as of December 31, 2006 RMB	
<i>Current</i>					
Receivables and inventories	3,448	84	—	3,532	
Accruals	457	408	—	865	
<i>Non-current</i>					
Property, plant and equipment	18	583	—	601	
Accelerated depreciation	(4,290)	(367)	—	(4,657)	
Tax value of losses carried forward	130	(25)	—	105	
Lease prepayments	375	(24)	—	351	
Available-for-sale financial assets (i)	—	—	(4)	(4)	
Others	(27)	77	—	50	
Net deferred tax assets	<u>111</u>	<u>736</u>	<u>(4)</u>	<u>843</u>	
	Balance as of January 1, 2007 RMB	Recognized in consolidated statements of income RMB	Acquisitions of subsidiaries RMB	Recognized in equity RMB	Balance as of December 31, 2007 RMB
<i>Current</i>					
Receivables and inventories	3,532	309	—	—	3,841
Accruals	865	1,748	—	—	2,613
<i>Non-current</i>					
Property, plant and equipment	601	711	(47)	—	1,265
Accelerated depreciation	(4,657)	513	—	—	(4,144)
Tax value of losses carried forward	105	71	—	—	176
Lease prepayments (ii)	351	(8)	—	(37)	306
Available-for-sale financial assets (i)	(4)	—	—	(112)	(116)
Embedded derivative component of the Convertible Bonds	—	803	—	—	803
Others	50	9	—	—	59
Net deferred tax assets	<u>843</u>	<u>4,156</u>	<u>(47)</u>	<u>(149)</u>	<u>4,803</u>

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	Balance as of January 1, 2008 <u>RMB</u>	Recognized in consolidated statements of income <u>RMB</u>	Recognized in equity <u>RMB</u>	Balance as of December 31, 2008 <u>RMB</u>
<i>Current</i>				
Receivables and inventories	3,841	516	—	4,357
Accruals	2,613	(2,352)	—	261
<i>Non-current</i>				
Property, plant and equipment	1,265	1,340	—	2,605
Accelerated depreciation	(4,144)	428	—	(3,716)
Tax value of losses carried forward	176	3,739	—	3,915
Lease prepayments	306	(6)	—	300
Available-for-sale financial assets (i)	(116)	—	64	(52)
Embedded derivative component of the Convertible Bonds	803	(954)	—	(151)
Others	59	(3)	—	56
Net deferred tax assets	<u>4,803</u>	<u>2,708</u>	<u>64</u>	<u>7,575</u>

Notes:

- (i) The amount recognized in equity represents the deferred tax effect of change in fair value of available-for-sale financial assets which was recognized directly in equity.
- (ii) The amount recognized in equity represents the effect of change in tax rate on deferred tax assets previously recognized directly in equity as a result of the new tax law.

**23. SHORT-TERM AND LONG-TERM DEBTS AND LOANS FROM SINOPEC GROUP COMPANY AND ITS AFFILIATES**

Short-term debts represent:

	<u>December 31,</u>	
	<u>2007</u>	<u>2008</u>
	<u>RMB</u>	<u>RMB</u>
<b>Third parties' debts</b>		
Short-term bank loans	21,294	40,735
Current portion of long-term bank loans	12,259	17,109
Current portion of long-term other loans	1,027	2,052
	<u>13,286</u>	<u>19,161</u>
Corporate bonds (a)	10,074	15,000
	<u>44,654</u>	<u>74,896</u>
<b>Loans from Sinopec Group Company and its affiliates</b>		
Short-term loans	15,660	23,237
Current portion of long-term loans	180	350
	<u>15,840</u>	<u>23,587</u>
	<u>60,494</u>	<u>98,483</u>

The Group's weighted average interest rates on short-term loans were 5.4% and 4.7% as of December 31, 2007 and 2008, respectively.

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Long-term debts comprise:

	Interest rate and final maturity	December 31,	
		2007 RMB	2008 RMB
<b>Third parties' debts</b>			
<b>Long-term bank loans</b>			
Renminbi denominated	Interest rates ranging from interest free to 7.6% per annum as of December 31, 2008 with maturities through 2018	46,912	42,036
Japanese Yen denominated	Interest rates ranging from 2.6% to 3.0% per annum as of December 31, 2008 with maturities through 2024	2,147	2,121
US Dollar denominated	Interest rates ranging from interest free to 7.4% per annum as of December 31, 2008 with maturities through 2031	1,189	746
Euro denominated	Interest rate ranging from 6.6% to 6.7% per annum as of December 31, 2008 with maturities through 2011	78	197
Hong Kong Dollar denominated	Floating rate as of Hong Kong Interbank Offer Rate plus 0.5% per annum as of December 31, 2007, paid off as of December 31, 2008	375	—
		<u>50,701</u>	<u>45,100</u>
<b>Long-term other loans</b>			
Renminbi denominated	Interest rates ranging from interest free to 5.2% per annum as of December 31, 2008 with maturities through 2011	3,075	2,075
US Dollar denominated	Interest rates ranging from interest free to 2.0% per annum as of December 31, 2008 with maturities through 2015	38	33
		<u>3,113</u>	<u>2,108</u>

CHINA PETROLEUM & CHEMICAL CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)  
(Amounts in millions, except per share data and except otherwise stated)

		<u>Interest rate and final maturity</u>	
		<u>December 31,</u>	
		<u>2007</u>	<u>2008</u>
		<u>RMB</u>	<u>RMB</u>
<b>Corporate bonds</b>			
Renminbi denominated	Fixed interest rate at 4.61% per annum as of December 31, 2008 with maturity in February 2014 (b)	3,500	3,500
	Fixed interest rate at 4.20% per annum as of December 31, 2008 with maturity in May 2017 (c)	5,000	5,000
	Fixed interest rate at 5.40% per annum as of December 31, 2008 with maturity in November 2012 (d)	8,500	8,500
	Fixed interest rate at 5.68% per annum as of December 31, 2008 with maturity in November 2017 (e)	11,500	11,500
		<u>28,500</u>	<u>28,500</u>
<b>Convertible bonds</b>			
Hong Kong Dollar denominated	Zero coupon convertible bonds with maturity in April 2014 (f)	14,106	9,870
Renminbi denominated	Bonds with Warrants with fixed interest rate at 0.8% per annum and maturity in February 2014 (g)	—	23,837
		<u>14,106</u>	<u>33,707</u>
Total third parties' long-term debts		96,420	109,415
Less: Current portion		<u>(13,286)</u>	<u>(19,161)</u>
		<u>83,134</u>	<u>90,254</u>
<b>Long-term loans from Sinopec Group Company and its affiliates</b>			
Renminbi denominated	Interest rates ranging from interest free to 7.3% per annum as of December 31, 2008 with maturities through 2020	37,360	37,240
Less: Current portion		<u>(180)</u>	<u>(350)</u>
		<u>37,180</u>	<u>36,890</u>
		<u>120,314</u>	<u>127,144</u>

Notes:

- (a) The Company issued 182-day corporate bonds of face value at RMB 10,000 to corporate investors in the PRC debenture market on October 22, 2007 at par value of RMB 100. The effective yield of the 182-day corporate bonds is 4.12% per annum. The Company redeemed the corporate bonds in April 2008.

The Company issued six-month corporate bonds of face value at RMB 15,000 to corporate investors in the PRC debenture market on December 22, 2008 at par value of RMB 100. The effective yield of the six-month corporate bonds is 2.3% per annum. The corporate bonds mature in June 2009.

- (b) The Company issued ten-year corporate bonds of RMB 3,500 to PRC citizens as well as PRC legal and non-legal persons on February 24, 2004. The ten-year corporate bond bears a fixed interest rate of 4.61% per annum and interest is paid annually. These corporate bonds are guaranteed by Sinopec Group Company.
- (c) The Company issued ten-year corporate bonds of RMB 5,000 to corporate investors in the PRC debenture market on May 10, 2007. The ten-year corporate bond bears a fixed interest rate of 4.20% per annum and interest is paid annually. These corporate bonds are guaranteed by Sinopec Group Company.

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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)**  
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- (d) The Company issued five-year corporate bonds of RMB 8,500 to corporate investors in the PRC debenture market on November 13, 2007. The five-year corporate bond bears a fixed interest rate of 5.40% per annum and interest is paid annually. These corporate bonds are guaranteed by Sinopec Group Company.
- (e) The Company issued ten-year corporate bonds of RMB 11,500 to corporate investors in the PRC debenture market on November 13, 2007. The ten-year corporate bond bears a fixed interest rate of 5.68% per annum and interest is paid annually. These corporate bonds are guaranteed by Sinopec Group Company.
- (f) On April 24, 2007, the Company issued zero coupon convertible bonds due 2014 with an aggregate principal amount of HK\$11,700 (the "Convertible Bonds"). The holders can convert the Convertible Bonds into shares of the Company from June 4, 2007 onwards at a price of HK\$10.76 per share, subject to adjustment for, amongst other things, subdivision or consolidation of shares, bonus issues, rights issues, capital distribution, change of control and other events, which have a dilutive effect on the issued share capital of the Company (the "Conversion component"). Unless previously redeemed, converted or purchased and cancelled, the Convertible Bonds will be redeemed on the maturity date at 121.069% of the principal amount. The Company has an early redemption option at any time after April 24, 2011 (subject to certain criteria) (the "Early Redemption Option") and a cash settlement option when the holders exercise their conversion right (the "Cash Settlement Option"). The holders also have an early redemption option to require the Company to redeem all or some of the Convertible Bonds as of April 24, 2011 at an early redemption amount of 111.544% of the principal amount.

As of December 31, 2007, the carrying amounts of the liability component and the derivative component, representing the Conversion component, the Early Redemption Option and the Cash Settlement Option, of the Convertible Bonds, were RMB 10,159 and RMB 3,947, respectively. No conversion of the Convertible Bonds has occurred up to December 31, 2007.

As of December 31, 2008, the carrying amounts of the liability and the derivative component of the Convertible Bonds were RMB 9,870 and RMB nil, respectively. No conversion of the Convertible Bonds has occurred up to December 31, 2008.

As of December 31, 2007 and 2008, the fair value of the derivative components of the Convertible Bonds was calculated using the Black-Scholes Model. The following are the major inputs used in the Black-Scholes Model:

	<b>2007</b>	<b>2008</b>
Stock price of underlying shares	HKD 11.78	HKD 4.69
Conversion price	HKD 10.76	HKD 10.76
	50 basis	450 basis
Option adjusted spread	points	points
Average risk free rate	3.60%	1.64%
Average expected life	4.8 years	3.8 years

Any change in the major inputs into the Model will result in changes in the fair values of the derivative components. The change in the fair value of the conversion option from April 24, 2007 to December 31, 2007 and from December 31, 2007 to December 31, 2008 resulted in an unrealized loss of RMB 3,211 and an unrealized gain of RMB 3,947, respectively, which have been recorded in the "finance costs" section of the consolidated statements of income.

The initial carrying amount of the liability component is the residual amount, which is after deducting the allocated issuance cost of the Convertible Bonds relating to the liability component and the fair value of the derivative component as of April 24, 2007. Interest expense is calculated using the effective interest method by applying the effective interest rate of 4.19% to the adjusted liability component. Should the aforesaid derivative components not been separated out and the entire Convertible Bonds been considered as the liability component, the effective interest rate would have been 3.03%.

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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)**  
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- (g) On February 26, 2008, the Company issued bonds with stock warrants due 2014 with an aggregate principal amount of RMB 30,000 in the PRC (the “Bonds with Warrants”). The Bonds with Warrants, which bear a fixed interest rate of 0.80% per annum payable annually, were issued at par value of RMB 100. The Bonds with Warrants are guaranteed by Sinopec Group Company. Every ten Bonds with Warrants are entitled to warrants to subscribe 50.5 A shares of the Company during the 5 trading days prior to March 3, 2010 at an initial exercise price of RMB 19.68 per share (the “Warrants”), subject to adjustment for, amongst other things, cash dividends, subdivision or consolidation of shares, bonus issues, rights issues, capital distribution, change of control and other events which have a dilutive effect on the issued share capital of the Company.

On December 31, 2008, the exercise price of the Warrants was adjusted to RMB 19.43 per share as a result of the final dividend in respect of the year ended December 31, 2007 and the interim dividend in respect of the year ended December 31, 2008 declared and paid during the year ended December 31, 2008.

The initial recognition of the liability component of the Bond with Warrants is measured as the present value of the future interest and principal payments, discounted at the market rate of interest applicable at the time of initial recognition to similar liabilities that do not have a conversion option (“market interest rate”). Interest expense is calculated using the effective interest method by applying the market interest rate of 5.40% to the liability component. The excess of proceeds from the issuance of the Bonds with Warrants, net of issuance costs, over the amount initially recognized as the liability component is recognized as the equity component in capital reserve until either the Warrants is exercised or expired. Should the equity component not been separated out and the entire Bonds with Warrants been considered as the liability component, the effective interest rate would have been 0.80%. The initial carrying amounts of liability and equity components of the Bonds with Warrants were RMB 22,971 and RMB 6,879 upon issuance, respectively.

Third parties’ loans of RMB 87 and RMB 52 as of December 31, 2007 and 2008, respectively, are secured by certain of the Group’s property, plant and equipment. The net book value of property, plant and equipment of the Group pledged as security amounted to RMB 141 and RMB 259 as of December 31, 2007 and 2008, respectively.

**CHINA PETROLEUM & CHEMICAL CORPORATION AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)**  
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**24. TRADE ACCOUNTS AND BILLS PAYABLES**

	<b>December 31,</b>	
	<b>2007</b>	<b>2008</b>
	<b>RMB</b>	<b>RMB</b>
Amounts due to third parties	87,577	52,997
Amounts due to Sinopec Group Company and its affiliates	3,522	1,840
Amounts due to associates and jointly controlled entities	1,950	1,830
	<u>93,049</u>	<u>56,667</u>
Bills payable	12,162	17,493
	<u>105,211</u>	<u>74,160</u>

**25. ACCRUED EXPENSES AND OTHER PAYABLES**

	<b>December 31,</b>	
	<b>2007</b>	<b>2008</b>
	<b>RMB</b>	<b>RMB</b>
Amounts due to Sinopec Group Company and its affiliates	12,907	12,624
Accrued expenditures	29,260	31,211
Provision for onerous contracts for purchases of crude oil (i)	6,700	—
Taxes other than income tax	8,836	21,518
Receipts in advance	23,551	27,796
Advances from third parties	1,103	1,822
Others	6,814	6,907
	<u>89,171</u>	<u>101,878</u>

Note:

- (i) As of December 31, 2007, the Group entered into certain non-cancellable purchase commitment contracts of crude oil for delivery in 2008. Due to the distortion of the correlation of domestic refined petroleum product prices and the crude oil prices, the Group determined that the economic benefits to be derived from processing the crude oil under these purchase contracts would be lower than the unavoidable cost of meeting the Group's obligations under these purchase contracts. Consequently, a provision for onerous contracts of RMB 6,700 was recognized in accordance with the policy set out in Note 2(p) as of December 31, 2007. The provision for onerous contracts for purchases of crude oil as of December 31, 2007 approximated the actual losses incurred from these non-cancellable purchase commitment contracts during the year ended December 31, 2008. As of December 31, 2008, the Group did not recognize such a provision, as management expected the economic benefits to be derived from non-cancellable purchase commitment contracts entered into by the Group as of December 31, 2008 would be higher than the unavoidable costs of meeting the obligation under these contracts.

**26. OTHER LIABILITIES**

Other liabilities primarily represent provision for future dismantlement costs of oil and gas properties. As of and before December 31, 2006, the Group did not have legal obligation nor constructive obligation to take any dismantlement measures for its retired oil and gas properties. During the year ended December 31, 2007, due to the rising environmental concern in the PRC, the Group has committed to the PRC government to establish certain standardized measures for the dismantlement of its retired oil and gas properties by making reference to the industry practices and is thereafter constructively obligated to take dismantlement measures of its retired oil and gas properties. During the years ended December 31, 2007 and 2008, the Group recognized provisions of RMB 7,211 and RMB 1,482, respectively, utilized RMB 20 and 222, respectively, and recognized accretion expenses of RMB 353 and RMB 430, respectively, in respect of its obligations for the dismantlement of its retired oil and gas properties. As of December 31, 2007 and 2008, the amount of provision in respect of the obligations for the dismantlement of the Group's retired oil and gas properties was RMB 7,544 and RMB 9,234, respectively.



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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)**  
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**27. SHARE CAPITAL**

	<b>December 31,</b>	
	<b>2007</b>	<b>2008</b>
	<b>RMB</b>	<b>RMB</b>
<b>Registered, issued and fully paid</b>		
69,921,951,000 domestic listed A shares of RMB 1.00 each	69,922	69,922
16,780,488,000 overseas listed H shares of RMB 1.00 each	16,780	16,780
	<u>86,702</u>	<u>86,702</u>

The Company was established on February 25, 2000 with a registered capital of 68.8 billion domestic state-owned shares with a par value of RMB 1.00 each. Such shares were issued to Sinopec Group Company in consideration for the assets and liabilities of the Predecessor Operations transferred to the Company (Note 1).

Pursuant to the resolutions passed at an Extraordinary General Meeting held on July 25, 2000 and approvals from relevant government authorities, the Company is authorized to increase its share capital to a maximum of 88.3 billion shares with a par value of RMB 1.00 each and offer not more than 19.5 billion shares with a par value of RMB 1.00 each to investors outside the PRC. Sinopec Group Company is authorized to offer not more than 3.5 billion shares of its shareholdings in the Company to investors outside the PRC. The shares sold by Sinopec Group Company to investors outside the PRC would be converted into H shares.

In October 2000, the Company issued 15,102,439,000 H shares with a par value of RMB 1.00 each, representing 12,521,864,000 H shares and 25,805,750 American Depositary Shares (“ADSs”, each representing 100 H shares), at prices of HK\$ 1.59 per H share and US\$ 20.645 per ADS, respectively, by way of a global initial public offering to Hong Kong and overseas investors. As part of the global initial public offering, 1,678,049,000 domestic state-owned ordinary shares of RMB 1.00 each owned by Sinopec Group Company were converted into H shares and sold to Hong Kong and overseas investors.

In July 2001, the Company issued 2.8 billion domestic listed A shares with a par value of RMB 1.00 each at RMB 4.22 by way of a public offering to natural persons and institutional investors in the PRC.

On September 25, 2006, the shareholders of listed A shares accepted the proposal offered by the shareholders of state-owned A shares whereby the shareholders of state-owned A shares agreed to transfer 2.8 state-owned A shares to shareholders of listed A shares for every 10 listed A shares they held, in exchange for the approval for the listing of all state-owned A shares. In October 2006, the 67,121,951,000 domestic state-owned A shares became listed A shares.

All A shares and H shares rank pari passu in all material aspects.

**Capital management**

Management optimizes the structure of the Group’s capital, comprising equity and loans. In order to maintain or adjust the capital structure of the Group, management may cause the Group to issue new shares, adjust the capital expenditure plan, sell assets to reduce debt, or adjust the proportion of short-term and long-term loans. Management monitors capital on the basis of debt-to-equity ratio, which is calculated by dividing long-term loans (excluding current portion), including long-term debts and loans from Sinopec Group Company and its affiliates, by the total of equity attributable to equity shareholders of the Company and long-term loans (excluding current portion), and liability-to-asset ratio, which is calculated by dividing total liabilities by total assets. Management’s strategy is to make appropriate adjustments according to the Group’s operating and investment needs and the changes of market conditions, and to maintain the debt-to-equity ratio and the liability-to-asset ratio of the Group at a range considered reasonable. The debt-to-equity ratio of the Group was 28.1% and 27.9% as of December 31, 2007 and 2008, respectively. The liability-to-asset ratio of the Group was 54.6% and 54.5% as of December 31, 2007 and 2008, respectively.

The schedule of the contractual maturities of loans and commitments are disclosed in Notes 23 and 29, respectively.

There were no changes in the management’s approach to capital management of the Group during the year. Neither the Company nor any of its subsidiaries are subject to externally imposed capital requirements.

CHINA PETROLEUM & CHEMICAL CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)  
(Amounts in millions, except per share data and except otherwise stated)

28. RESERVES

	<u>2007</u>	<u>2008</u>
	RMB	RMB
<b>Capital reserve (Note (a))</b>		
Balance as of January 1	(21,590)	(22,652)
Transfer from other reserves to capital reserve	(1,062)	—
Issuance of the Bonds with Warrants (Note 23 (g))	—	6,879
Acquisition of non-controlling interests of subsidiaries	—	(318)
Distribution to Sinopec Group Company (Note (b))	—	(202)
Balance as of December 31	<u>(22,652)</u>	<u>(16,293)</u>
<b>Share premium (Note (c))</b>		
Balance as of January 1 / December 31	<u>18,072</u>	<u>18,072</u>
<b>Revaluation reserve</b>		
Balance as of January 1	24,752	24,114
Revaluation surplus realized	(638)	(347)
Balance as of December 31	<u>24,114</u>	<u>23,767</u>
<b>Statutory surplus reserve (Note (d))</b>		
Balance as of January 1	32,094	37,797
Adjustment of statutory surplus reserve	235	1,189
Appropriation	5,468	4,092
Balance as of December 31	<u>37,797</u>	<u>43,078</u>
<b>Discretionary surplus reserve (Note (f))</b>		
Balance as of January 1	27,000	27,000
Appropriation	—	20,000
Balance as of December 31	<u>27,000</u>	<u>47,000</u>
<b>Other reserves</b>		
Balance as of January 1	1,758	3,100
Unrealized gain / (loss) for the change in fair value of available-for-sale financial assets, net of deferred tax (Note (k))	2,892	(2,320)
Effect of change in tax rate	(54)	—
Realization of deferred tax on lease prepayments	(7)	(6)
Transfer from retained earnings to other reserves	(151)	—
Transfer from other reserves to capital reserve	1,062	—
Contribution from Sinopec Group Company (Note (g))	68	—
Consideration for Acquisition of Refinery Plants (Note 1)	(2,468)	—
Balance as of December 31	<u>3,100</u>	<u>774</u>
<b>Retained earnings (Note (h))</b>		
Balance as of January 1	95,546	133,300
Net income attributable to equity shareholders of the Company	56,533	29,769
Final dividend inspect of the previous year, approved and paid during the year (Note (i))	(9,537)	(9,971)
Interim dividend (Note (j))	(4,335)	(2,601)
Adjustment to the statutory surplus reserve	(235)	(1,189)
Appropriation	(5,468)	(24,092)
Revaluation surplus realized	638	347
Realization of deferred tax on lease prepayments	7	6
Transfer from retained earnings to other reserves	151	—
Balance as of December 31	<u>133,300</u>	<u>125,569</u>
	<u>220,731</u>	<u>241,967</u>

## CHINA PETROLEUM & CHEMICAL CORPORATION AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued) (Amounts in millions, except per share data and except otherwise stated)

#### Notes:

- (a) The capital reserve represents (i) the difference between the total amount of the par value of shares issued and the amount of the net assets transferred from Sinopec Group Company in connection with the Reorganization and (ii) the difference between the considerations paid over the amount of the net assets of certain entities and related operations acquired from Sinopec Group Company and (iii) the equity component of the Bonds with Warrants.
- (b) During the year ended December 31, 2008, the Group paid additional cash consideration of RMB 96 for the Acquisition of Refinery Plants (Note 1) to Sinopec Group Company, which was accounted for as an equity transaction. In addition, the Group acquired certain assets and liabilities, including the oilfield downhole operation (the "Downhole Assets"), from Sinopec Group Company. The difference between the consideration paid over the carrying value of these net assets acquired was RMB 106, which was accounted for as an equity transaction.
- (c) The application of the share premium account is governed by Sections 168 and 169 of the PRC Company Law.
- (d) According to the Company's Articles of Association, the Company is required to transfer 10% of its net income in accordance with the PRC accounting policies adopted by the Group to statutory surplus reserve until the reserve balance reaches 50% of the registered capital. The transfer to this reserve must be made before distribution of a dividend to shareholders. Statutory surplus reserve can be used to make good previous years' losses, if any, and may be converted into share capital by the issue of new shares to shareholders in proportion to their existing shareholdings or by increasing the par value of the shares currently held by them, provided that the balance after such issue is not less than 25% of the registered capital.

Before January 1, 2007, the net income for this purpose was determined in accordance with the PRC accounting policies complying with Accounting Standards for Business Enterprises and the Accounting Regulations for Business Enterprises issued by the Ministry of Finance of the PRC ("MOF") before 2006, and RMB 5,066 was transferred to this reserve for the year ended December 31, 2006. On January 1, 2007, the Group adopted the accounting policies complying with the new Accounting Standards for Business Enterprises ("ASBE") issued by the MOF on February 15, 2006, which resulted in certain PRC accounting policies being changed and applied retrospectively. The statutory surplus reserve, amounting to RMB 235, has been adjusted accordingly. The adjustment to the statutory surplus reserve was reflected as a movement for the year ended December 31, 2007. During the year ended December 31, 2007, the Company transferred RMB 5,468, being 10% of the net income determined in accordance with the PRC accounting policies complying with ASBE, to this reserve.

Pursuant to the requirement in Cai Kuai [2008] No. 11 "Interpretation of ASBE No. 2" issued by the MOF on August 7, 2008, the Group changed certain PRC accounting policies that were applied retrospectively. The statutory surplus reserve, amounting to RMB 1,189, has been adjusted accordingly. The adjustment to statutory surplus reserve was reflected as a movement for the year ended December 31, 2008. During the year ended December 31, 2008, the Company transferred RMB 4,092, being 10% of the current year's net income determined in accordance with the PRC accounting policies complying with ASBE, to this reserve.

- (e) Before January 1, 2006, according to the Company's Articles of Association, the Company was required to transfer 5% to 10% of its net income, as determined in accordance with the PRC accounting policies, to the statutory public welfare fund. This fund could only be utilized on capital items for the collective benefits of the Company's employees such as the construction of dormitories, canteen and other staff welfare facilities. The transfer to this fund must be made before distribution of a dividend to shareholders.

According to the Company Law of the PRC which was revised on October 27, 2005, the Company is no longer required to make appropriation to the statutory public welfare fund commencing from January 1, 2006. Pursuant to the notice "Cai Qi [2006] No. 67" issued by the MOF on March 15, 2006, the balance of this fund as of December 31, 2005 was transferred to the statutory surplus reserve.

- (f) The directors authorized the transfer of RMB 20,000, which was approved by the shareholders at Annual General Meeting on May 29, 2007, to discretionary surplus reserve for the year ended December 31, 2006. The directors authorized the transfer of RMB 20,000, subject to the shareholders' approval at the Annual

## CHINA PETROLEUM & CHEMICAL CORPORATION AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued) (Amounts in millions, except per share data and except otherwise stated)

General Meeting, to discretionary surplus reserve for the year ended December 31, 2008. The usage of the discretionary surplus reserve is similar to that of statutory surplus reserve.

- (g) These represent net assets distributed to / contributed from Sinopec Group Company for no monetary consideration.
- (h) According to the Company's Articles of Association, the amount of retained earnings available for distribution to equity shareholders of the Company is the lower of the amount determined in accordance with the accounting policies complying with ASBE and the amount determined in accordance with the accounting policies complying with IFRS. As of December 31, 2007 and 2008, the amount of retained earnings available for distribution was RMB 77,805 and RMB 82,147, respectively, being the amount determined in accordance with the accounting policies complying with IFRS. Final dividend for the year ended December 31, 2008 of RMB 7,803 proposed after the balance sheet date has not been recognized as a liability at the balance sheet date.
- (i) Pursuant to the shareholders' approval at the Annual General Meeting on May 29, 2007, a final dividend of RMB 0.11 per share totaling RMB 9,537 in respect of the year ended December 31, 2006 was declared and paid on June 29, 2007.

Pursuant to the shareholders' approval at the Annual General Meeting on May 26, 2008, a final dividend of RMB 0.115 per share totaling RMB 9,971 in respect of the year ended December 31, 2007 was declared and paid on June 30, 2008.

- (j) Pursuant to the Company's Articles of Association and a resolution passed at the Director's meeting on August 24, 2007, the directors authorized to declare an interim dividend for the year ended December 31, 2007 of RMB 0.05 per share totaling RMB 4,335, which was paid on September 28, 2007.

Pursuant to the Company's Articles of Association and a resolution passed at the Directors' meeting on August 22, 2008, the directors authorized to declare an interim dividend for the year ended December 31, 2008 of RMB 0.03 per share totaling RMB 2,601, which was paid on September 19, 2008.

- (k) During the years ended December 31, 2007 and 2008, the unrealized gain / loss for the change in fair value of available-for-sale financial assets, net of deferred tax, included the share of the unrealized gain / loss for the change in fair value of available-for-sale financial assets in an associate based on the Group's proportionate interest in this associate, which amounted to an unrealized gain of RMB 2,711 and an unrealized loss of RMB 2,206, respectively.

## 29. COMMITMENTS AND CONTINGENT LIABILITIES

### *Operating lease commitments*

The Group leases land and buildings, service stations and other equipment through non-cancellable operating leases. These operating leases do not contain provisions for contingent lease rentals. None of the rental agreements contain escalation provisions that may require higher future rental payments.

As of December 31, 2007 and 2008, the future minimum lease payments under operating leases are as follows:

	December 31,	
	2007	2008
	RMB	RMB
Within one year	4,620	6,066
Between one and two years	4,497	5,750
Between two and three years	4,477	5,655
Between three and four years	4,407	5,595
Between four and five years	4,465	5,519
Thereafter	119,726	149,893
	<u>142,192</u>	<u>178,478</u>

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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)**  
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**Capital commitments**

As of December 31, 2007 and 2008, capital commitments are as follows:

	<b>December 31,</b>	
	<b>2007</b>	<b>2008</b>
	<b>RMB</b>	<b>RMB</b>
Authorized and contracted for	130,816	120,773
Authorized but not contracted for	114,854	48,100
	<u>245,670</u>	<u>168,873</u>

These capital commitments relate to oil and gas exploration and development, refining and petrochemical production capacity expansion projects and the construction of service stations and oil depots.

**Exploration and production licenses**

Exploration licenses for exploration activities are registered with the Ministry of Land and Resources. The maximum term of the Group's exploration licenses is 7 years, and may be renewed twice within 30 days prior to expiration of the original term with each renewal being for a two-year term. The Group is obligated to make progressive annual minimum exploration investment relating to the exploration blocks in respect of which the license is issued. The Ministry of Land and Resources also issues production licenses to the Group on the basis of the reserve reports approved by relevant authorities. The maximum term of a full production license is 30 years unless a special dispensation was given by the State Council. The maximum term of production licenses issued to the Group is 80 years as a special dispensation was given to the Group by the State Council. The Group's production license is renewable upon application by the Group 30 days prior to expiration.

The Group is required to make payments of exploration license fees and production right usage fees to the Ministry of Land and Resources annually which are expensed as incurred. Payments incurred were approximately RMB 236, RMB 303 and RMB 437 for the years ended December 31, 2006, 2007 and 2008, respectively.

Estimated future annual payments are as follows:

	<b>December 31,</b>	
	<b>2007</b>	<b>2008</b>
	<b>RMB</b>	<b>RMB</b>
Within one year	218	123
Between one and two years	150	118
Between two and three years	66	20
Between three and four years	20	20
Between four and five years	19	19
Thereafter	656	651
	<u>1,129</u>	<u>951</u>

CHINA PETROLEUM & CHEMICAL CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)  
(Amounts in millions, except per share data and except otherwise stated)

*Contingent liabilities*

As of December 31, 2007 and 2008, guarantees given to banks in respect of banking facilities granted to the parties below were as follows:

	December 31,	
	2007	2008
	RMB	RMB
Associates and jointly controlled entities	9,812	11,404

Management monitors the conditions that are subject to the guarantees to identify whether it is probable that a loss has occurred, and recognize any such losses under guarantees when those losses are estimable. As of December 31, 2007 and 2008, it is not probable that the Group will be required to make payments under the guarantees. Thus no liability has been accrued for the Group's obligation under these guarantee arrangements.

*Environmental contingencies*

Under existing legislation, management believes that there are no probable liabilities that will have a material adverse effect on the financial position or operating results of the Group. The PRC government, however, has moved, and may move further towards more rigorous enforcement of applicable laws, and towards the adoption of more stringent environmental standards. Environmental liabilities are subject to considerable uncertainties which affect management's ability to estimate the ultimate cost of remediation efforts. These uncertainties include i) the exact nature and extent of the contamination at various sites including, but not limited to refineries, oil fields, service stations, terminals and land development areas, whether operating, closed or sold, ii) the extent of required cleanup efforts, iii) varying costs of alternative remediation strategies, iv) changes in environmental remediation requirements, and v) the identification of new remediation sites. The amount of such future cost is indeterminable due to such factors as the unknown magnitude of possible contamination and the unknown timing and extent of the corrective actions that may be required. Accordingly, the outcome of environmental liabilities under proposed or future environmental legislation cannot reasonably be estimated at present, and could be material. The Group paid normal routine pollutant discharge fees of approximately RMB 1,594, RMB 2,085 and RMB 2,284 for the years ended December 31, 2006, 2007 and 2008, respectively.

*Legal contingencies*

The Group is a defendant in certain lawsuits as well as the named party in other proceedings arising in the ordinary course of business. Management has assessed the likelihood of an unfavourable outcome of such contingencies, lawsuits or other proceedings and believes that any resulting liabilities will not have a material adverse effect on the financial position, operating results or cash flows of the Group.

**30. RELATED PARTY TRANSACTIONS**

Parties are considered to be related to the Group if the Group has the ability, directly or indirectly, to control or jointly control the party or exercise significant influence over the party in making financial and operating decisions, or vice versa, or where the Group and the party are subject to common control. Related parties may be individuals (being members of key management personnel, significant shareholders and / or their close family members) or other entities and include entities which are under the significant influence of related parties of the Group where those parties are individuals, and post-employment benefit plans which are for the benefit of employees of the Group or of any entity that is a related party of the Group.

*(a) Transactions with Sinopec Group Company and its affiliates, associates and jointly controlled entities*

The Group is part of a larger group of companies under Sinopec Group Company, which is owned by the PRC government, and has significant transactions and relationships with Sinopec Group Company and its affiliates. Because of these relationships, it is possible that the terms of these transactions are not the same as those that would result from transactions among wholly unrelated parties.

**CHINA PETROLEUM & CHEMICAL CORPORATION AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)**  
**(Amounts in millions, except per share data and except otherwise stated)**

The principal related party transactions with Sinopec Group Company and its affiliates, associates and jointly controlled entities, which were carried out in the ordinary course of business, are as follows:

	Note	Years ended December 31,		
		2006	2007	2008
		RMB	RMB	RMB
Sales of goods	(i)	138,670	144,581	197,032
Purchases	(ii)	50,360	64,440	65,071
Transportation and storage	(iii)	1,587	1,141	1,199
Exploration and development services	(iv)	22,048	32,121	33,034
Production related services	(v)	12,508	19,238	13,768
Ancillary and social services	(vi)	1,710	1,621	1,611
Operating lease charges	(vii)	3,826	3,967	5,446
Agency commission income	(viii)	60	60	78
Interest received	(ix)	56	34	19
Interest paid	(x)	1,302	789	1,322
Net deposits withdrawn / (placed with) from related parties	(xi)	4,777	356	(348)
Net loans obtained from related parties	(xii)	2,291	6,987	7,457

The amounts set out in the table above in respect of each of the years in the three-year period ended December 31, 2008 represent the relevant costs to the Group and income from related parties as determined by the corresponding contracts with the related parties.

There were no guarantees given to banks by the Group in respect of banking facilities to Sinopec Group Company and its affiliates as of December 31, 2007 and 2008. Guarantees given to banks by the Group in respect of banking facilities to associates and jointly controlled entities are disclosed in Note 29.

The directors of the Company are of the opinion that the above transactions with related parties were conducted in the ordinary course of business and on normal commercial terms or in accordance with the agreements governing such transactions, and this has been confirmed by the independent non-executive directors.

Notes:

- (i) Sales of goods represent the sale of crude oil, intermediate petrochemical products, petroleum products and ancillary materials.
- (ii) Purchases represent the purchase of materials and utility supplies directly related to the Group's operations such as the procurement of raw and ancillary materials and related services, supply of water, electricity and gas.
- (iii) Transportation and storage represent the cost for the use of railway, road and marine transportation services, pipelines, loading, unloading and storage facilities.
- (iv) Exploration and development services comprise direct costs incurred in the exploration and development such as geophysical, drilling, well testing and well measurement services.
- (v) Production related services represent ancillary services rendered in relation to the Group's operations such as equipment repair and general maintenance, insurance premium, technical research, communications, fire fighting, security, product quality testing and analysis, information technology, design and engineering, construction which includes the construction of oilfield ground facilities, refineries and chemical plants, manufacture of replacement parts and machinery, installation, project management and environmental protection.
- (vi) Ancillary and social services represent expenditures for social welfare and support services such as educational facilities, media communication services, sanitation, accommodation, canteens, property maintenance and management services.
- (vii) Operating lease charges represent the rental paid to Sinopec Group Company for operating leases in respect of land, buildings and equipment.
- (viii) Agency commission income represents commission earned for acting as an agent in respect of sales of products and purchase of materials for certain entities owned by Sinopec Group Company.

## CHINA PETROLEUM & CHEMICAL CORPORATION AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued) (Amounts in millions, except per share data and except otherwise stated)

- (ix) Interest received represents interest received from deposits placed with Sinopec Finance Company Limited, a finance company controlled by Sinopec Group Company. The applicable interest rate is determined in accordance with the prevailing saving deposit rate. The balance of deposits as of December 31, 2007 and 2008 were RMB 338 and RMB 686, respectively.
- (x) Interest paid represents interest charges on the loans and advances obtained from Sinopec Group Company and its affiliates.
- (xi) Deposits placed with / withdrawn from related parties represent net deposits placed with / withdrawn from Sinopec Finance Company Limited.
- (xii) The Group obtained or repaid loans from or to Sinopec Group Company and its affiliates.

In connection with the Reorganization, the Company and Sinopec Group Company entered into a number of agreements under which 1) Sinopec Group Company will provide goods and products and a range of ancillary, social and supporting services to the Group and 2) the Group will sell certain goods to Sinopec Group Company. The terms of these agreements are summarized as follows:

- (a) The Company has entered into a non-exclusive Agreement for Mutual Provision of Products and Ancillary Services (“Mutual Provision Agreement”) with Sinopec Group Company effective from January 1, 2000 in which Sinopec Group Company has agreed to provide the Group with certain ancillary production services, construction services, information advisory services, supply services and other services and products. While each of Sinopec Group Company and the Company is permitted to terminate the Mutual Provision Agreement upon at least six months notice, Sinopec Group Company has agreed not to terminate the agreement if the Group is unable to obtain comparable services from a third party. The pricing policy for these services and products provided by Sinopec Group Company to the Group is as follows:
  - the government-prescribed price;
  - where there is no government-prescribed price, the government-guidance price;
  - where there is neither a government-prescribed price nor a government-guidance price, the market price; or
  - where none of the above is applicable, the price to be agreed between the parties, which shall be based on a reasonable cost incurred in providing such services plus a profit margin not exceeding 6%.
- (b) The Company has entered into a non-exclusive Agreement for Provision of Cultural and Educational, Health Care and Community Services with Sinopec Group Company effective from January 1, 2000 in which Sinopec Group Company has agreed to provide the Group with certain cultural, educational, health care and community services on the same pricing terms and termination conditions as agreed to in the above Mutual Provision Agreement.
- (c) The Company has entered into a series of lease agreements with Sinopec Group Company to lease certain land at a rental of approximately RMB 3,234 and RMB 4,234 per annum for the years ended December 31, 2007 and 2008, respectively, and certain buildings at a rental of approximately RMB 568 and RMB 568 per annum for the years ended December 31, 2007 and 2008, respectively. The Company and Sinopec Group Company can renegotiate the rental amount every three years for land and every year for buildings, however such amount cannot exceed the market price as determined by an independent third party. The Group has the option to terminate these leases upon six months notice to Sinopec Group Company.
- (d) The Company has entered into agreements with Sinopec Group Company effective from January 1, 2000 under which the Group has been granted the right to use certain trademarks, patents, technology and computer software developed by Sinopec Group Company.
- (e) The Company has entered into a service stations franchise agreement with Sinopec Group Company effective from January 1, 2000 under which its service stations and retail stores would exclusively sell the refined products supplied by the Group.



Pursuant to the resolutions passed at the Directors' meeting held on June 26, 2008, the Group acquired the Downhole Assets from Sinopec Group Company, primarily property, plant and equipment, for a cash consideration of RMB 1,624, which approximated the net carrying value of the assets and liabilities of the Downhole Assets.

Amounts due from / to Sinopec Group Company and its affiliates, associates and jointly controlled entities included in the following accounts caption are summarized as follows:

	<b>December 31,</b>	
	<b>2007</b>	<b>2008</b>
	<b>RMB</b>	<b>RMB</b>
Trade accounts receivable	3,990	4,081
Prepaid expenses and other current assets	7,082	4,550
Total amounts due from Sinopec Group Company and its affiliates, associates and jointly controlled entities	<u>11,072</u>	<u>8,631</u>
Trade accounts payable	5,472	3,670
Accrued expenses and other payables	12,907	12,624
Short-term loans and current portion of long-term loans from Sinopec Group Company and its affiliates	15,840	23,587
Long-term loans excluding current portion from Sinopec Group Company and its affiliates	<u>37,180</u>	<u>36,890</u>
Total amounts due to Sinopec Group Company and its affiliates, associates and jointly controlled entities	<u>71,399</u>	<u>76,771</u>

Amounts due from / to Sinopec Group Company and its affiliates, associates and jointly controlled entities, other than short-term loans and long-term loans, bear no interest, are unsecured and are repayable in accordance with normal commercial terms. The terms and conditions associated with short-term loans and long-term loans payable to Sinopec Group Company and its affiliates are set out in Note 23.

As of and for the years ended December 31, 2007 and 2008, no individually significant impairment losses for bad and doubtful debts were recognized in respect of amounts due from Sinopec Group Company and its affiliates, associates and jointly controlled entities.

**CHINA PETROLEUM & CHEMICAL CORPORATION AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)**  
**(Amounts in millions, except per share data and except otherwise stated)**

**(b) Key management personnel emoluments**

Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the Group, directly or indirectly, including directors and supervisors of the Group. The key management personnel compensations are as follows:

	<b>Years ended December 31,</b>		
	<b>2006</b>	<b>2007</b>	<b>2008</b>
	<b>RMB'000</b>	<b>RMB'000</b>	<b>RMB'000</b>
Short-term employee benefits	4,571	5,896	6,530
Retirement scheme contributions	184	184	198
	<u>4,755</u>	<u>6,080</u>	<u>6,728</u>

Total emoluments are included in “personnel expenses” as disclosed in Note 6.

**(c) Contributions to defined contribution retirement plans**

The Group participates in various defined contribution retirement plans organized by municipal and provincial governments for its staff. The details of the Group’s employee benefits plan are disclosed in Note 31. As of December 31, 2007 and 2008, the accrued contribution to post-employment benefit plans was not material.

**(d) Transactions with other state-controlled entities in the PRC**

The Group is a state-controlled energy and chemical enterprise and operates in an economic regime currently dominated by entities directly or indirectly controlled by the PRC government through its government authorities, agencies, affiliations and other organizations (collectively referred as “state-controlled entities”).

Apart from transactions with Sinopec Group Company and its affiliates, the Group has transactions with other state-controlled entities include but not limited to the following:

- sales and purchase of goods and ancillary materials;
- rendering and receiving services;
- lease of assets;
- depositing and borrowing money; and
- use of public utilities.

These transactions are conducted in the ordinary course of the Group’s business on terms comparable to those with other entities that are not state-controlled. The Group has established procurement policies, pricing strategy and approval process for purchases and sales of products and services which do not depend on whether the counterparties are state-controlled entities or not.

Having considered the transactions potentially affected by related party relationships, the Group’s pricing strategy, procurement policies and approval processes, and the information that would be necessary for an understanding of the potential effect of the related party relationship on the financial statements, the directors are of the opinion that the following related party transactions require disclosure of numeric details:

**CHINA PETROLEUM & CHEMICAL CORPORATION AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)**  
**(Amounts in millions, except per share data and except otherwise stated)**

(i) Transactions with other state-controlled energy and chemical companies

The Group's major domestic suppliers of crude oil and refined petroleum products are China National Petroleum Corporation and its subsidiaries ("CNPC Group") and China National Offshore Oil Corporation and its subsidiaries ("CNOOC Group"), which are state-controlled entities.

During the years ended December 31, 2006, 2007 and 2008, the aggregate amount of crude oil purchased by the Group's refining segment from CNPC Group and CNOOC Group and refined petroleum purchased by the Group's marketing and distribution segment from CNPC Group was RMB 64,959, RMB 70,341 and RMB 113,612, respectively.

The aggregate amounts due from / to CNPC Group and CNOOC Group are summarized as follows:

	<b>December 31,</b>	
	<b>2007</b>	<b>2008</b>
	<b>RMB</b>	<b>RMB</b>
Trade accounts receivable	326	292
Prepaid expenses and other current assets	934	113
<b>Total amounts due from CNPC Group and CNOOC Group</b>	<b>1,260</b>	<b>405</b>
Trade accounts payable	3,494	2,045
Accrued expenses and other payables	371	433
<b>Total amounts due to CNPC Group and CNOOC Group</b>	<b>3,865</b>	<b>2,478</b>

(ii) Transactions with state-controlled banks

The Group deposits its cash with several state-controlled banks in the PRC. The Group also obtains short-term and long-term loans from these banks in the ordinary course of business. The interest rates of the bank deposits and loans are regulated by the PBOC. The Group's interest income from and interest expense to these state-controlled banks in the PRC are as follows:

	<b>Years ended December 31,</b>		
	<b>2006</b>	<b>2007</b>	<b>2008</b>
	<b>RMB</b>	<b>RMB</b>	<b>RMB</b>
Interest income	466	225	244
Interest expense	5,682	5,264	6,966

The amounts of cash deposited at and loans from state-controlled banks in the PRC are summarized as follows:

	<b>December 31,</b>	
	<b>2007</b>	<b>2008</b>
	<b>RMB</b>	<b>RMB</b>
Cash and cash equivalents	6,522	5,675
Time deposits with financial institutions	647	449
<b>Total deposits at state-controlled banks in the PRC</b>	<b>7,169</b>	<b>6,124</b>
Short-term loans and current portion of long-term loans	27,813	55,841
Long-term loans excluding current portion of long-term loans	37,338	27,844
<b>Total loans from state-controlled banks in the PRC</b>	<b>65,151</b>	<b>83,685</b>

## CHINA PETROLEUM & CHEMICAL CORPORATION AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued) (Amounts in millions, except per share data and except otherwise stated)

#### 31. EMPLOYEE BENEFITS PLAN

As stipulated by the regulations of the PRC, the Group participates in various defined contribution retirement plans organized by municipal and provincial governments for its staff. The Group is required to make contributions to the retirement plans at rates ranging from 18.0% to 23.0% of the salaries, bonuses and certain allowances of its staff. A member of the plan is entitled to a pension equal to a fixed proportion of the salary prevailing at his or her retirement date. The Group has no other material obligation for the payment of pension benefits associated with these plans beyond the annual contributions described above. The Group's contributions for the years ended December 31, 2006, 2007 and 2008 were RMB 2,394, RMB 2,806 and RMB 2,861, respectively.

#### 32. SEGMENTAL REPORTING

The Group has five operating segments as follows:

- (i) Exploration and production, which explores and develops oil fields, produces crude oil and natural gas and sells such products to the refining segment of the Group and external customers.
- (ii) Refining, which processes and purifies crude oil, that is sourced from the exploration and production segment of the Group and external suppliers, and manufactures and sells petroleum products to the chemicals and marketing and distribution segments of the Group and external customers.
- (iii) Marketing and distribution, which owns and operates oil depots and service stations in the PRC, and distributes and sells refined petroleum products (mainly gasoline and diesel) in the PRC through wholesale and retail sales networks.
- (iv) Chemicals, which manufactures and sells petrochemical products, derivative petrochemical products and other chemical products mainly to external customers.
- (v) Corporate and others, which largely comprise the trading activities of the import and export companies of the Group and research and development undertaken by other subsidiaries.

CHINA PETROLEUM & CHEMICAL CORPORATION AND SUBSIDIARIES

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(Amounts in millions, except per share data and except otherwise stated)

Reportable information on the Group's business segments is as follows:

	Years ended December 31,		
	2006 RMB	2007 RMB	2008 RMB
<b>Sales of goods</b>			
Exploration and production			
External sales	19,936	20,437	26,403
Inter-segment sales	109,075	107,473	151,393
	<u>129,011</u>	<u>127,910</u>	<u>177,796</u>
Refining			
External sales	114,725	117,256	129,668
Inter-segment sales	477,766	534,671	683,965
	<u>592,491</u>	<u>651,927</u>	<u>813,633</u>
Marketing and distribution			
External sales	588,022	659,552	802,817
Inter-segment sales	4,849	2,841	3,200
	<u>592,871</u>	<u>662,393</u>	<u>806,017</u>
Chemicals			
External sales	196,024	217,452	207,396
Inter-segment sales	12,299	15,990	27,481
	<u>208,323</u>	<u>233,442</u>	<u>234,877</u>
Corporate and others			
External sales	116,181	159,172	254,037
Inter-segment sales	145,287	297,145	479,982
	<u>261,468</u>	<u>456,317</u>	<u>734,019</u>
Elimination of inter-segment sales	<u>(749,276)</u>	<u>(958,120)</u>	<u>(1,346,021)</u>
Sales of goods	<u>1,034,888</u>	<u>1,173,869</u>	<u>1,420,321</u>
<b>Other operating revenues</b>			
Exploration and production	14,155	17,757	18,705
Refining	4,750	4,996	4,948
Marketing and distribution	687	461	1,181
Chemicals	6,604	7,247	6,214
Corporate and others	657	513	732
Other operating revenues	<u>26,853</u>	<u>30,974</u>	<u>31,780</u>
<b>Other income</b>			
Refining	5,161	1,926	40,502
Marketing and distribution	—	2,937	9,840
Total other income	<u>5,161</u>	<u>4,863</u>	<u>50,342</u>
<b>Sales of goods, other operating revenues and other income</b>	<u>1,066,902</u>	<u>1,209,706</u>	<u>1,502,443</u>

CHINA PETROLEUM & CHEMICAL CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)  
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	Years ended December 31,		
	2006 RMB	2007 RMB	2008 RMB
<b>Result</b>			
<b>Operating income / (loss)</b>			
By segment			
- Exploration and production	63,182	48,766	66,569
- Refining	(25,710)	(10,452)	(61,538)
- Marketing and distribution	30,234	35,727	38,209
- Chemicals	14,458	13,306	(13,102)
- Corporate and others	(1,532)	(1,483)	(2,015)
Total operating income	80,632	85,864	28,123
<b>Income / (loss) from associates and jointly controlled entities</b>			
- Exploration and production	233	164	216
- Refining	149	(114)	(822)
- Marketing and distribution	404	519	708
- Chemicals	2,416	2,959	(92)
- Corporate and others	232	516	570
Aggregate income from associates and jointly controlled entities	3,434	4,044	580
<b>Finance costs</b>			
Interest expense	(7,101)	(7,314)	(11,326)
Interest income	538	405	445
Unrealized (loss) / gain on embedded derivative component of the Convertible Bonds	—	(3,211)	3,947
Foreign currency exchange loss	(140)	(311)	(954)
Foreign currency exchange gain	890	2,330	3,112
<b>Net finance costs</b>	(5,813)	(8,101)	(4,776)
Investment income	289	1,657	390
<b>Earning before income tax</b>	78,542	83,464	24,317
Tax (expense) / benefit	(23,504)	(24,721)	1,883
<b>Net income</b>	55,038	58,743	26,200

Information on associates and jointly controlled entities is included in Note 18 and 19. Additions to long-lived assets by operating segment are included in Notes 15 and 16.

CHINA PETROLEUM & CHEMICAL CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)  
(Amounts in millions, except per share data and except otherwise stated)

	December 31,		
	<u>2006</u>	<u>2007</u>	<u>2008</u>
	RMB	RMB	RMB
<b>Assets</b>			
<b>Segment assets</b>			
- Exploration and production	155,043	198,945	235,866
- Refining	170,888	193,956	180,270
- Marketing and distribution	108,053	127,047	132,434
- Chemicals	108,597	120,988	121,964
- Corporate and others	22,641	34,285	31,124
<b>Total segment assets</b>	<u>565,222</u>	<u>675,221</u>	<u>701,658</u>
<b>Interest in associates and jointly controlled entities</b>			
- Exploration and production	1,063	1,080	1,779
- Refining	1,398	3,915	5,415
- Marketing and distribution	4,692	5,355	5,630
- Chemicals	10,481	12,176	9,292
- Corporate and others	3,500	7,062	5,260
<b>Aggregate interest in associates and jointly controlled entities</b>	<u>21,134</u>	<u>29,588</u>	<u>27,376</u>
<b>Unallocated assets</b>	<u>24,476</u>	<u>27,916</u>	<u>38,793</u>
<b>Total assets</b>	<u><u>610,832</u></u>	<u><u>732,725</u></u>	<u><u>767,827</u></u>
<b>Liabilities</b>			
<b>Segment liabilities</b>			
- Exploration and production	30,082	45,185	62,375
- Refining	31,454	46,017	35,758
- Marketing and distribution	27,090	31,118	37,423
- Chemicals	19,142	20,786	16,220
- Corporate and others	35,913	51,804	32,566
<b>Total segment liabilities</b>	<u>143,681</u>	<u>194,910</u>	<u>184,342</u>
<b>Unallocated liabilities</b>	<u>180,494</u>	<u>205,057</u>	<u>234,163</u>
<b>Total liabilities</b>	<u><u>324,175</u></u>	<u><u>399,967</u></u>	<u><u>418,505</u></u>

Segment capital expenditure is the total cost incurred during the year to acquire segment assets that are expected to be used for more than one year.

CHINA PETROLEUM & CHEMICAL CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)  
 (Amounts in millions, except per share data and except otherwise stated)

	Years ended December 31,		
	2006	2007	2008
	RMB	RMB	RMB
<b>Capital expenditure</b>			
Exploration and production	35,198	54,498	57,646
Refining	22,587	22,763	12,491
Marketing and distribution	11,319	12,548	14,148
Chemicals	12,629	16,184	20,622
Corporate and others	2,170	3,289	2,393
	<u>83,903</u>	<u>109,282</u>	<u>107,300</u>
<b>Depreciation, depletion and amortization</b>			
Exploration and production	12,945	18,216	22,115
Refining	8,212	9,020	9,484
Marketing and distribution	3,452	6,032	4,946
Chemicals	8,537	8,977	8,463
Corporate and others	408	1,070	815
	<u>33,554</u>	<u>43,315</u>	<u>45,823</u>
<b>Impairment losses on long-lived assets</b>			
Exploration and production	552	481	5,991
Refining	—	1,070	270
Marketing and distribution	23	1,237	709
Chemicals	250	318	1,511
Corporate and others	—	—	19
	<u>825</u>	<u>3,106</u>	<u>8,500</u>



**CHINA PETROLEUM & CHEMICAL CORPORATION AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)**  
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**33. PRINCIPAL SUBSIDIARIES**

As of December 31, 2008, the following list contains the particulars of subsidiaries which principally affected the results, assets and liabilities of the Group.

<u>Name of company</u>	<u>Particulars of issued capital</u>	<u>Type of legal entity</u>	<u>Percentage of equity</u>	<u>Principal activities</u>
China Petrochemical International Company Limited	RMB 1,663	Limited company	100.00	Trading of petrochemical products
Sinopec Sales Company Limited	RMB 1,700	Limited company	100.00	Marketing and distribution of refined petroleum products
Sinopec Yangzi Petrochemical Company Limited	RMB 16,337	Limited company	100.00	Manufacturing of intermediate petrochemical products and petroleum products
Sinopec Fujian Petrochemical Company Limited (i)	RMB 2,253	Limited company	50.00	Manufacturing of plastics, intermediate petrochemical products and petroleum products
Sinopec Shanghai Petrochemical Company Limited	RMB 7,200	Limited company	55.56	Manufacturing of synthetic fibres, resin and plastics, intermediate petrochemical products and petroleum products
Sinopec Kantons Holdings Limited	HKD 104	Limited company	72.34	Trading of crude oil and petroleum products
Sinopec Yizheng Chemical Fibre Company Limited (i)	RMB 4,000	Limited company	42.00	Production and sale of polyester chips and polyester fibres
Sinopec Zhongyuan Petrochemical Company Limited	RMB 2,400	Limited company	93.51	Manufacturing of chemical products
Sinopec Shell (Jiangsu) Petroleum Marketing Company Limited	RMB 830	Limited company	60.00	Marketing and distribution of refined petroleum products
BP Sinopec (Zhejiang) Petroleum Company Limited	RMB 800	Limited company	60.00	Marketing and distribution of refined petroleum products
Sinopec Qingdao Refining and Chemical Company Limited	RMB 3,400	Limited company	85.00	Manufacturing of intermediate petrochemical products and petroleum products
China International United Petroleum and Chemical Company Limited	RMB 3,040	Limited company	100.00	Trading of crude oil and petrochemical products
Sinopec Hainan Refining and Chemical Company Limited	RMB 3,986	Limited company	75.00	Manufacturing of intermediate petrochemical products and petroleum products
Sinopec (Hong Kong) Limited	HKD 5,477	Limited company	100.00	Trading of crude oil and petrochemical products
Sinopec Senmei (Fujian) Petroleum Ltd.	RMB 1,840	Limited company	55.00	Marketing and distribution of refined petroleum products

Except for Sinopec Kantons Holdings Limited and Sinopec (Hong Kong) Limited, which are incorporated in Bermuda and Hong Kong respectively, all of the above principal subsidiaries are incorporated in the PRC.

- (i) The Group consolidated the financial statements of the entity because the Group controlled the board of this entity and had the power to govern its financial and operating policies.

## CHINA PETROLEUM & CHEMICAL CORPORATION AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued) (Amounts in millions, except per share data and except otherwise stated)

#### 34. FINANCIAL RISK MANAGEMENT AND FAIR VALUES

##### *Overview*

Financial assets of the Group include cash and cash equivalents, time deposits with financial institutions, investments, trade accounts receivable, bills receivable, amounts due from Sinopec Group Company and its affiliates, advances to third parties, amounts due from associates and jointly controlled entities, derivative financial instruments and other receivables. Financial liabilities of the Group include short-term and long-term debts, loans from Sinopec Group Company and its affiliates, trade accounts payable, bills payable, amounts due to Sinopec Group Company and its affiliates, and advances from third parties.

The Group has exposure to the following risks from its use of financial instruments:

- credit risk;
- liquidity risk;
- market risk; and
- equity price risk.

The Board of Directors has overall responsibility for the establishment, oversight of the Group's risk management framework, and developing and monitoring the Group's risk management policies.

The Group's risk management policies are established to identify and analyze the risks faced by the Group, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions and the Group's activities. The Group, through its training and management standards and procedures, aims to develop a disciplined and constructive control environment in which all employees understand their roles and obligations. Internal audit department undertakes both regular and ad hoc reviews of risk management controls and procedures, the results of which are reported to the Group's audit committee.

##### *Credit risk*

Credit risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Group's deposits placed with financial institutions and receivables from customers. To limit exposure to credit risk relating to deposits, the Group primarily places cash deposits only with large financial institution in the PRC with acceptable credit ratings. The majority of the Group's trade accounts receivable relate to sales of petroleum and chemical products to related parties and third parties operating in the petroleum and chemical industries. Management performs ongoing credit evaluations of its customers' financial condition and generally does not require collateral on trade accounts receivable. The Group maintains an impairment loss for doubtful accounts and actual losses have been within management's expectations. No single customer accounted for greater than 10% of total trade accounts receivable. The details of the Group's credit policy for and quantitative disclosures in respect of the Group's exposure on credit risk for trade receivables are set out in Note 12.

The carrying amounts of cash and cash equivalents, time deposits with financial institutions, trade accounts and bills receivables, derivative financial instruments and other receivables, represent the Group's maximum exposure to credit risk in relation to financial assets.

CHINA PETROLEUM & CHEMICAL CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)  
(Amounts in millions, except per share data and except otherwise stated)

*Liquidity risk*

Liquidity risk is the risk that the Group will not be able to meet its financial obligations as they fall due. The Group's approach in managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Group's reputation. The Group prepares monthly cash flow budget to ensure that they will always have sufficient liquidity to meet its financial obligation as they fall due. The Group arranges and negotiates financing with financial institutions and maintains a certain level of standby credit facilities to reduce liquidity risk.

As of December 31, 2007 and 2008, the Group has standby credit facilities with several PRC financial institutions which provide the Group to borrow up to RMB 164,500 and RMB 185,000 on an unsecured basis, at a weighted average interest rate of 5.619% and 4.647% per annum, respectively. As of December 31, 2007 and 2008, the Group's outstanding borrowings under these facilities were RMB 13,269 and RMB 33,484 and were included in short-term debts, respectively.

The following table sets out the remaining contractual maturities at the balance sheet date of the Group's financial liabilities, which are based on contractual undiscounted cash flows (including interest payments computed using contractual rates or, if floating, based on prevailing rates current at the balance sheet date) and the earliest date the Group would be required to repay:

<b>December 31, 2007</b>						
	<b>Carrying amount</b>	<b>Total contractual undiscounted cash flow</b>	<b>Within 1 year or on demand</b>	<b>More than 1 year but less than 2 years</b>	<b>More than 2 years but less than 5 years</b>	<b>More than 5 years</b>
	<b>RMB</b>	<b>RMB</b>	<b>RMB</b>	<b>RMB</b>	<b>RMB</b>	<b>RMB</b>
Short-term debts	44,654	45,869	45,869	—	—	—
Long-term debts	83,134	101,886	3,906	22,708	31,643	43,629
Loans from Sinopec Group Company and its affiliates	53,020	53,793	16,485	327	1,420	35,561
Trade accounts payable	93,049	93,049	93,049	—	—	—
Bills payable	12,162	12,233	12,233	—	—	—
Accrued expenses and other payables	50,084	50,084	50,084	—	—	—
	<b>336,103</b>	<b>356,914</b>	<b>221,626</b>	<b>23,035</b>	<b>33,063</b>	<b>79,190</b>
<b>December 31, 2008</b>						
	<b>Carrying amount</b>	<b>Total contractual undiscounted cash flow</b>	<b>Within 1 year or on demand</b>	<b>More than 1 year but less than 2 years</b>	<b>More than 2 years but less than 5 years</b>	<b>More than 5 years</b>
	<b>RMB</b>	<b>RMB</b>	<b>RMB</b>	<b>RMB</b>	<b>RMB</b>	<b>RMB</b>
Short-term debts	74,896	76,669	76,669	—	—	—
Long-term debts	90,254	115,721	3,442	12,712	30,013	69,554
Loans from Sinopec Group Company and its affiliates	60,477	61,659	24,503	509	627	36,020
Trade accounts payable	56,667	56,667	56,667	—	—	—
Bills payable	17,493	17,508	17,508	—	—	—
Accrued expenses and other payables	52,564	52,564	52,564	—	—	—
	<b>352,351</b>	<b>380,788</b>	<b>231,353</b>	<b>13,221</b>	<b>30,640</b>	<b>105,574</b>
Derivatives settled gross:						
Forward exchange contracts						
- outflow	(4,366)	(4,415)	(4,415)	—	—	—
- inflow	4,480	4,531	4,531	—	—	—

Management believes that the Group's current cash on hand, expected cash flows from operations and available standby credit facilities from financial institutions will be sufficient to meet the Group's working capital requirements and repay its short term debts and obligations when they become due.

**CHINA PETROLEUM & CHEMICAL CORPORATION AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)**  
**(Amounts in millions, except per share data and except otherwise stated)**

***Currency risk***

Currency risk arises on financial instruments that are denominated in a currency other than the functional currency in which they are measured. The Group's currency risk exposure primarily relates to short-term and long-term debts and loans from Sinopec Group Company and its affiliates denominated in US dollars, Japanese Yen and Hong Kong dollars, and the Group entered into a number of foreign exchange contracts to manage such exposure.

The changes in the fair value of forward exchange contracts that economically hedge monetary assets and liabilities in foreign currencies are recognized as finance costs in the consolidated statements of income. The net fair value of forward exchange contracts used by the Group as economic hedges of monetary assets and liabilities in foreign currencies as of December 31, 2007 and 2008 was RMB nil and RMB 114, respectively, recognized.

Included in derivative financial instruments, short-term and long-term debts and loans from Sinopec Group Company and its affiliates of the Group are the following amounts denominated in a currency other than the functional currency of the entity to which they relate:

	<b>December 31,</b>	
	<b>2007</b>	<b>2008</b>
<b>Gross exposure arising from loans and borrowings</b>		
US Dollars	USD (780)	USD (1,232)
Japanese Yen	JPY (33,494)	JPY (28,037)
Hong Kong Dollars	HKD (15,135)	HKD (11,192)
<b>Notional amounts of forward exchange contracts</b>		
US Dollars	USD —	USD 660

A 5 percent strengthening of Renminbi against the following currencies as of December 31 would have increased net income and retained earnings of the Group by the amounts shown below. This analysis has been determined assuming that the change in foreign exchange rates had occurred at the balance sheet date and had been applied to the foreign currency balances to which the Group has significant exposure as stated above, and that all other variables, in particular interest rates, remain constant. The analysis is performed on the same basis for 2007.

	<b>December 31,</b>	
	<b>2007</b>	<b>2008</b>
US Dollars	191	147
Japanese Yen	72	80
Hong Kong Dollars	475	370

Other than the amounts as disclosed above, the amounts of other financial assets and liabilities of the Group are substantially denominated in the functional currency of respective entity of the Group.

***Interest rate risk***

The Group's interest rate risk exposure arises primarily from its short-term and long-term debts. Debts carrying interest at variable rates and at fixed rates expose the Group to cash flow interest rate risk and fair value interest rate risk respectively. The interest rates of short-term and long-term debts, and loans from Sinopec Group Company and its affiliates of the Group are disclosed in Note 23.

As of December 31, 2007 and 2008, it is estimated that a general increase / decrease of 100 basis points in variable interest rates, with all other variables held constant, would decrease / increase the Group's net income and retained earnings by approximately RMB 154 and RMB 263, respectively. This sensitivity analysis has been determined assuming that the change in interest rates had occurred at the balance sheet date and the change was applied to the Group's debts outstanding at that date with exposure to cash flow interest rate risk. The analysis is performed on the same basis for 2007.

## CHINA PETROLEUM & CHEMICAL CORPORATION AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued) (Amounts in millions, except per share data and except otherwise stated)

#### *Equity price risk*

The Group is exposed to equity price risk arising from changes in the Company's own share price to the extent that the Company's own equity instruments underlie the fair values of derivatives of the Group. As of December 31, 2008, the Group's exposure to equity price risk is the derivative embedded in the Convertible Bonds issued by the Company as disclosed in Note 23(f).

As of December 31, 2008, it is estimated that an increase of 20% in the Company's own share price would decrease the Group's net income and retained earnings by approximately RMB 62 while a decrease of 20% in the Company's own share price would have no effect to the Group's net income and retained earnings. The sensitivity analysis has been determined assuming that the changes in the Company's own share price had occurred at the balance sheet date and that all other variables remain constant.

#### *Fair values*

The disclosures of the fair value estimates, methods and assumptions, set forth below for the Group's financial instruments, are made to comply with the requirements of IFRS 7 and IAS 39 and should be read in conjunction with the Group's consolidated financial statements and related notes. The estimated fair value amounts have been determined by the Group using market information and valuation methodologies considered appropriate. However, considerable judgment is required to interpret market data to develop the estimates of fair value. Accordingly, the estimates presented herein are not necessarily indicative of the amounts the Group could realize in a current market exchange. The use of different market assumptions and / or estimation methodologies may have a material effect on the estimated fair value amounts.

The fair values of the Group's financial instruments (other than long-term indebtedness and investment securities) approximate their carrying amounts due to the short-term maturity of these instruments. The fair values of long-term indebtedness are estimated by discounting future cash flows using current market interest rates offered to the Group for debt with substantially the same characteristics and maturities ranging 5.40% to 6.97% and 3.58% to 5.94% for the years ended December 31, 2007 and 2008, respectively. The following table presents the carrying amount and fair value of the Group's long-term indebtedness other than loans from Sinopec Group Company and its affiliates as of December 31, 2007 and 2008:

	<b>December 31,</b>	
	<b>2007</b>	<b>2008</b>
	<b>RMB</b>	<b>RMB</b>
Carrying amount	96,420	109,415
Fair value	95,600	113,060

The Group has not developed an internal valuation model necessary to make the estimate of the fair value of loans from Sinopec Group Company and its affiliates as it is not considered practicable to estimate their fair value because the cost of obtaining discount and borrowing rates for comparable borrowings would be excessive based on the Reorganization of the Group, its existing capital structure and the terms of the borrowings.

The fair value of available-for-sale equity securities, which amounted to RMB 653 and RMB 154 as of December 31, 2007 and 2008, respectively, was based on quoted market price on PRC stock exchanges. Investments in unquoted equity securities are individually and in aggregate not material to the Group's financial condition or results of operations. There are no listed market prices for such interests in the PRC and, accordingly, a reasonable estimate of fair value could not be made without incurring excessive costs. The Group intends to hold these unquoted equity securities for long term purpose.

### **35. ACCOUNTING ESTIMATES AND JUDGMENTS**

The Group's financial condition and results of operations are sensitive to accounting methods, assumptions and estimates that underlie the preparation of the financial statements. Management bases the assumptions and estimates on historical experience and on various other assumptions that it believes to be reasonable and which form the basis for making judgments about matters that are not readily apparent from other sources. On an on-going basis, management evaluates its estimates. Actual results may differ from those estimates as facts, circumstances and conditions change.

## CHINA PETROLEUM & CHEMICAL CORPORATION AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued) (Amounts in millions, except per share data and except otherwise stated)

The selection of critical accounting policies, the judgments and other uncertainties affecting application of those policies and the sensitivity of reported results to changes in conditions and assumptions are factors to be considered when reviewing the financial statements. The principal accounting policies are set forth in Note 2. Management believes the following critical accounting policies involve the most significant judgments and estimates used in the preparation of the financial statements.

#### *Oil and gas properties and reserves*

The accounting for the exploration and production's oil and gas activities is subject to accounting rules that are unique to the oil and gas industry. There are two methods to account for oil and gas business activities, the successful efforts method and the full cost method. The Group has elected to use the successful efforts method. The successful efforts method reflects the volatility that is inherent in exploring for mineral resources in that costs of unsuccessful exploratory efforts are charged to expense as they are incurred. These costs primarily include dry hole costs, seismic costs and other exploratory costs. Under the full cost method, these costs are capitalized and written-off or depreciated over time.

Engineering estimates of the Group's oil and gas reserves are inherently imprecise and represent only approximate amounts because of the subjective judgments involved in developing such information. There are authoritative guidelines regarding the engineering criteria that have to be met before estimated oil and gas reserves can be designated as "proved". Proved and proved developed reserves estimates are updated at least annually and take into account recent production and technical information about each field. In addition, as prices and cost levels change from year to year, the estimate of proved and proved developed reserves also changes. This change is considered a change in estimate for accounting purposes and is reflected on a prospective basis in related depreciation rates.

Future dismantlement costs for oil and gas properties are estimated with reference to engineering estimates after taking into consideration the anticipated method of dismantlement required in accordance with industry practices in similar geographic area, including estimation of economic life of oil and gas properties, technology and price level. The present values of these estimated future dismantlement costs are capitalized as oil and gas properties with equivalent amounts recognized as provision for dismantlement costs.

Despite the inherent imprecision in these engineering estimates, these estimates are used in determining depreciation expense, impairment expense and future dismantlement costs. Depreciation rates are determined based on estimated proved developed reserve quantities (the denominator) and capitalized costs of producing properties (the numerator). Producing properties' capitalized costs are amortized based on the units of oil or gas produced.

#### *Impairment for long lived assets*

If circumstances indicate that the net book value of a long-lived asset may not be recoverable, the asset may be considered "impaired", and an impairment loss may be recognized in accordance with IAS 36 "Impairment of Assets". The carrying amounts of long-lived assets are reviewed periodically in order to assess whether the recoverable amounts have declined below the carrying amounts. These assets are tested for impairment whenever events or changes in circumstances indicate that their recorded carrying amounts may not be recoverable. When such a decline has occurred, the carrying amount is reduced to recoverable amount. For goodwill, the recoverable amount is estimated annually. The recoverable amount is the greater of the net selling price and the value in use. It is difficult to precisely estimate selling price because quoted market prices for the Group's assets or cash-generating units are not readily available. In determining the value in use, expected cash flows generated by the asset or the cash-generating unit are discounted to their present value, which requires significant judgment relating to level of sale volume, selling price and amount of operating costs. Management uses all readily available information in determining an amount that is a reasonable approximation of recoverable amount, including estimates based on reasonable and supportable assumptions and projections of sale volume, selling price and amount of operating costs.

## CHINA PETROLEUM & CHEMICAL CORPORATION AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued) (Amounts in millions, except per share data and except otherwise stated)

#### *Depreciation*

Property, plant and equipment, other than oil and gas properties, are depreciated on a straight-line basis over the estimated useful lives of the assets, after taking into account the estimated residual value. Management reviews the estimated useful lives of the assets regularly in order to determine the amount of depreciation expense to be recorded during any reporting period. The useful lives are based on the Group's historical experience with similar assets and take into account anticipated technological changes. The depreciation expense for future periods is adjusted if there are significant changes from previous estimates.

#### *Impairment for bad and doubtful debts*

Management estimates impairment losses for bad and doubtful debts resulting from the inability of the Group's customers to make the required payments. Management bases the estimates on the aging of the accounts receivable balance, customer credit-worthiness, and historical write-off experience. If the financial condition of the customers were to deteriorate, actual write-offs would be higher than estimated.

#### *Allowance for diminution in value of inventories*

If the costs of inventories fall below their net realizable values, an allowance for diminution in value of inventories is recognized. Net realizable value represents the estimated selling price in the ordinary course of business, less the estimated costs of completion and the estimated costs necessary to make the sale. Management bases the estimates on all available information, including the current market prices of the finished goods and raw materials, and historical operating costs. If the actual selling prices were to be lower or the costs of completion were to be higher than estimated, the actual allowance for diminution in value of inventories could be higher than estimated.

#### **36. POSSIBLE IMPACT OF AMENDMENTS, NEW STANDARDS AND INTERPRETATIONS ISSUED BUT NOT YET EFFECTIVE FOR THE ANNUAL ACCOUNTING PERIOD ENDED DECEMBER 31, 2008**

Up to the date of issue of these financial statements, the IASB has issued a number of amendments, new standards and interpretations which are not yet effective for the annual accounting period ended December 31, 2008 and which have not been adopted in these financial statements.

Management is in the process of making an assessment of what the impact of these amendments, new standards and new interpretations is expected to be in the period of initial application and has so far concluded that the adoption of these amendments, new standards and new interpretations is unlikely to have a significant impact on the Group's results of operations and financial position.

#### **37. POST BALANCE SHEET EVENTS**

Pursuant to the resolution passed at the Directors' meeting on March 27, 2009, the Group entered into a number of agreements with Sinopec Group Company and fellow subsidiaries to acquire the entire equity interests of Sinopec Qingdao Petrochemical Company Limited and certain assets and related liabilities related to the exploration and production, the refining, and the marketing and distribution segments from Sinopec Group Company and fellow subsidiaries for a total cash consideration of RMB 1,839, and to dispose of certain assets in the Group's chemicals segment to a fellow subsidiary for a cash consideration of RMB 157. These transactions are subject to the approval from the relevant PRC governmental and regulatory bodies.

#### **38. PARENT AND ULTIMATE HOLDING COMPANY**

The directors consider the parent and ultimate holding company of the Group as of December 31, 2008 is Sinopec Group Company, a state-owned enterprise established in the PRC. This entity does not produce financial statements available for public use.

**CHINA PETROLEUM & CHEMICAL CORPORATION AND SUBSIDIARIES**

**SUPPLEMENTAL INFORMATION ON OIL AND GAS PRODUCING  
ACTIVITIES (UNAUDITED)  
(All currency amounts in millions)**

The results of operations for producing activities for the years ended December 31, 2006, 2007 and 2008 are shown above. Revenues include sales to unaffiliated parties and transfers (essentially at third-party sales prices) to other segments of the Group. All revenues reported in this table do not include royalties to others as there were none. In accordance with SFAS No. 69, income taxes are based on statutory tax rates, reflecting allowable deductions and tax credits. General corporate overhead and interest income and expense are excluded from the results of operations.

**Table IV: Reserve quantities information**

The Group's estimated net proved underground oil and gas reserves and changes thereto for the years ended December 31, 2006, 2007 and 2008 are shown in the following table.

Proved oil and gas reserves are the estimated quantities of crude oil, natural gas, and natural gas liquids which geological and engineering data demonstrate with reasonable certainty to be recoverable in future years from known reservoirs under existing economic and operating conditions, i.e., prices and costs as of the date the estimate is made. Prices include consideration of changes in existing prices provided only by contractual arrangements, but not on escalations based upon future conditions. Due to the inherent uncertainties and the limited nature of reservoir data, estimates of underground reserves are subject to change as additional information becomes available.

Proved reserves do not include additional quantities recoverable beyond the term of the relevant production licenses, or that may result from extensions of currently proved areas, or from application of improved recovery processes not yet tested and determined to be economical. The Group's estimated proved reserves do not include any quantities that are recoverable through application of tertiary recovery techniques.

Proved developed reserves are the quantities expected to be recovered through existing wells with existing equipment and operating methods.

"Net" reserves exclude royalties and interests owned by others and reflect contractual arrangements in effect at the time of the estimate.

	<b>Years ended December 31,</b>		
	<b>2006</b>	<b>2007</b>	<b>2008</b>
<b>Proved developed and undeveloped reserves (oil) (million barrels)</b>			
Beginning of year	3,294	3,293	3,024
Revisions of previous estimates	(10)	(250)	(94)
Improved recovery	146	125	98
Extensions and discoveries	148	148	110
Production	(285)	(292)	(297)
End of year	<u>3,293</u>	<u>3,024</u>	<u>2,841</u>
<b>Proved developed reserves</b>			
Beginning of year	<u>2,870</u>	<u>2,903</u>	<u>2,651</u>
End of year	<u>2,903</u>	<u>2,651</u>	<u>2,451</u>
<b>Proved developed and undeveloped reserves (gas) (billion cubic feet)</b>			
Beginning of year	2,952	2,856	6,331
Revisions of previous estimates	(9)	222	203
Extensions and discoveries	170	3,536	718
Production	(257)	(283)	(293)
End of year	<u>2,856</u>	<u>6,331</u>	<u>6,959</u>
<b>Proved developed reserves</b>			
Beginning of year	<u>1,557</u>	<u>1,472</u>	<u>1,518</u>
End of year	<u>1,472</u>	<u>1,518</u>	<u>1,571</u>



**CHINA PETROLEUM & CHEMICAL CORPORATION AND SUBSIDIARIES**

**SUPPLEMENTAL INFORMATION ON OIL AND GAS PRODUCING  
ACTIVITIES (UNAUDITED) - (Continued)  
(All currency amounts in millions)**

**Table V: Standardized measure of discounted future net cash flows**

The standardized measure of discounted future net cash flows, related to the above proved oil and gas reserves, is calculated in accordance with the requirements of SFAS No. 69. Estimated future cash inflows from production are computed by applying year-end prices for oil and gas to year-end quantities of estimated net proved reserves. Future price changes are limited to those provided by contractual arrangements in existence at the end of each reporting year. Future development and production costs are those estimated future expenditures necessary to develop and produce year-end estimated proved reserves based on year-end cost indices, assuming continuation of year-end economic conditions. Estimated future income taxes are calculated by applying appropriate year-end statutory tax rates to estimated future pre-tax net cash flows, less the tax basis of related assets. Discounted future net cash flows are calculated using 10% midperiod discount factors. This discounting requires a year-by-year estimate of when the future expenditure will be incurred and when the reserves will be produced.

The information provided does not represent management's estimate of the Group's expected future cash flows or value of proved oil and gas reserves. Estimates of proved reserve quantities are imprecise and change over time as new information becomes available. Moreover, probable and possible reserves, which may become proved in the future, are excluded from the calculations. The arbitrary valuation prescribed under SFAS No. 69 requires assumptions as to the timing and amount of future development and production costs. The calculations are made for the years ended December 31, 2006, 2007 and 2008 and should not be relied upon as an indication of the Group's future cash flows or value of its oil and gas reserves.

	<b>Years ended December 31,</b>		
	<b>2006</b>	<b>2007</b>	<b>2008</b>
Future cash flows	1,235,524	1,835,471	977,904
Future production costs	(487,895)	(799,408)	(536,442)
Future development costs	(33,523)	(68,970)	(42,207)
Future income tax expenses	(189,465)	(196,103)	(44,249)
Undiscounted future net cash flows	524,641	770,990	355,006
10% annual discount for estimated timing of cash flows	(241,180)	(349,987)	(113,367)
Standardized measure of discounted future net cash flows	283,461	421,003	241,639

**Table VI: Changes in the standardized measure of discounted future net cash flows**

	<b>Years ended December 31,</b>		
	<b>2006</b>	<b>2007</b>	<b>2008</b>
	<b>RMB</b>	<b>RMB</b>	<b>RMB</b>
Sales and transfers of oil and gas produced, net of production costs	(92,849)	(77,522)	(112,424)
Net changes in prices and production costs	(114,796)	165,191	(231,578)
Net change due to extensions, discoveries and improved recoveries	51,445	68,788	32,011
Revisions of previous quantity estimates	(1,207)	(46,980)	(8,298)
Previously estimated development costs incurred during the year	8,516	8,783	27,578
Accretion of discount	30,190	23,726	36,031
Net change in income taxes	43,784	(4,716)	76,964
Others	332	272	352
Net change for the year	(74,585)	137,542	(179,364)

**SIGNATURE**

The registrant hereby certifies that it meets all of the requirements for filing on Form 20-F and that it has duly caused and authorized the undersigned to sign this annual report on its behalf.

China Petroleum & Chemical Corporation

By:           /s/ Chen Ge          

Name: Chen Ge

Title: Secretary to the Board of Directors

Date: May 20, 2009