SEMICONDUCTOR MANUFACTURING INTERNATIONAL CORP
Form 20-F
June 22, 2009

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 20-F

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2008
Commission file number 1-31994

Semiconductor Manufacturing International Corporation
(Exact name of Registrant as specified in its charter)
(Translation of Registrant s name into English)

Cayman Islands
(Jurisdiction of incorporation or organization)
18 Zhangjiang Road, Pudong New Area, Shanghai, China 201203
(Address of principal executive offices)
Ms. Morning Wu, Acting Chief Financial Officer
Telephone: (8621) 3861-0000
Facsimile: (8621) 3895-3568

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

Title of each class	Name of each exchange on which registered
Ordinary Shares, par value US$0.0004	The Stock Exchange of Hong Kong Limited*
American Depositary Shares	The New York Stock Exchange, Inc.

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 ordinary shares as of the close of the period covered by the annual report.
As of December 31, 2008, there were 22,327,784,827 ordinary shares, par value US$0.0004 per share, outstanding, of which 3,154,359,550 ordinary shares were held in the form of 63,087,191 ADSs. Each ADS represents 50 ordinary shares.
Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes þ No o
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 o No þ

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 þ No o
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes o No þ
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 Securities Exchange Act of 1934 (Check one):

Large accelerated filer þ	Accelerated filer o	Non-accelerated filer o

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

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

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 Securities Exchange Act of 1934). Yes o No þ

* Not for trading, but only in connection with the listing of American Depositary Shares on the New York Stock Exchange, Inc.

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CAUTIONARY STATEMENT FOR PURPOSES OF THE SAFE HARBOR PROVISIONS OF THE PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995

This annual report contains, in addition to historical information, forward-looking statements within the meaning of the safe harbor provisions of the U.S. Private Securities Litigation Reform Act of 1995. These forward-looking statements are based on SMIC s current assumptions, expectations and projections about future events. SMIC uses words like believe, anticipate, intend, estimate, expect, project and similar expressions to identify forward loo statements, although not all forward-looking statements contain these words. These forward-looking statements are necessarily estimates reflecting the best judgment of SMIC s senior management and involve significant risks, both known and unknown, uncertainties and other factors that may cause SMIC s actual performance, financial condition or results of operations to be materially different from those suggested by the forward-looking statements including, among others, risks associated with cyclicality and market conditions in the semiconductor industry, intense competition, timely wafer acceptance by SMIC s customers, timely introduction of new technologies, SMIC s ability to ramp new products into volume, supply and demand for semiconductor foundry services, industry overcapacity, shortages in equipment, components and raw materials, availability of manufacturing capacity, the current global financial crisis, orders or judgments from pending litigation and financial stability in end markets.

Except as required by law, SMIC undertakes no obligation and does not intend to update any forward-looking statement, whether as a result of new information, future events or otherwise.

ADDITIONAL INFORMATION

References in this annual report to:

Average selling price of wafers are to simplified average selling price which is calculated as total revenue divided by total shipments.

China or the PRC are to the People s Republic of China, excluding for the purpose of this annual report, Hong Kong, Macau and Taiwan;

Company or SMIC are to Semiconductor Manufacturing International Corporation;

EUR are to Euros;

global offering are to the initial public offering of our ADSs and our ordinary shares, which offering was completed on March 18, 2004;

HK$ are to Hong Kong dollars;

Jpy are to Japanese Yen;

NYSE or New York Stock Exchange are to the New York Stock Exchange, Inc.;

Rmb or RMB are to Renminbi;

SEC are to the U.S. Securities and Exchange Commission;

SEHK , HKSE or Hong Kong Stock Exchange are to The Stock Exchange of Hong Kong Limited; and

US$ or USD are to U.S. dollars.

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All references in this annual report to silicon wafer quantities are to 8-inch wafer equivalents, unless otherwise specified. Conversion of quantities of 12-inch wafers to 8-inch wafer equivalents is achieved by multiplying the number of 12-inch wafers by 2.25. When we refer to the capacity of wafer fabrication facilities, we are referring to the installed capacity based on specifications established by the manufacturers of the equipment used in those facilities. References to key process technology nodes, such as 0.35 micron, 0.25 micron, 0.18 micron, 0.15 micron, 0.13 micron, 90 nanometer, and 65 nanometer resolutions are down to but not including the next key process technology node of finer resolution. For example, when we state 0.25 micron process technology, that also includes 0.22 micron, 0.21 micron, 0.20 micron and 0.19 micron technologies. 0.18 micron process technology also includes 0.17 micron and 0.16 micron technologies; 0.15 micron process technology includes 0.14 micron technology; and 0.13 micron process technology includes 0.11 micron and 0.10 micron technologies. References to U.S. GAAP mean the generally accepted accounting principles in the United States. Unless otherwise indicated, our financial information presented in this annual report has been prepared in accordance with U.S. GAAP.

All references to our ordinary shares in this annual report gives effect to the 10-for-1 share split we effected in the form of a share dividend immediately prior to the completion of the global offering. All references to price per ordinary share and price per preference share reflect the share split referenced above.

The Glossary of Technical Terms contained in Annex A of this annual report sets forth the description of certain technical terms and definitions used in this annual report.

PART I

Item 1. Identity of Directors, Senior Management and Advisors

Not applicable.

Item 2. Offer Statistics and Expected Timetable

Not applicable.

Item 3. Key Information

Selected Consolidated Financial Data

The selected consolidated financial data presented below as of and for the years ended December 31, 2006, 2007 and 2008 are derived from, and should be read in conjunction with, and are qualified in their entirety by reference to, our audited consolidated financial statements, including the related notes, included elsewhere in this annual report. The selected consolidated financial data as of and for the years ended December 31, 2004 and 2005 is derived from our audited consolidated financial statements not included in this annual report. The selected consolidated financial data presented below has been prepared in accordance with U.S. GAAP.

	For the year ended December 31,				
	2004	**2005**	**2006**	**2007**	**2008**
	(in US$ thousands, except for per share, per ADS data, percentages, and operating data)				
Statement of Operations Data:					
Sales	$ 974,664	$ 1,171,319	$ 1,465,323	$ 1,549,765	**$ 1,353,711**
Cost of sales[(1)]	716,225	1,105,134	1,338,155	1,397,038	**1,412,851**
Gross profit	258,439	66,185	127,168	152,727	**(59,140)**

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	For the year ended December 31,				
	2004	**2005**	**2006**	**2007**	**2008**
	(in US$ thousands, except for per share, per ADS data, percentages, and operating data)				
Operating expenses:					
Research and development	74,113	78,865	94,171	97,034	**102,240**
General and administrative	54,038	35,701	47,365	74,490	**58,841**
Selling and marketing	10,384	17,713	18,231	18,716	**20,661**
Litigation settlement	16,695				
Amortization of acquired intangible assets	14,368	20,946	24,393	27,071	**32,191**
Impairment loss of long-lived assets					**106,741**
Income from sale of plant and equipment and other fixed assets			(43,122)	(28,651)	**(2,877)**
Total operating expenses	169,598	153,225	141,038	188,659	**317,797**
Income (loss) from operations	88,841	(87,040)	(13,870)	(35,932)	**(376,937)**
Other income (expenses):					
Interest income	10,587	11,356	14,916	12,349	**11,542**
Interest expense	(13,698)	(38,784)	(50,926)	(37,936)	**(50,767)**
Foreign currency exchange gain (loss)	8,218	(3,355)	(21,912)	11,250	**3,230**
Other, net	2,441	4,462	1,821	2,238	**7,429**
Total other income (expense), net	7,548	(26,322)	(56,101)	(12,100)	**(28,566)**
Income (loss) before income tax	96,389	(113,362)	(69,971)	(48,032)	**(405,503)**

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	For the year ended December 31,				
	2004	**2005**	**2006**	**2007**	**2008**
	(in US$ thousands, except for per share, per ADS data, percentages, and operating data)				
Income tax benefit (expense)	(186)	(285)	24,928	29,720	**(26,433)**
Minority interest		251	(19)	2,856	**(7,851)**
Loss from equity investment		(1,379)	(4,201)	(4,013)	**(444)**
Net (loss) income before cumulative effect of a change in accounting principle	96,203	(114,775)	(49,263)	(19,468)	**(440,231)**
Cumulative effect of a change in accounting principle			5,154		
Net (loss) income	96,203	(114,775)	(44,109)	(19,468)	**(440,231)**
Deemed dividend on preference shares[(2)]	18,840				
Income (loss) attributable to holders of ordinary shares	77,363	(114,775)	(44,109)	(19,468)	**(440,231)**
Income (loss) per ordinary share, basic	$ 0.01	$ (0.00)	$ (0.00)	$ (0.00)	**$ (0.02)**
Income (loss) per ordinary share, diluted	$ 0.00	$ (0.00)	$ (0.00)	$ (0.00)	**$ (0.02)**
Ordinary shares used in calculating basic income (loss) per ordinary share[(4)]	14,199,163,517	18,184,429,255	18,334,498,923	18,501,940,489	**18,682,544,866**
Ordinary shares used in calculating	17,934,393,066	18,184,429,255	18,334,498,923	18,501,940,489	**18,682,544,866**

diluted income (loss) per ordinary share[3][4]

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	For the year ended December 31,				
	2004	**2005**	**2006**	**2007**	**2008**
	(in US$ thousands, except for per share, per ADS data, percentages, and operating data)				
Income (loss) per ADS, basic[5]	$ 0.27	$ (0.32)	$ (0.12)	$ (0.05)	**$ (1.18)**
Income (loss) per ADS, diluted[5]	$ 0.22	$ (0.32)	$ (0.12)	$ (0.05)	**$ (1.18)**
ADS used in calculating basic income (loss) per ADS[5]	283,983,270	363,688,585	366,689,978	370,038,810	**373,650,897**
ADS used in calculating diluted income (loss) per ADS[5]	358,687,861	363,688,585	366,689,978	370,038,810	**373,650,897**
Other Financial Data:					
Gross margin	26.50%	5.70%	8.70%	9.90%	**-4.40%**
Operating margin	9.10%	-7.40%	-0.90%	-2.30%	**-27.80%**
Net margin	9.90%	-9.80%	-3.00%	-1.30%	**-32.50%**
Operating Data:					
Wafers shipped (in 8 equivalents)					
Total	943,463	1,347,302	1,614,888	1,849,957	**1,611,208**
ASP[6]	1,033	869	907	838	**840**

(1) Including amortization of deferred stock compensation for employees directly involved in manufacturing activities.

(2) Deemed dividend represents the difference between the sale and conversion

prices of warrants to purchase convertible preference shares we issued and their respective fair market values.

(3) Anti-dilutive preference shares, options and warrants were excluded from the weighted average ordinary shares outstanding for the diluted per share calculation.

(4) All share information has been adjusted retroactively to reflect the 10-for-1 share split effected upon completion of the global offering of our ordinary shares in March 2004.

(5) Fifty ordinary shares equals one ADS.

(6) Total sales/total wafers shipped.

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	As of December 31,				
	2004	2005	2006	2007	**2008**
	(in US$ thousands)				
Balance Sheet Data:					
Cash and cash equivalents	$ 607,173	$ 585,797	$ 363,620	$ 469,284	**$ 450,230**
Restricted cash					**6,255**
Short-term investments	20,364	13,796	57,951	7,638	**19,928**
Accounts receivable, net of allowances	169,188	241,334	252,185	298,388	**199,372**
Inventories	144,018	191,238	275,179	248,310	**171,637**
Total current assets	955,418	1,047,465	1,049,666	1,075,302	**926,858**
Land use rights, net	39,198	34,768	38,323	57,552	**74,293**
Plant and equipment, net	3,311,925	3,285,631	3,244,401	3,202,958	**2,963,386**
Total assets	4,384,276	4,586,633	4,541,292	4,708,444	**4,270,622**
Total current liabilities	723,871	896,038	677,362	930,190	**899,773**
Total long-term liabilities	544,462	622,497	817,710	730,790	**578,689**
Total liabilities	1,268,333	1,518,535	1,495,072	1,660,980	**1,478,462**
Minority interest		38,782	38,800	34,944	**42,795**
Stockholders equity	$ 3,115,942	$ 3,029,316	$ 3,007,420	$ 3,012,519	**$ 2,749,365**

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	For the year ended December 31,				
	2004	2005	2006	2007	**2008**
	(in US$ thousands, except percentages)				
Cash Flow Data:					
Net income (loss)	$ 96,203	$ (114,775)	$ (49,263)	$ (19,468)	**$ (440,231)**
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:					
Depreciation and amortization	456,961	769,472	919,616	706,277	**761,809**
Net cash provided by operating activities	518,662	648,105	769,649	672,465	**569,782**
Purchases of plant and equipment	(1,838,773)	(872,519)	(882,580)	(717,171)	**(669,055)**
Net cash used in investing activities	(1,826,787)	(859,652)	(917,369)	(643,344)	**(761,713)**
Net cash provided by (used in) financing activities	1,469,764	190,364	(74,440)	76,637	**173,314**
Net increase (decrease) in cash and cash equivalents	$ 161,896	$ (21,376)	$ (222,177)	$ 105,664	**$ (19,054)**
Other Financial Data:					
Gross margin	26.50%	5.70%	8.70%	9.90%	**-4.40%**
Operating margin	9.10%	-7.40%	-0.90%	-2.30%	**-27.80%**
Net margin	9.90%	-9.80%	-3.00%	-1.30%	**-32.50%**

Risk Factors

Risks Related to Our Financial Condition and Business

We may not be able to achieve or maintain a level of profitability, primarily due to our high fixed costs and correspondingly high levels of depreciation expenses.

Our losses from operations totaled $35.9 million in 2007 and $376.9 million in 2008. We may not be able to achieve or maintain profitability on an annual or quarterly basis, primarily because our business is characterized by high fixed costs relating to equipment purchases, which result in correspondingly high levels of depreciation expenses. We will continue to incur high capital expenditures and depreciation expenses as we equip and ramp up additional fabs, expand our capacity at our existing fabs and construct new fabs.

The cyclical nature of the semiconductor industry and periodic overcapacity in the industry make our business and operating results particularly vulnerable to economic downturns, such as the current global economic crisis.

The semiconductor industry has historically been highly cyclical and, at various times, has experienced significant downturns characterized by fluctuations in end-user demand, reduced demand for integrated circuits, rapid erosion of average selling prices and production overcapacity. Companies in the semiconductor industry have expanded aggressively during periods of increased demand in order to have the capacity needed to meet expected demand in the future. If actual demand does not increase or declines, or if companies in the industry expand too aggressively in light of the actual increase in demand, the industry will generally experience a period in which industry-wide capacity exceeds demand, as was the case in the first quarter of 2009 during the current global economic crisis.

During the current global economic crisis, the United States and other countries around the world have been experiencing deteriorating economic conditions. There has been an erosion of global consumer confidence amidst concerns over declining asset values, inflation, energy costs, geopolitical issues, the availability and cost of credit, rising unemployment, and the stability and solvency of financial institutions, financial markets, businesses and sovereign nations.

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Adverse economic conditions could cause our expenses to vary materially from our expectations. The failure of financial institutions could negatively impact our treasury operations, as the financial condition of such parties may deteriorate rapidly and without notice in times or market volatility and disruption. Other income and expense could vary materially from expectations depending on changes in interest rates, borrowing costs and currency exchange rates. Economic downturns also may lead to restructuring actions and associated expenses.

During periods when industry-wide capacity exceeds demand, as was the case in the first quarter of 2009 during the current global economic crisis, our operations are subject to more intense competition, and our results of operations are likely to suffer because of the resulting pricing pressure and capacity underutilization. Severe pricing pressure could result in the overall foundry industry becoming less profitable, at least for the duration of the downturn, and could prevent us from achieving or maintaining profitability. We expect that industry cyclicality will continue. In addition, a slowdown in the growth in demand for, or the continued reduction in selling prices of, devices that use semiconductors may decrease the demand for our services and reduce our profit margins. If we cannot take appropriate or effective actions in a timely manner during the current and any future economic downturns, such as reducing our costs to sufficiently offset declines in demand for our services, our business and operating results may be adversely affected. A prolonged period of economic decline could have a material adverse effect on our results of operations. Economic uncertainty also makes it difficult for us to make accurate forecasts of revenue, gross margin and expenses.

The impact of deteriorating economic conditions on our customers and suppliers could adversely affect our business.

Customer financial difficulties have resulted, and could result in the future, in increases in bad debt write-offs and additions to reserves in our receivables portfolio. In particular, our exposure to certain financially troubled customers could have an adverse affect on our results of operations. In addition, we depend on suppliers of raw materials, such as silicon wafers, gases and chemicals, and spare equipment parts, in order to maintain our production processes. Our business may be disrupted if we are unable to obtain these raw materials from our suppliers and our suppliers from their suppliers due to the insolvency of key suppliers who may be unable to obtain credit.

The former trend of increasing demand for foundry services has slowed down, primarily as a result of the current global economic crisis. As a result, we may achieve a lower rate of return on investments than previously anticipated and our business and operating results may be adversely affected.

Until the onset of the current global economic crisis, the demand for foundry services by IDMs, fabless semiconductor companies and systems companies had been increasing in recent years. We made significant investments in anticipation of the continuation of this trend. The reversal of this trend as a result of the current global economic crisis will likely result in a lower rate of return on our investments than anticipated. For example, some IDMs have changed their strategy and targeted greater internal production, and consequently they have reduced their outsourcing of wafer fabrication. In addition, as a result of the current industry downturn, in order to maintain their equipment s utilization rates, these IDMs may allocate a smaller portion of their fabricating needs to foundry service providers and perform a greater amount of foundry services for system companies and fabless semiconductor companies. As a result, our business and operating results may be adversely affected.

Our results of operations may fluctuate from year to year, which may make it difficult to predict our future performance which may be below our expectations or those of the public market analysts and investors in these periods.

Our sales, expenses, and results of operations may fluctuate significantly from year to year due to a number of factors, many of which are outside our control. Our business and operations are subject to a number of factors, including:

- our customers sales outlook, purchasing patterns and inventory adjustments based on general economic conditions or other factors;
- the loss of one or more key customers or the significant reduction or postponement of orders from such customers;
- timing of new technology development and the qualification of this technology by our customers;

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timing of our expansion and development of our facilities;
our ability to obtain equipment and raw materials; and
our ability to obtain financing in a timely manner.

Due to the factors noted above and other risks discussed in this section, many of which are beyond our control, you should not rely on year-to-year comparisons to predict our future performance. Unfavorable changes in any of the above factors may adversely affect our business and operating results. In addition, our operating results may be below the expectations of public market analysts and investors in some future periods.

If we are unable to maintain high capacity utilization, optimize the technology and product mix of our services or improve our yields, our margins may substantially decline, thereby adversely affecting our operating results.

Our ability to achieve and maintain profitability depends, in part, on our ability to:

maintain high capacity utilization, which is the actual number of wafers we produce in relation to our capacity;
optimize our technology and product mix, which is the relative number of wafers fabricated utilizing higher margin technologies as compared to commodity and lower margin technologies; and
continuously maintain and improve our yield, which is the percentage of usable fabricated devices on a wafer.

Our capacity utilization affects our operating results because a large percentage of our costs are fixed. In general, more advanced technologies sell for higher prices and higher margins. Therefore, our technology and product mix has a direct impact upon our average selling prices and overall margins. Our yields directly affect our ability to attract and retain customers, as well as the price of our services. If we are unable to maintain high capacity utilization, optimize the technology and product mix of our wafer production and continuously improve our yields, our margins may substantially decline, thereby adversely affecting our operating results.

Our rapid expansion has presented significant challenges to our management and administrative systems and resources, and as a result, we may experience difficulties managing our growth, which may adversely affect our business and operating results.

Since our inception in 2000, we have grown rapidly. Our wafer shipment and sales grew from zero in 2000 to 1,611,208 wafers and US$1.4 billion in 2008. During this period, we commenced commercial production at two 8-inch fabs (which includes our Shanghai mega fab and Tianjin fab) and one 12-inch mega fab in Beijing, and the range of process technologies we offered grew significantly. We are also in the process of ramping up one additional 12-inch fab at our Shanghai site and have already undertaken management contracts to manage the operations of wafer manufacturing facilities in Chengdu and Wuhan, China. In addition, we are constructing one additional 8-inch fab in Shenzhen. At December 31, 2000, we had 122 employees; and at December 31, 2008, we had 10,598 employees. We may hire a significant number of additional employees as our fabs in Tianjin, Beijing, and Shanghai increase in production capacity. This expansion, as well as our participation in a joint venture with Toppan Printing Co., Ltd. in Shanghai and a joint venture with United Test and Assembly Center Ltd. to establish an assembly and testing facility in Chengdu, and the management of wafer manufacturing facilities in Chengdu and Wuhan, China, have presented, and continue to present, significant challenges for our management and administrative systems and resources. If we fail to develop and maintain management and administrative systems and resources sufficient to keep pace with our planned growth, we may experience difficulties managing our growth and our business and operating results could be adversely affected.

If we lose one or more of our key personnel without obtaining adequate replacements in a timely manner or if we are unable to retain and recruit skilled personnel, our operations could become disrupted and the growth of our business could be delayed or restricted.

Our success depends on the continued service of our key executive officers, and in particular, Richard Ru Gin Chang, our President and Chief Executive Officer. We do not carry key person insurance on any of our personnel. If we lose the services of any of our key executive officers, it could be very difficult to find, relocate and integrate adequate replacement personnel into our operations, which could seriously harm our operations and the growth of our business.

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We will require an increased number of experienced executives, engineers and other skilled employees in the future to implement our growth plans. There is intense competition for the services of these personnel in the semiconductor industry. In addition, we expect demand for skilled and experienced personnel in China to increase in the future as new wafer fabrication facilities and other similar high technology businesses are established there. If we are unable to retain our existing personnel or attract, assimilate and retain new experienced personnel in the future, our operations could become disrupted and the growth of our business could be delayed or restricted.

Our customers generally do not place purchase orders far in advance, which makes it difficult for us to predict our future sales, adjust our production costs and efficiently allocate our capacity on a timely basis and could therefore have an adverse effect on our business and operating results.

Our customers generally do not place purchase orders far in advance of the required shipping dates. In addition, due to the cyclical nature of the semiconductor industry, our customers purchase orders have varied significantly from period to period. As a result, we do not typically operate with any significant backlog, which makes it difficult for us to forecast our sales in future periods. Also, since our cost of sales and operating expenses have high fixed cost components, including depreciation and employee costs, we may be unable to adjust our cost structure in a timely manner to compensate for shortfalls in sales. Our current and anticipated customers may not place orders with us in accordance with our expectations or at all. As a result, it may be difficult to plan our capacity, which requires significant lead time to ramp-up and cannot be altered easily. If our capacity does not match our customer demand, we will either be burdened with expensive and unutilized overcapacity or unable to support our customers requirements, both of which could have an adverse effect on our business and results of operations.

Our sales cycles can be long, which could adversely affect our operating results and cause our income stream to be unpredictable.

Our sales cycles, which measure the time between our first contact with a customer and the first shipment of product orders to the customer, vary substantially and can last as long as one year or more, particularly for new technologies. Sales cycles to IDM customers typically take relatively longer since they usually require our engineers to become familiar with the customer s proprietary technology before production can commence. In addition, even after we make the initial product shipments, it may take the customer several more months to reach full production of that product using our foundry services. As a result of these long sales cycles, we may be required to invest substantial time and incur significant expenses in advance of the receipt of any product order and related revenue. Orders ultimately received may not be in accordance with our expectation with respect to product, volume, price or other terms, which could adversely affect our operating results and cause our income stream to be unpredictable.

We must consistently anticipate trends in technology development or else we will be unable to maintain or increase our business and operating margins.

The semiconductor industry is developing rapidly and the related technology is constantly evolving. If we are unable to anticipate the trends in technology development and rapidly develop and implement new and innovative technology that our customers require, we may not be able to produce sufficiently advanced products at competitive prices. As the life cycle for a process technology matures, the average selling price falls. Accordingly, unless we continually upgrade our capability to manufacture any new products that our customers design, our customers may use the services of our competitors instead of ours and the average selling prices of our wafers may fall, which could adversely affect our business and operating margins.

Our sales are dependent upon a small number of customers and any decrease in sales to any of them could adversely affect our results of operations.

We have been dependent on a small number of customers for a substantial portion of our business. For the year ended December 31, 2008, our five largest customers accounted for 58.2% of our total sales. We expect that we will continue to be dependent upon a relatively limited number of customers for a significant portion of our sales. Sales generated from these customers, individually or in the aggregate, may not reach or exceed our expectations or historical levels in any future period. Our sales could be significantly reduced if any of these customers cancels or reduces its orders, significantly changes its product delivery schedule, or demands lower prices, which could have an adverse effect on our results of operations.

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Since our operating cash flows will not be sufficient to cover our planned capital expenditures, we will require additional external financing, which may not be available on acceptable terms or at all. Any failure to raise adequate funds in a timely manner could adversely affect our business and operating results.

In 2008, our capital expenditures totaled approximately US$666 million and we currently expect our capital expenditures in 2009 to total approximately US$190 million to be adjusted based on market conditions. These capital expenditures will be used primarily to expand our operations at our mega-fabs in Shanghai and Beijing. In addition, our actual expenditures may exceed our planned expenditures for a variety of reasons, including changes in our business plan, our process technology, market conditions, equipment prices, customer requirements or interest rates. Future acquisitions, mergers, strategic investments, or other developments also may require additional financing. The amount of capital required to meet our growth and development targets is difficult to predict in the highly cyclical and rapidly changing semiconductor industry.

Our operating cash flows may not be sufficient to meet our capital expenditure requirements in 2009. If our operating cash flows are insufficient, we plan to fund the expected shortfall through bank loans. If necessary, we will also explore other forms of external financing. Our ability to obtain external financing is subject to a variety of uncertainties, including:

- our future financial condition, results of operations and cash flows;
- general market conditions for financing activities of semiconductor companies;
- our future stock price; and
- our future credit rating.

External financing may not be available in a timely manner, on acceptable terms, or at all. Since our capacity expansion is a key component of our overall business strategy, any failure to raise adequate funds could adversely affect our business and operating results.

The construction and equipping of new fabs and the expansion of existing fabs are subject to certain risks that could result in delays or cost overruns, which could require us to expend additional capital and adversely affect our business and operating results.

We plan to continue to expand our business through the development of new fabs. There are a number of events that could delay these expansion projects or increase the costs of building and equipping these or future fabs in accordance with our plans. Such potential events include, but are not limited to:

- shortages and late delivery of building materials and facility equipment;
- delays in the delivery, installation, commissioning and qualification of our manufacturing equipment;
- seasonal factors, such as a long and intensive wet season that limits construction;
- labor disputes;
- design or construction changes with respect to building spaces or equipment layout;
- delays in securing the necessary governmental approvals and land use rights; and
- technological, capacity and other changes to our plans for new fabs necessitated by changes in market conditions.

As a result, our projections relating to capacity, process technology capabilities or technology developments may significantly differ from actual capacity, process technology capabilities or technology developments.

Delays in the construction and equipping or expansion of any of our fabs could result in the loss or delayed receipt of earnings, an increase in financing costs, or the failure to meet profit and earnings projections, any of which could

adversely affect our business and operating results.

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If we cannot compete successfully in our industry, particularly in China, our results of operations and financial condition will be adversely affected.

The worldwide semiconductor foundry industry is highly competitive. We compete with other foundries, such as TSMC, United Microelectronics Corporation, or UMC, and Chartered Semiconductor Manufacturing Ltd., or Chartered Semiconductor, as well as the foundry services offered by some IDMs, such as IBM. We also compete with smaller semiconductor foundries in China, Korea, Malaysia and other countries. Some of our competitors have greater access to capital and substantially higher capacity, longer or more established relationships with their customers, superior research and development capability, and greater marketing and other resources than we do. As a result, these companies may be able to compete more aggressively over a longer period of time than we can.

Our competitors have established operations in mainland China in order to compete for the growing domestic market in China. TSMC has commenced commercial production at its fab in China, and UMC has established a relationship with a fab in commercial production in China. We understand that the ability of these fabs to manufacture wafers using certain more advanced technologies is subject to restrictions by the home jurisdiction of TSMC and UMC. Such restrictions could be reduced or lifted at any time, which may lead to increased domestic competition with such competitors and adversely affect our business and operating results.

Our ability to compete successfully depends to some extent upon factors outside of our control, including import and export controls, exchange controls, exchange rate fluctuations, interest rate fluctuations and political developments. If we cannot compete successfully in our industry or are unable to maintain our position as a leading foundry in China, our results of operations and financial condition will be adversely affected.

We may be unable to obtain in a timely manner and at a reasonable cost the equipment necessary for our business and therefore may be unable to achieve our expansion plans or meet our customers orders, which could negatively impact our competitiveness, financial condition and results of operations.

The semiconductor industry is capital-intensive and requires investment in advanced equipment that is available from a limited number of manufacturers. The market for equipment used in semiconductor foundries is characterized, from time to time, by significant demand, limited supply and long delivery cycles. Our business plan depends upon our ability to obtain our required equipment in a timely manner and at acceptable prices. During times of significant demand for the types of equipment we use, lead times for delivery can be as long as one year. Shortages of equipment could result in an increase in equipment prices and longer delivery times. If we are unable to obtain equipment in a timely manner and at a reasonable cost, we may be unable to achieve our expansion plans or meet our customers orders, which could negatively impact our competitiveness, financial condition, and results of operations.

We expect to have an ongoing need to obtain licenses for the proprietary technology of others, which subjects us to the payment of license fees and potential delays in the development and marketing of our products.

While we continue to develop and pursue patent protection for our own technologies, we expect to continue to rely on third party license arrangements to enable us to manufacture certain advanced wafers. As of December 31, 2008, we had been granted four hundred fifty six patents worldwide, of which, fifty three are in Taiwan, fifty four are in the U.S., and three hundred forty nine are in China, whereas we believe our competitors and other industry participants have been issued numerous patents concerning wafer fabrication in multiple jurisdictions. Our limited patent portfolio may in the future adversely affect our ability to obtain licenses to the proprietary technology of others on favorable license terms due to our inability to offer cross-licensing arrangements. The fees associated with such licenses could adversely affect our financial condition and operating results. They might also render our services less competitive. If for any reason we are unable to license necessary technology on acceptable terms, it may become necessary for us to develop alternative technology internally, which could be costly and delay the marketing and delivery of key products and therefore have an adverse effect on our business and operating results. In addition, we may be unable to independently develop the technology required by our customers on a timely basis or at all, in which case our customers may purchase wafers from our competitors.

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We may be subject to claims of intellectual property rights infringement owing to the nature of our industry, our limited patent portfolio and limitations of the indemnification provisions in our technology license agreements. These claims could adversely affect our business and operating results.

There is frequent intellectual property litigation, involving patents, copyrights, trade secrets, mask works and other intellectual property subject matters, in our industry. In some cases, a company can avoid or settle litigation on favorable terms because it possesses patents that can be asserted against the plaintiff. The limited size of our current patent portfolio will not likely place us in such a bargaining position. Moreover, some of our technology license agreements with our major technology partners do not provide for us to be indemnified in the event that the processes we license pursuant to such agreements infringe third party intellectual property rights. We could be sued for allegedly infringing one or more patents as to which we will be unable to obtain a license and unable to design around. As a result, we would be foreclosed from manufacturing or selling the products which are dependent upon such technology, which could have a material adverse effect on our business. We may litigate the issues of whether these patents are valid or infringed, but in the event of a loss we could be required to pay substantial monetary damages and be enjoined from further production or sale of such products.

If we breach the terms and conditions of a settlement agreement regarding the patent and trade secret litigation with TSMC, we may be required to accelerate the payment of the then outstanding amounts due under the settlement agreement. If we are unable to successfully defend ourselves within the current ongoing litigation with TSMC, we may be required to pay damages, obtain a license from TSMC, or discontinue sales of certain of our products.

On August 25, 2006, TSMC filed a lawsuit against the Company and certain subsidiaries, namely SMIC (Shanghai), SMIC (Beijing) and SM IC (Americas) in the Superior Court of the State of California, County of Alameda for alleged breach of a settlement agreement, alleged breach of promissory notes and alleged trade secret misappropriation by the Company. TSMC seeks, among other things, damages, injunctive relief, attorneys fees, and the acceleration of the remaining payments outstanding under that settlement agreement.

In the present litigation, TSMC alleges that the Company has incorporated TSMC trade secrets in the manufacture of the Company s 0.13 micron or smaller process products. TSMC further alleges that as a result of this claimed breach, TSMC s patent license is terminated and the covenant not to sue is no longer in effect with respect to the Company s larger process products. The Company has vigorously denied all allegations of misappropriation. The Court has made no finding that TSMC s claims are valid. The Court has set a trial date of September 8, 2009.

On September 13, 2006, the Company announced that in addition to filing a response strongly denying the allegations of TSMC in the United States lawsuit, it filed on September 12, 2006, a cross-complaint against TSMC seeking, among other things, damages for TSMC s breach of contract and breach of implied covenant of good faith and fair dealing.

On November 16, 2006, the High Court in Beijing, the People s Republic of China, accepted the filing of a complaint by the Company and its wholly-owned subsidiaries, namely, SMIC (Shanghai) and SMIC (Beijing), regarding the unfair competition arising from the breach of bona fide (i.e. integrity, good faith) principle and commercial defamation by TSMC (PRC Complaint). In the PRC Complaint, the Company is seeking, among other things, an injunction to stop TSMC s infringing acts, public apology from TSMC to the Company and compensation from TSMC to the Company, including profits gained by TSMC from their infringing acts.

On August 14, 2007, the Company filed an amended cross-complaint against TSMC seeking, among other things, damages for TSMC s breach of contract and breach of patent license agreement. TSMC thereafter denied the allegations of the Company s amended cross-complaint and subsequently filed additional claims that the Company breached a settlement agreement by filing an action in the Beijing High Court. The Company has denied these additional claims by TSMC.

On August 15-17, 2007, the California Court held a preliminary injunction hearing on TSMC s motion to enjoin use of certain process recipes in certain of the Company s 0.13 micron logic process flows.

On September 7, 2007, the Court denied TSMC s preliminary injunction motion, thereby leaving unaffected the Company s development and sales. However, the court required the Company to provide 10 days advance notice to TSMC if the Company plans to disclose logic technology to non-SMIC entities under certain circumstances, to allow

TSMC to object to the planned disclosure.

In May 2008, TSMC filed a motion in the California Court for summary adjudication against the Company on several of the Company s cross claims. The Company opposed the motion and on August 6, 2008, the Court granted in part and denied in part TSMC s motion.

On June 23, 2008, the Company filed in the California court a cross-complaint against TSMC seeking, among other things, damages for TSMC s unlawful misappropriation of trade secrets from SMIC to improve its competitive position against SMIC.

On July 10, 2008, the California Court held a preliminary injunction hearing on TSMC s motion to enjoin disclosure of information on certain process recipes in the Company s 0.30 micron logic process flows to 3rd parties. On August 8, 2008, the Court granted-in-part TSMC s motion and preliminarily enjoined SMIC from disclosing fourteen 0.30 ìm process steps. On October 3, 2008, SMIC filed a notice of appeal of the Court s August 8, 2008 Order with the California Court of Appeal. This appeal is currently pending.

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During the pre-trial proceedings in the matter, questions arose regarding the actual terms of the 2005 Settlement Agreement between SMIC and TSMC. Accordingly, the California Court held a preliminary trial on January 13 to 16, 2009, limited to a determination of the terms of the Settlement Agreement and an interpretation of any requirements to meet and confer prior to institution of litigation. On March 10, 2009, the Court issued a Statement of Decision finding, in part, that an agreement between the parties was executed on January 30, 2005, and thereafter amended on February 2, 2005, as urged by TSMC. The Company believes the Court s ruling is erroneous. The ruling may be appealed by SMIC following the filing of a final judgment by the Court in this matter.

On May 1, 2009, the Company filed motions for summary adjudication against TSMC s claims for breach of promissory notes and violation of The California Uniform Trade Secrets Act. The motions will be heard by the Court on July 17, 2009.

The California Court has further scheduled a trial upon all liability issues related to a selected list of TSMC trade secret claims and SMIC trade secret claims to commence on September 8, 2009.

In the Company s action in the Beijing High People s Court, following an unsuccessful challenge to that Court s jurisdiction by TSMC, the Court has held evidentiary hearings on October 15, October 29, and November 25, 2008. The Court rendered its first-instance judgment on June 10, 2009. Claims of SMIC against TSMC were not supported by the Court in the first-instance judgment. The first-instance judgment is not final and either TSMC or SMIC may further appeal to the PRC Supreme People s Court according to the law.

If TSMC were to succeed on its claims in the United States, we may be ordered to pay damages for breach of contract and discontinue sales of certain of our products in the United States or elsewhere.

The occurrence of any of these events could have a material adverse effect on our business and operating results and, in any event, the cost of litigation is substantial.

If our relationships with our technology partners deteriorate or we are unable to enter into new technology alliances, we may not be able to continue providing our customers with leading edge process technology, which could adversely affect our competitive position and operating results.

Enhancing our process technologies is critical to our ability to provide high quality services for our customers. We intend to continue to advance our process technologies through internal research and development efforts and technology alliances with other companies. Although we have an internal research and development team focused on developing new process technologies, we depend upon our technology partners to advance our portfolio of process technologies. We currently have joint technology development arrangements and technology sharing arrangements with several companies and research institutes. If we are unable to continue our technology alliances with these entities, or maintain on mutually beneficial terms any of our other joint development arrangements, research and development alliances and other similar agreements, or are unable to enter into new technology alliances with other leading developers of semiconductor technology, we may not be able to continue providing our customers with leading edge process technology, which could adversely affect our competitive position and operating results.

Global or regional economic, political and social conditions could adversely affect our business and operating results.

External factors such as potential terrorist attacks, acts of war, financial crises, such as the current global economic crisis, or geopolitical and social turmoil in those parts of the world that serve as markets for our products could significantly adversely affect our business and operating results in ways that cannot presently be predicted. These uncertainties could make it difficult for our customers and us to accurately plan future business activities. More generally, these geopolitical, social and economic conditions could result in increased volatility in worldwide financial markets and economies that could adversely impact our sales. We are not insured for losses and interruptions caused by terrorist acts or acts of war. Therefore, any of these events or circumstances could adversely affect our business and operating results.

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The recent outbreak of the H1N1 swine flu, the recurrence of an outbreak of the H5N1 strain of bird flu (Avian Flu), Severe Acute Respiratory Syndrome (SARS), or an outbreak of any other similar epidemic could, directly or indirectly, adversely affect our operating results.

The recent outbreak of the H1N1 virus in North America and Europe has caused governments to take measures to prevent spread of the virus. In addition, there have been reports of swine flu cases in Asia. If the H1N1 virus further spreads, the epidemic could negatively affect the economy. For example, past occurrences of epidemics such as SARS have caused different degrees of damage to the national and local economies in China. If any of our employees are identified as a possible source of spreading the H1N1 virus, the Avian Flu or any other similar epidemic, we may be required to quarantine employees that are suspected of being infected, as well as others that have come into contact with those employees. We may also be required to disinfect our affected premises, which could cause a temporary suspension of our manufacturing capacity, thus adversely affecting our operations. The current outbreak of the H1N1 virus or a recurrence of an outbreak of SARS, Avian Flu or other similar epidemic could restrict the level of economic activities generally and/or slow down or disrupt our business activities which could in turn adversely affect our results of operations.

Exchange rate fluctuations could increase our costs, which could adversely affect our operating results and the value of our ADSs.

Our financial statements are prepared in U.S. dollars. Our sales are generally denominated in U.S. dollars and our operating expenses and capital expenditures are generally denominated in U.S. dollars, Japanese Yen, Euros and Renminbi. Although we enter into foreign currency forward exchange contracts, we are still affected by fluctuations in exchange rates between the U.S. dollar and each of the Japanese Yen, the Euro and the Renminbi. Any significant fluctuations among these currencies may lead to an increase in our costs, which could adversely affect our operating results. See Risks Related to Conducting Operations in China Devaluation or appreciation in the value of the Renminbi or restrictions on convertibility of the Renminbi could adversely affect our business and operating results for a discussion of risks relating to the Renminbi.

Fluctuations in the exchange rate of the Hong Kong dollar against the U.S. dollar will affect the U.S. dollar value of the ADSs, since our ordinary shares are listed and traded on the Hong Kong Stock Exchange and the price of such shares are denominated in Hong Kong dollars. While the Hong Kong government has continued to pursue a pegged exchange rate policy, with the Hong Kong dollar trading in the range of HK$7.75 to HK$7.85 per US$1.00 for 2008, we cannot assure you that such policy will be maintained. Exchange rate fluctuations also will affect the amount of U.S. dollars received upon the payment of any cash dividends or other distributions paid in Hong Kong dollars and the Hong Kong dollar proceeds received from any sales of ordinary shares. Therefore, such fluctuations could also adversely affect the value of our ADSs.

If we fail to maintain an effective system of internal control over financial reporting, we may not be able to accurately report our financial results or prevent fraud and, because of the inherent limitation of internal control over financial reporting, material misstatements due to error or fraud may not be prevented or detected on a timely basis.

We are subject to reporting obligations under the United States securities laws. The SEC, as required by Section 404 of the Sarbanes-Oxley Act of 2002, or the Sarbanes-Oxley Act, adopted rules requiring public companies to include a management report on such company s internal controls over financial reporting in its annual report, which contains management s assessment of the effectiveness of the company s internal controls over financial reporting. In addition, an independent registered public accounting firm must attest to the effectiveness of the company s internal controls over financial reporting. Our management has concluded that our internal controls over our financial reporting as of December 31, 2008 are effective. However, we cannot assure you that in the future we or our independent registered public accounting firm will not identify material weaknesses during the Section 404 of the Sarbanes-Oxley Act audit process or for other reasons. In addition, because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. As a result, if we fail to maintain effective internal controls over financial reporting or should we be unable to prevent or detect material misstatements due to error or fraud on a timely basis, investors could lose confidence in the reliability of our financial statements, which in

turn could harm our business and negatively impact the trading price of our securities. Furthermore, we have incurred and expect to continue to incur considerable costs and to use significant management time and other resources in an effort to comply with Section 404 and other requirements of the Sarbanes-Oxley Act.

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Risks Related to Manufacturing

Our manufacturing processes are highly complex, costly and potentially vulnerable to impurities and other disruptions, which could significantly increase our costs and delay product shipments to our customers.

Our manufacturing processes are highly complex, require advanced and costly equipment, demand a high degree of precision and may have to be modified to improve yields and product performance. Dust and other impurities, difficulties in the fabrication process or defects with respect to the equipment or facilities used can lower yields, cause quality control problems, interrupt production or result in losses of products in process. As system complexity has increased and process technology has become more advanced, manufacturing tolerances have been reduced and requirements for precision have become even more demanding. As a result, we may experience production difficulties, which could significantly increase our costs and delay product shipments to our customers.

We may have difficulty in ramping up production, which could cause delays in product deliveries and loss of customers and adversely affect our business and operating results.

As is common in the semiconductor industry, we may experience difficulty in ramping up production at new or existing facilities, such as our Beijing mega-fab in which we expect to add a significant amount of new equipment. This could be due to a variety of factors, including hiring and training of new personnel, implementing new fabrication processes, recalibrating and re-qualifying existing processes and the inability to achieve required yield levels.

In the future, we may face construction delays or interruptions, infrastructure failure, or delays in upgrading or expanding existing facilities or changing our process technologies, which may adversely affect our ability to ramp up production in accordance with our plans. Our failure to ramp up our production on a timely basis could cause delays in product deliveries, which may result in the loss of customers and sales. It could also prevent us from recouping our investments in a timely manner or at all, and adversely affect our business and operating results.

We have formed joint ventures that, if not successful, may adversely impact our business and operating results.

In July 2004, we announced an agreement with Toppan Printing Co., Ltd., to establish Toppan SMIC Electronics (Shanghai) Co., Ltd., a joint venture in Shanghai, to manufacture color filters and micro-lenses for CMOS image sensors. In May 2005, we announced an agreement with United Test and Assembly Center Ltd. to establish a joint venture in Chengdu to provide assembly and testing services for memory and logic devices.

The results of the joint ventures are reflected in our operating results to the extent of our ownership interest, and losses of the joint ventures could adversely impact our operating results. For example, as a result of our ownership of Toppan SMIC Electronics (Shanghai) Co., Ltd., we recorded a loss of US$0.44 million in 2008. Integration of assets and operations being contributed by each partner will involve complex activities that must be completed in a short period of time. The joint ventures are likely to continue to face numerous challenges in commencing their operations and operating successfully. The business of the joint ventures will be subject to operational risks that would normally arise for these types of businesses pertaining to manufacturing, sales, service, marketing, and corporate functions. Competition in the CMOS image sensor market and semiconductor assembly and testing industry will involve challenges from well-established companies with substantial resources and significant market share.

If the joint ventures are not successful or less successful than we anticipate, we may incur higher costs for performing assembly and testing services through our current partners or for manufacturing color filters and micro-lenses, which typically require mature technologies and thus command a lower wafer price and generate lower margins, at our existing fabs. Either result may adversely affect our business and operating results.

If we are unable to obtain raw materials and spare parts in a timely manner, our production schedules could be delayed and our costs could increase.

We depend on suppliers of raw materials, such as silicon wafers, gases and chemicals, and spare equipment parts, in order to maintain our production processes. To maintain operations, we must obtain from our suppliers sufficient quantities of quality raw materials and spare equipment parts at acceptable prices and in a timely manner. The most important raw material used in our production is silicon in the form of raw wafers. We currently purchase approximately 68.0% of our overall raw wafer requirements from our top three raw wafer suppliers. In addition, a portion of our gas and chemical requirements currently must be sourced from outside China. We may not be able to obtain adequate supplies of raw materials and spare parts in a timely manner and at a reasonable cost. In addition,

from time to time, we may need to reject raw materials and parts that do not meet our specifications, resulting in potential delays or declines in output. If the supply of raw materials and necessary spare parts is substantially reduced or if there are significant increases in their prices, we may incur additional costs to acquire sufficient quantities of these parts and materials to maintain our production schedules and commitments to customers.

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Our production may be interrupted, limited or delayed if we cannot maintain sufficient sources of fresh water and electricity, which could adversely affect our business and operating results.

The semiconductor fabrication process requires extensive amounts of fresh water and a stable source of electricity. As our production capabilities increase and our business grows, our requirements for these resources will grow substantially. While we have not, to date, experienced any instances of the lack of sufficient supplies of water or material disruptions in the electricity supply to any of our fabs, we may not have access to sufficient supplies of water and electricity to accommodate our planned growth. Droughts, pipeline interruptions, power interruptions, electricity shortages or government intervention, particularly in the form of rationing, are factors that could restrict our access to these utilities in the areas in which our fabs are located. In particular, our fab in Tianjin and our Beijing mega-fab are located in areas that are susceptible to severe water shortages during the summer months. If there is an insufficient supply of fresh water or electricity to satisfy our requirements, we may need to limit or delay our production, which could adversely affect our business and operating results. In addition, a power outage, even of very limited duration, could result in a loss of wafers in production and a deterioration in yield.

Our operations may be delayed or interrupted due to natural disasters which could adversely affect our business and operating results.

We depend on suppliers of raw materials, such as silicon wafers, gases and chemicals, and spare equipment parts, in order to maintain our production processes in addition to requiring extensive amounts of fresh water and a stable source of electricity. The occurrence of natural disasters such as earthquakes may disrupt this required access to goods and services provided by our suppliers as well as access to fresh water and electricity. As a result, our production could be limited or delayed due to the disruption of access to required supplies, in addition to possible damage caused to our manufacturing equipment and related infrastructure, which could adversely affect our business and operating results.

We are subject to the risk of damage due to fires or explosions because the materials we use in our manufacturing processes are highly flammable. Such damage could temporarily reduce our manufacturing capacity, thereby adversely affecting our business and operating results.

We use highly flammable materials such as silane and hydrogen in our manufacturing processes and are therefore subject to the risk of loss arising from explosions and fires. While we have not, to date, experienced any explosion or fire due to the nature of our raw materials, the risk of explosion and fire associated with these materials cannot be completely eliminated. Although we maintain comprehensive fire insurance and insurance for the loss of property and the loss of profit resulting from business interruption, our insurance coverage may not be sufficient to cover all of our potential losses due to an explosion or fire. If any of our fabs were to be damaged or cease operations as a result of an explosion or fire, it could temporarily reduce our manufacturing capacity, which could adversely affect our business and operating results.

Our Beijing mega-fab is located in an area that is susceptible to seasonal dust storms, which could create impurities in the production process at these facilities and require us to take additional measures or spend additional capital to further insulate these fabs from dust, thereby adversely affecting our business and operating results.

The location of our Beijing mega-fab makes it susceptible to seasonal dust storms, which could cause dust particles to enter the buildings and affect the production process. Although we are constructing precautionary filtration systems, these may not adequately insulate the Beijing mega-fab against dust contamination. If dust were to affect production in the Beijing mega-fab, we could experience quality control problems, losses of products in process and delays in shipping products to our customers. In addition, we may have to spend additional capital to further insulate the Beijing mega-fab from dust if our current precautionary measures are insufficient. The occurrence of any of these events could adversely affect our business and operating results.

Our operations may be delayed or interrupted and our business could suffer as a result of steps we may be required to take in order to comply with environmental regulations.

We are subject to a variety of Chinese environmental regulations relating to the use, discharge and disposal of toxic or otherwise hazardous materials used in our production processes. Any failure or any claim that we have failed to comply with these regulations could cause delays in our production and capacity expansion and affect our company s

public image, either of which could harm our business. In addition, any failure to comply with these regulations could subject us to substantial fines or other liabilities or require us to suspend or adversely modify our operations.

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Risks Related to Conducting Operations in China

Our business is subject to extensive government regulation and benefits from certain government incentives, and changes in these regulations or incentives could adversely affect our business and operating results.

The Chinese government has broad discretion and authority to regulate the technology industry in China. China s government has also implemented policies from time to time to regulate economic expansion in China. The economy of China has been transitioning from a planned economy to a market-oriented economy. Although in recent years the Chinese government has implemented measures emphasizing the utilization of market forces for economic reform, the reduction of state ownership of productive assets, and the establishment of sound corporate governance in business enterprises, a substantial portion of productive assets in China is still owned by the Chinese government. In addition, the Chinese government continues to play a significant role in regulating industrial development. It also exercises significant control over China s economic growth through the allocation of resources, controlling payment of foreign currency-denominated obligations, setting monetary policy, and providing preferential treatment to particular industries or companies. New regulations or the readjustment of previously implemented regulations could require us to change our business plan, increase our costs or limit our ability to sell products and conduct activities in China, which could adversely affect our business and operating results.

In addition, the Chinese government and provincial and local governments have provided, and continue to provide, various incentives to domestic companies in the semiconductor industry, including our company, in order to encourage the development of the industry. Such incentives include tax rebates, reduced tax rates, favorable lending policies, and other measures. Any of these incentives could be reduced or eliminated by governmental authorities at any time. For example, in 2004, the Chinese government announced that by April 1, 2005, the preferential value-added tax policies, which previously entitled certain qualified companies to receive a refund of the amount exceeding 3% of the actual value-added tax burden relating to self-made integrated circuit product sales, would be eliminated. While we have not previously benefited materially from such preferential value-added tax policies, any reduction or elimination of other incentives currently provided to us could adversely affect our business and operating results.

Because our business model depends on growth in the electronics manufacturing supply chain in China, any slowdown in this growth could adversely affect our business and operating results.

Our business is dependent upon the economy and the business environment in China. In particular, our growth strategy is based upon the assumption that demand in China for devices that use semiconductors will continue to grow. Therefore, any slowdown in the growth of consumer demand in China for products that use semiconductors, such as computers, mobile phones or other consumer electronics, could have a serious adverse effect on our business. In addition, our business plan assumes that an increasing number of non-domestic IDMs, fabless semiconductor companies and systems companies will establish operations in China. Any decline in the rate of migration to China of semiconductor design companies or companies that require semiconductors as components for their products could adversely affect our business and operating results.

Limits placed on exports into China could substantially harm our business and operating results.

The growth of our business will depend on the ability of our suppliers to export, and our ability to import, equipment, materials, spare parts, process know-how and other technologies and hardware into China. Any restrictions placed on the import and export of these products and technologies could adversely impact our growth and substantially harm our business. In particular, the United States requires our suppliers and us to obtain licenses to export certain products, equipment, materials, spare parts and technologies from that country. If we or our suppliers are unable to obtain export licenses in a timely manner, our business and operating results could be adversely affected.

In July 1996, thirty-three countries ratified the Wassenaar Arrangement on Export Controls for Conventional Arms and Dual-Use Goods and Technologies, which established a worldwide arrangement to restrict the transfer of conventional arms and dual-use goods and technologies. Under the terms of the Wassenaar Arrangement, the participating countries, including the United States, have restricted exports to China of technology, equipment, materials and spare parts that potentially may be used for military purposes in addition to their commercial applications. To the extent that technology, equipment, materials or spare parts used in our manufacturing processes are or become subject to the restrictions of the arrangement, our ability to procure these products and technology

could be impaired, which could adversely affect our business and operating results. There could also be a change in the export license regulatory regime in the countries from which we purchase our equipment, materials and spare parts that could delay our ability to obtain export licenses for the equipment, materials, spare parts and technology we require to conduct our business.

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Devaluation or appreciation in the value of the Renminbi or restrictions on convertibility of the Renminbi could adversely affect our business and operating results.

The value of the Renminbi is subject to changes in China s governmental policies and to international economic and political developments. Since 1994, the conversion of Renminbi into foreign currencies, including Hong Kong and U.S. dollars, has been based on rates set by the People s Bank of China (PBOC), which are set daily based on the previous day s interbank foreign exchange market rates and current exchange rates on the world financial markets. The Renminbi to U.S. dollar exchange rate experienced significant volatility prior to 1994, including periods of sharp devaluation. On July 21, 2005, the PBOC announced an adjustment of the exchange rate of the U.S. dollar to Renminbi from 1:8.27 to 1:8.11 and modified the system by which the exchange rates are determined. The central parity rate of the U.S. Dollar to Renminbi was set at 6.8346 on December 31, 2008 versus 7.3046 on December 28, 2007 by PBOC. The cumulative appreciation of the Renminbi against the U.S. dollar in 2008 was approximately 6.43%. There remains significant international pressure on the PRC government to adopt an even more flexible currency policy, which could result in a further and more significant appreciation of the Renminbi against the U.S. dollar. As a result, the exchange rate may become volatile and the Renminbi may be devalued again against the U.S. dollar or other currencies, or the Renminbi may be permitted to enter into a full or limited free float, which may result in an appreciation in the value of the Renminbi against the U.S. dollar, any of which could have an adverse affect on our business and operating results.

In the past, financial markets in many Asian countries have experienced severe volatility and, as a result, some Asian currencies have experienced significant devaluation from time to time. The devaluation of some Asian currencies may have the effect of rendering exports from China more expensive and less competitive and therefore place pressure on China s government to devalue the Renminbi. An appreciation in the value of the Renminbi could have a similar effect. Any devaluation of the Renminbi could result in an increase in volatility of Asian currency and capital markets. Future volatility of Asian financial markets could have an adverse impact on our ability to expand our product sales into Asian markets outside of China.

We receive a portion of our sales in Renminbi, which is currently not a freely convertible currency. For the year ended December 31, 2008, approximately 5.4% of our sales were denominated in Renminbi. While we have used these proceeds for the payment of our Renminbi expenses, we may in the future need to convert these sales into foreign currencies to allow us to purchase imported materials and equipment, particularly as we expect the proportion of our sales to China-based companies to increase in the future. Under China s existing foreign exchange regulations, payments of current account items, including profit distributions, interest payments and expenditures from trade may be made in foreign currencies without government approval, except for certain procedural requirements. The Chinese government may, however, at its discretion, restrict access in the future to foreign currencies for current account transactions and prohibit us from converting our Renminbi sales into foreign currencies. If this were to occur, we may not be able to meet our foreign currency payment obligations.

China s entry into the World Trade Organization has resulted in lower Chinese tariff levels, which benefit our competitors from outside China and could adversely affect our business and operating results.

As a result of joining the World Trade Organization, or WTO, China has reduced its average rate of import tariffs to 11.5% in 2003 and will reduce it further by 2010. The import tariff for some information technology-related products has been reduced to zero. As a consequence, we expect stronger competition in China from our foreign competitors, particularly in terms of product pricing, which could adversely affect our business and operating results.

China s legal system embodies uncertainties that could adversely affect our business and operating results.

Since 1979, many new laws and regulations covering general economic matters have been promulgated in China. Despite this activity to develop the legal system, China s system of laws is not yet complete. Even where adequate law exists in China, enforcement of existing laws or contracts based on existing law may be uncertain and sporadic, and it may be difficult to obtain swift and equitable enforcement or to obtain enforcement of a judgment by a court of another jurisdiction. The relative inexperience of China s judiciary in many cases creates additional uncertainty as to the outcome of any litigation. In addition, interpretation of statutes and regulations may be subject to government policies reflecting domestic political changes.

Our activities in China will be subject to administrative review and approval by various national and local agencies of China s government. See Item 4 Information on the Company Regulation. Because of the changes occurring in China s legal and regulatory structure, we may not be able to secure the requisite governmental approval for our activities. Failure to obtain the requisite governmental approval for any of our activities could adversely affect our business and operating results.

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Our corporate structure may restrict our ability to receive dividends from, and transfer funds to, our Chinese operating subsidiaries, which could restrict our ability to act in response to changing market conditions and reallocate funds from one Chinese subsidiary to another in a timely manner.

We are a Cayman Islands holding company and substantially all of our operations are conducted through our Chinese operating subsidiaries, Semiconductor Manufacturing International (Shanghai) Corporation, or SMIC Shanghai, Semiconductor Manufacturing International (Beijing) Corporation, or SMIC Beijing, and Semiconductor Manufacturing International (Tianjin) Corporation. The ability of these subsidiaries to distribute dividends and other payments to us may be restricted by factors that include changes in applicable foreign exchange and other laws and regulations. In particular, under Chinese law, these operating subsidiaries may only pay dividends after 10% of their net profit has been set aside as reserve funds, unless such reserves have reached at least 50% of their respective registered capital. In addition, the profit available for distribution from our Chinese operating subsidiaries is determined in accordance with generally accepted accounting principles in China. This calculation may differ from the one performed in accordance with U.S. GAAP. As a result, we may not have sufficient distributions from our Chinese subsidiaries to enable necessary profit distributions to us or any distributions to our shareholders in the future, which calculation would be based upon our financial statements prepared under U.S. GAAP.

Distributions by our Chinese subsidiaries to us may be subject to governmental approval and taxation. Any transfer of funds from our company to our Chinese subsidiaries, either as a shareholder loan or as an increase in registered capital, is subject to registration or approval of Chinese governmental authorities, including the relevant administration of foreign exchange and/or the relevant examining and approval authority. In addition, it is not permitted under Chinese law for our Chinese subsidiaries to directly lend money to each other. Therefore, it is difficult to change our capital expenditure plans once the relevant funds have been remitted from our company to our Chinese subsidiaries. These limitations on the free flow of funds between us and our Chinese subsidiaries could restrict our ability to act in response to changing market conditions and reallocate funds from one Chinese subsidiary to another in a timely manner.

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Risks Related to Ownership of Our Shares and ADSs and Our Trading Markets

Future sales of securities by us or our shareholders may decrease the value of your investment.

Future sales by us or our existing shareholders of substantial amounts of our ordinary shares or ADSs in the public markets could adversely affect market prices prevailing from time to time.

We cannot predict the effect, if any, of any such future sales or of the perception that any such future sales will occur, on the market price for our ordinary shares or ADSs.

Holders of our ADSs will not have the same voting rights as the holders of our shares and may not receive voting materials in time to be able to exercise their right to vote.

Holders of our ADSs may not be able to exercise voting rights attaching to the shares evidenced by our ADSs on an individual basis. Holders of our ADSs have appointed the depositary or its nominee as their representative to exercise the voting rights attaching to the shares represented by the ADSs. You may not receive voting materials in time to instruct the depositary to vote, and it is possible that you, or persons who hold their ADSs through brokers, dealers or other third parties, will not have the opportunity to exercise a right to vote.

You may not be able to participate in rights offerings and may experience dilution of your holdings as a result.

We may from time to time distribute rights to our shareholders, including rights to acquire our securities. Under the deposit agreement for the ADSs, the depositary will not offer those rights to ADS holders unless both the rights and the underlying securities to be distributed to ADS holders are either registered under the Securities Act or exempt from registration under the Securities Act with respect to all holders of ADSs. We are under no obligation to file a registration statement with respect to any such rights or underlying securities or to endeavor to cause such a registration statement to be declared effective. In addition, we may not be able to take advantage of any exemptions from registration under the Securities Act. Accordingly, holders of our ADSs may be unable to participate in our rights offerings and may experience dilution in their holdings as a result.

The laws of the Cayman Islands and China may not provide our shareholders with benefits provided to shareholders of corporations incorporated in the United States.

Our corporate affairs are governed by our memorandum and articles of association, by the Companies Law (Revised) and the common law of the Cayman Islands. The rights of shareholders to take action against our directors, actions by minority shareholders and the fiduciary responsibilities of our directors to us under Cayman Islands law are to a large extent governed by the common law of the Cayman Islands. The common law in the Cayman Islands is derived in part from comparatively limited judicial precedent in the Cayman Islands and from English common law, the decisions of whose courts are of persuasive authority but are not binding on a court in the Cayman Islands. The rights of our shareholders and the fiduciary responsibilities of our directors under Cayman Islands law are not as clearly established as they would be under statutes or judicial precedents in the United States. In particular, the Cayman Islands have a less developed body of securities laws as compared to the United States. Therefore, our public shareholders may have more difficulty protecting their interests in the face of actions by our management, directors or controlling shareholders than would shareholders of a corporation incorporated in a jurisdiction in the United States. In addition, Cayman Islands companies may not have standing to initiate a shareholder derivative action before the federal courts of the United States.

It may be difficult for you to enforce any judgment obtained in the United States against our company, which may limit the remedies otherwise available to our shareholders.

Substantially all of our assets are located outside the United States. Almost all of our current operations are conducted in China. Moreover, a number of our directors and officers are nationals or residents of countries other than the United States. All or a substantial portion of the assets of these persons are located outside the United States. As a result, it may be difficult for you to effect service of process within the United States upon these persons. In addition, there is uncertainty as to whether the courts of the Cayman Islands or China would recognize or enforce judgments of United States courts obtained against us or such persons predicated upon the civil liability provisions of the securities law of the United States or any state thereof, or be competent to hear original actions brought in the Cayman Islands or China, respectively, against us or such persons predicated upon the securities laws of the United States or any state thereof. See Item 4 Information on the Company Business Overview Enforceability of Civil Liabilities.

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Item 4. Information on the Company

History and Development of the Company

We were established as an exempted company under the laws of the Cayman Islands on April 3, 2000. Our legal name is Semiconductor Manufacturing International Corporation. Our principal place of business is 18 Zhangjiang Road, Pudong New Area, Shanghai, China 201203, telephone number: (86) 21-3861-0000. Our registered office is located at PO Box 309, Ugland House, Grand Cayman, KY1-1104, Cayman Islands. Since our global offering, we have been listed on the New York Stock Exchange under the symbol SMI and the Stock Exchange of Hong Kong under the stock code 0981.

We were founded by Dr. Richard Ru Gin Chang, our Chief Executive Officer and President, who has more than 29 years of experience in the semiconductor industry. In August 2000, we started construction of the first fab in our Shanghai mega-fab. The first fab in the Shanghai mega-fab commenced pilot production in September 2001. That fab and the portion of our second fab in our Shanghai mega-fab which provides aluminum interconnects, commenced commercial production in January 2002. The portion of this second fab which provides copper interconnects and a third fab in our Shanghai mega-fab commenced commercial production in January 2003. All the fabs comprising the Shanghai mega-fab are located in the Zhangjiang High-Tech Park. In January 2004, we completed the acquisition of an 8-inch wafer fab located in the Xiqing Economic Development Area in Tianjin, China, and commenced mass production in May 2004. We commenced construction of our Beijing mega-fab in the Beijing Economic and Technological Development Area in December 2002. The Beijing mega-fab consists of three twelve-inch fabs and commenced commercial production in March 2005. The Beijing mega-fab is China s first 12-inch fab. In January 2008, the Company announced its plan to start a new IC production project in Shenzhen with extensive support from the Shenzhen municipal government. The project broke ground in the first half of 2008.

We have entered into an agreement with Toppan Printing Co., Ltd., to establish Toppan SMIC Electronics (Shanghai) Co., Ltd., to manufacture color filters and micro-lenses for CMOS image sensors and a joint venture agreement with United Test and Assembly Center Ltd. to provide assembly and testing services in Chengdu focusing on memory and logic devices. We have also entered into agreements to manage the operations of wafer manufacturing facilities in Chengdu and Wuhan, China. We maintain customer service and marketing offices in Japan, Europe, and the United States and a representative office in Hong Kong.

The foundry industry requires a significant amount of capital expenditures in order to construct, equip, and ramp up fabs. We incurred capital expenditures of US$912 million, US$860 million, and US$666 million in 2006, 2007 and 2008, respectively, for these purposes. We anticipate that in 2009, we will incur approximately US$190 million of capital expenditures to be adjusted based on market conditions, principally to expand our operations at our mega-fabs in Shanghai and Beijing and fab in Tianjin and new fab in Shenzhen. If our operating cash flows are insufficient, we plan to fund the expected shortfall through bank loans. If necessary, we will also explore other forms of external financing.

Our fabs had an aggregate capacity, as of December 31, 2008, of 160,500 8-inch wafer equivalents per month for wafer fabrication. We anticipate a slight increase to aggregate capacity by the end of 2009 subject to market conditions.

For additional information, see Item 5 Operating and Financial Review and Prospects Factors that Impact Our Results of Operations Substantial Capital Expenditures and Capacity Expansion.

Business Overview

We are one of the leading semiconductor foundries in the world. We operate three 8-inch wafer fabrication facilities in our Shanghai mega-fab located in the Zhangjiang High-Tech Park in Shanghai, China, an 8-inch wafer fab in Tianjin, China and a 12-inch wafer fab in our Beijing mega-fab located in the Beijing Economic and Technological Development Area in Beijing, China. These fabs had an aggregate capacity as of December 31, 2008 of 160,500 8-inch wafer equivalents per month for wafer fabrication which positions us as the leading foundry in China. In addition, we have a 12-inch fab in Shanghai currently engaged primarily in research and development activities, and a 8-inch fab under construction in Shenzhen. We have also entered into agreements to manage the operations of wafer manufacturing facilities in Chengdu and Wuhan, China. We also operate a fab at our Shanghai site which produces solar cells and modules. Due to the unique nature of solar cells and modules, this fab is not considered a part of our

Shanghai mega-fab.

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We currently provide semiconductor fabrication services using 0.35 micron to 65 nanometer process technology for the following devices:

- logic technologies, including standard logic, mixed-signal, RF and high voltage circuits;
- memory technologies, including DRAM, SRAM, Flash, and EEPROM; and
- specialty technologies, including LCoS, and CIS.

During the first quarter of 2008, the Company reached an agreement with our customers to completely exit the commodity DRAM business. The conversion of DRAM capacity into logic production was completed on schedule in the fourth quarter. As a result, our Beijing 300mm logic capacity has placed us in a better position to serve our global and China customers. In connection with the decision to exit the commodity DRAM business, we recorded an impairment loss of $105.8 million on long-lived assets during the first quarter of 2008.

In addition to wafer fabrication, our service offerings include a comprehensive portfolio of intellectual property consisting of libraries and circuit design blocks, design support, mask-making, wafer probing, gold/solder bumping and redistribution layer manufacturing. We also work with our partners to provide assembly and testing services. We have a global and diversified customer base that includes some of the world s leading IDMs and fabless semiconductor companies.

Our Industry

The Semiconductor Industry

Since the invention of the first semiconductor transistor in 1947, integrated circuits have become critical components in an increasingly broad range of electronics applications, including personal computers, wired and wireless communications equipment, televisions, consumer electronics and automotive and industrial control applications. Advancements in semiconductor design techniques and process technologies have allowed for the mass production of increasingly smaller and more powerful semiconductor devices at lower costs. This has resulted in the availability and proliferation of more complex integrated circuits with higher functionality. These integrated circuits may now each contain up to millions of transistors.

The key raw material for a semiconductor foundry is a raw wafer, which is a circular silicon plate. Raw wafers are available in different diameters (e.g., 5-inch, 6-inch, 8-inch or 12-inch) to meet the capabilities of different equipment. A fab capable of manufacturing integrated circuits on an 8-inch raw wafer is commonly described as an 8-inch fab. A raw wafer with a larger diameter has a greater surface area and consequently yields a greater number of integrated circuit dies. One method that foundries attempt to use to maintain their competitiveness is to increase the diameter of the wafers they use in manufacturing, such as the recent trend toward developing 12-inch wafers, each of which has approximately 2.25 times the number of gross dies achievable on an 8-inch wafer. In addition, since 12-inch fabs have been constructed more recently, the equipment used in these fabs permits smaller line-width process technologies to be utilized. However, this equipment is more expensive than equipment for the fabrication of 8-inch wafers as the market for this equipment is less mature with fewer suppliers and the technology involved is more complex.

Process technologies are the set of specifications and parameters implemented for manufacturing the circuitry on integrated circuits. The transistor circuitry on an integrated circuit typically follows lines that are less than one micron wide (1/1,000,000 of a meter). The line-widths of the circuitry, or the minimum physical dimensions of the transistor gate of integrated circuits in production, is used as a general rule for classifying generations of process technology of integrated circuits. Progress in the advancement of the integrated circuit has been driven by the scaling, or downsizing, of its components, primarily the transistors. By systematically shrinking the size of the transistors, the number of allowable transistors per die increases, and thus the number of dies on a given wafer, has also increased. Our current process technology ranges from 0.35 micron to 45-nanometer.

Importance of Integrated Circuits for China s Domestic Market and China s Emergence as a Global Electronics Manufacturing Center

China has emerged as a global manufacturing center for electronic products that are sold both within China and abroad. In recent years, numerous international companies have established facilities in China for the manufacture of a variety of electronic products, including household appliances, computers, mobile phones, telecommunications

equipment, digital consumer products and products with industrial applications. An increasing number of electronic systems manufacturers are relocating production facilities from the United States, Taiwan, and Southeast Asia to China. China is establishing itself as a favorable manufacturing location due to its well educated labor force, significantly lower costs of operations, large domestic market for semiconductors and cultural similarities and geographical proximity to Japan, Hong Kong, Taiwan, Singapore and Korea, among other factors. Such production growth represents additional potential demand for semiconductors manufactured in China.

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Increasing Importance of the Semiconductor Foundry Industry

As the cost of establishing new fabrication capacity has continued to rise, foundries have progressed from simply providing manufacturing capacity to becoming key strategic partners offering research and development capabilities and manufacturing process technologies. There have historically been a limited number of semiconductor foundries in the industry due to the high barriers to entry, which include significant capital commitments, scarcity of qualified engineers and advanced intellectual property and technology requirements. Many IDMs have begun outsourcing their fabrication requirements for complex and high performance semiconductor devices to foundries in order to supplement their own internal capacities and become more cost competitive. In addition, fabless semiconductor companies have shifted from relying on the excess fabrication capacity of IDMs to utilizing independent foundries to meet the majority of their wafer production needs.

Our Fabs

The table below sets forth a summary of our current fabs:

	Shanghai Mega-Fab	**Beijing Mega-Fab**	**Tianjin**
Number and Type of fab	(3) 8-inch fabs (1) 12-inch fab in R&D phase	(2) 12-inch fabs	(1) 8-inch fab
Pilot production commencement	September 2001	July 2004	February 2004
Commercial production commencement	January 2002	March 2005	May 2004
Wafer size	8-inch 12-inch (being equipped)	12-inch	8-inch
Production clean room size	34,610 m^2	23,876 m^2	8,463 m^2

In addition to our Shanghai mega-fab, we have two additional fabs at our Shanghai site. A portion of one facility in Shanghai is being leased to Toppan SMIC Electronics (Shanghai) Co., Ltd., which manufactures color filters and micro-lenses for CMOS image sensors. The other fab in Shanghai manufactures solar cells and modules. Most of the administrative and management functions of our fabs in different locations are centralized at our corporate headquarters in the Zhangjiang High-Tech Park in the Pudong New Area of Shanghai.

Additionally, we have one 8-inch fab under construction in Shenzhen. The expansion plan for this project will be adjusted based on overall market conditions.

Management of Fabs

We also have undertaken agreements relating to wafer manufacturing facilities in Chengdu and Wuhan, China. Under these agreements, we do not own any equity interest but will manage the operations of the facilities.

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Our Services

Wafer Fabrication Services

We currently provide semiconductor fabrication services using 0.35 micron to 65 nanometer technology for the following devices:

- logic technologies, including standard logic, mixed-signal, RF and high voltage circuits;
- memory technologies, including DRAM, SRAM, Flash, EEPROM and Mask ROM; and
- specialty technologies, including LCoS, and CIS.

These semiconductors are used in various computing, communications, consumer and industrial applications, such as computers, mobile telephones, digital televisions, digital cameras, DVD players, entertainment devices, other consumer electronics devices and automotive and industrial applications.

Our Technologies

We manufacture the following types of semiconductors:

Logic Semiconductors. Logic semiconductors process digital data to control the operation of electronic systems. The largest segment of the logic market, standard logic devices, includes microprocessors, microcontrollers, DSPs and graphic chips. Logic semiconductors are used in communications devices, computers and consumer products, with the most advanced logic semiconductors dedicated primarily to computing applications.

Mixed-Signal and RF. Analog/digital semiconductors combine analog and digital devices on a single semiconductor to process both analog signals and digital data. We make 0.35 micron to 0.13 micron mixed-signal and RF semiconductors using the CMOS process. The primary uses of mixed-signal semiconductors are in hard disk drives, wireless communications equipment and network communications equipment, while RF semiconductors are primarily used in communications devices, such as cell phones.

High Voltage. High voltage semiconductors are semiconductor devices that can drive high voltage electricity to systems that require voltage of between five volts to several hundred volts. Our high voltage technologies provide solutions for display driver integrated circuits, power supplies, power management, telecommunications, automotive electronics and industrial controls.

Memory Semiconductors. Memory semiconductors, which are used in electronic systems to store data and program instructions, are generally classified as either volatile memory, which lose their data content when power supplies are switched off, or non-volatile memory, which retain their data content without the need for a constant power supply. Examples of volatile memory include SRAM and DRAM, and examples of non-volatile memory include electrically erasable programmable read-only memory, or EEPROM, NAND Flash and OTP. Memory semiconductors are used in communications devices, computers and many consumer products.

Specialty Semiconductors.

LCoS. LCoS microdisplays are tiny, high resolution, low power displays designed for high definition televisions, projectors and other products that use or rely on displays. Compared with other display technologies, such as liquid crystal and plasma, LCoS displays have higher resolution and higher fill factor, resulting in superior images, colors and performance. LCoS process technology represents an enhancement of mixed-signal CMOS process technology with the addition of a highly reflective mirror layer.

CIS. CIS devices are sensors that are used in a wide range of camera-related systems, such as digital cameras, digital video cameras, handset cameras, personal computer cameras and surveillance cameras, which integrate image-capturing capabilities onto a chip. CIS is rapidly becoming a cost-effective and low power replacement for competing charged-coupled devices, or CCDs. Since CIS devices are fabricated with CMOS technology, they are easier to produce and more cost-effective than CCDs. By combining camera functions on a chip, from the capture of photos to the output of digital bits, CMOS image sensors reduce the parts required for a digital camera system, which in turn enhances reliability, facilitates miniaturization, and enables on-chip programming. Our CIS process is based on our CIS array technology.

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We are one of the leading foundries in the world in terms of the process technologies that we are capable of using in the manufacturing of semiconductors.

Fab	Month and year of commencement of commercial production of initial fab	Process technology (in microns) 2006	2007	2008	2009
Wafer fabrication:					
Shanghai Mega-fab (8)	January 2002	0.35/0.25/ 0.18/0.15/ 0.13/0.11/0.09	0.35/0.25/ 0.18/0.15/ 0.13/0.11/0.09	0.35/0.25/ 0.18/0.15/ 0.13/0.11/0.09	0.35/0.25/ 0.18/0.15/ 0.13/0.11/0.09
Shanghai fab (12)				0.09	0.11/0.09/0.065
Beijing Mega-fab (12)	March 2005	0.15/0.13/0.11/ 0.10/0.09	0.13/0.11/ 0.10/0.09	0.18/0.13/ 0.09	0.18/0.13/0.09/0.065
Tianjin fab (8)	May 2004	0.35/0.25/ 0.18/0.15	0.35/0.25/ 0.18/0.15	0.35/0.25/ 0.18/0.15	0.35/0.25 0.18/0.15

The following table sets forth a percentage breakdown of wafer sales by process technology for the years ended December 31, 2006, 2007, and 2008 and each of the quarters in the year ended December 31, 2008:

Process Technologies	For the year ended December 31, 2006	2007	For the three months ended March 31, 2008	June 30, 2008	September 30, 2008	December 31, 2008	For the year ended December 31, 2008
			(based on sales in US$)				
0.13 micron and below	49.60%	53.10%	44.70%	41.30%	44.50%	45.50%	43.90%
0.15 micron	5.70%	2.90%	4.30%	2.10%	2.00%	2.20%	2.70%
0.18 micron	35.70%	30.50%	32.10%	37.70%	33.90%	32.50%	34.10%
0.25 micron	2.00%	0.70%	0.50%	0.60%	0.50%	0.60%	0.60%
0.35 micron	7.00%	12.80%	18.40%	18.30%	19.10%	19.20%	18.70%
Total	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%

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Manufacturing Capacity

We currently manufacture 8-inch silicon wafers based on proprietary designs provided by our customers or third party designers. Since commencing commercial production, we have the largest 8-inch wafer fabrication capacity among the semiconductor foundries in China. We have the most advanced process technology among foundries in China. In January 2003, we commenced commercial production using 0.13 micron copper interconnects process technology. We are currently one of the few fabs in China to offer 0.13 micron copper interconnects process technology and both 90 nanometer and 65 nanometer wafer fabrication process technology.

The following table sets forth the historical capacity of our wafer fabrication and copper interconnects fabs as December 31, 2008:

Fab	**2006**	**2007**	**2008**
Wafer Fabrication:			
Wafer fabrication capacity as of year-end[(1)]:			
Shanghai mega-fab	106,000	98,000	88,000
Beijing mega-fab	56,250	65,250	40,500
Tianjin fab	20,000	22,000	32,000
Total monthly wafer fabrication capacity as of year-end[(1)]	182,250[(3)]	185,250[(3)]	160,500[(3)]
Wafer fabrication capacity utilization	90%	91%	86%

All output and capacity data is provided as 8-inch wafers or 8-inch wafer equivalents per month.

(1) Conversion of 12-inch wafers to 8-inch wafer equivalents is achieved by multiplying the number of 12-inch wafers by 2.25.

(2) Reflects wafers fabricated using the copper interconnects line and does not include wafers fabricated using

the aluminum interconnects line. As a small number of wafers produced by our aluminum interconnects lines also utilize the copper interconnects capabilities, our reported capacity and output data for our copper interconnects line overlaps to a limited extent with such data for our aluminum interconnects line.

(3) Mega fab structure includes copper interconnects in the total monthly capacity.

As of December 31, 2008, our aggregate wafer fabrication capacity was 160,500 8-inch wafer equivalents per month for wafer fabrication.

A key factor influencing our profit margins is our capacity utilization. Because a high percentage of our cost of sales is of a fixed nature, operations at or near full capacity have a significant positive effect on output and profitability. In 2005 our wafer fabs had an average annual utilization rate of 89%, in 2006, our wafer fabs had an average annual utilization rate of 90%, and in 2007, our wafer fabs had an average annual utilization rate of 91%. In 2008 our wafer fabs had an average utilization of 86%. Factors affecting utilization rates are the overall industry conditions, the level of customer orders, the complexity of the wafers and of the mix of wafers produced, mechanical failures and other operational disruptions such as the expansion of capacity or the relocation of equipment, and our ability to manage the production facilities and product flows efficiently. In addition, we have manufactured DRAM to fill our production lines when the volume demand of other products does not fully utilize our available capacity. As a result, our utilization rate has historically remained high.

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We determine the capacity of a fab based on the capacity ratings given by manufacturers of the equipment used in the fab, adjusted for, among other factors, actual output during uninterrupted trial runs, expected down time due to setup for production runs and approximately one to two days of scheduled annual maintenance, and expected product mix. Because these factors include subjective elements, our measurement of capacity utilization rates may not be comparable to those of our competitors. All of our fabs currently operate 24 hours per day, seven days per week, except during periods of annual maintenance. Employees in our fabs work shifts of 12 hours each day on a two-days-on, two-days-off basis.

We have often used DRAM as the initial product to test the production capabilities at a new fab. This is because DRAM requires higher process accuracy, more precise process control and a higher degree of engineering skills and operational disciplines, and can therefore assist in early identification of any potential process, equipment or fab-related production problems. This DRAM is either manufactured on a foundry basis for our customers or sold by us to the market through our distributors under technology licensing and royalty arrangements. However, the market for DRAM devices has also been more volatile and susceptible to sudden price drops in recent years. We expect that our production of DRAM wafers as a percentage of our overall production will decrease. During the first quarter of 2008, the Company reached an agreement with our customers to completely exit the commodity DRAM business. The conversion of DRAM capacity into logic production was completed on schedule in the fourth quarter of 2008. As a result, our Beijing 300mm logic capacity has placed us in a better position to serve our global and China customers. In connection with the decision to exit the commodity DRAM business, we recorded an impairment loss of $105.8 million on long-lived assets during the first quarter of 2008.

Capacity Expansion Plans

We intend to maintain our strategy of expanding capacity and improving our process technology to meet both the capacity requirements and the technological needs of our customers. Our capital expenditures in 2007 were approximately US$860 million and our capital expenditures in 2008 were approximately US$666 million. We currently expect that our capital expenditures in 2009 will be approximately US$190 million to be adjusted based on market conditions, which we plan to fund through our operating cash flows and bank loans. If necessary, we will also explore other forms of external financing. We plan to use this capital primarily to expand our operations at our mega-fabs in Shanghai and Beijing. In addition, our actual expenditures may exceed our planned expenditures for a variety of reasons, including changes in our business plan, our process technology, market conditions, equipment prices, or customer requirements. We will monitor the global economy, the semiconductor industry, the demands of our customers, and our cash flow from operations to adjust our capital expenditure plans.

We also will seek to participate in strategic partnerships to meet the demands of our customers. For example, in July 2004, we entered into an agreement with Toppan Printing Co., Ltd., to establish Toppan SMIC Electronics (Shanghai) Co., Ltd., a joint venture in Shanghai, for the manufacture of color filters and micro-lenses for CMOS image sensors. These products are increasingly being used in consumer products such as mobile phone cameras, digital cameras and automobile and home security applications. Toppan SMIC Electronics (Shanghai) Co., Ltd. commenced production in December 2005. We hold a 30% equity interest in Toppan SMIC Electronics (Shanghai) Co., Ltd.

Our Integrated Solutions

In addition to wafer fabrication, we provide our customers with a range of complementary services, from circuit design support and mask-making to wafer level probing and testing. This range of services is supported by our network of partners that assist in providing design, probing, final testing, packaging, assembly and distribution services.

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The diagram below sets forth our service model and our key points of interaction with our customers:

(1) A portion of this work is outsourced to our service partners.

(2) A portion of these services are outsourced to our service partners.

Design Support Services

Our design support services include providing our customers with access to the fundamental technology files and intellectual property libraries that facilitate customers own integrated circuit design. We also offer design reference flows and access to our design center alliance, as well as layout services. In addition, we collaborate with industry leaders in electronic design automation, library and intellectual property services to create a worldwide network of expertise, resources and services that are available to implement and produce a customer s designs. As of December 31, 2008, we employed over 200 engineers devoted solely to design support services.

Libraries

As part of the necessary building blocks for our customers semiconductor designs, we offer libraries of compatible designs for portions of semiconductors, such as standard cells, I/O and selected memory blocks, in addition to technology files. We have a dedicated team of engineers who work with our research and development department to develop, license or acquire from third parties selected key libraries early on in the development of new process technologies so that our customers can quickly design sophisticated integrated circuits that utilize the new process technologies. We also have arrangements with other providers of libraries to provide our customers with access to a broad library portfolio for their designs. In particular, we offer a portfolio of ASIC library and design kits for a wide range of tested and verified circuit applications and design-flow implementation. These include standard cell, I/O and memory compilers in 0.35 micron, 0.25 micron, 0.18 micron, 0.15 micron, 0.13 micron, 90 nanometer, and 65 nanometer process technologies. They have been developed primarily through our third party alliances, as well as by our internal research and development team, to facilitate easy design reuse and fast integration into the overall design system. We are currently developing additional libraries. Our library partners include ARM, Synopsys, Inc., VeriSilicon, and Virage Logic.

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Intellectual Property

Together with the intellectual property developed by our internal design team, our alliances with intellectual property providers enable us to offer foundational designs ranging from 0.35 micron to 65 nanometer and relating to mixed-signal, embedded memory, high-speed interface, digital peripheral device controllers, and embedded processors, among others. We use our own and third party design expertise to realize the functions of these various types of intellectual property. Our intellectual property partners include ARM, MIPS, Virage, Synopsys, and Verisilicon.

Design Reference Flows

Customers implementing designs on our processes can utilize our design reference flows. These flows have been created using design tools developed by our electronic design automation partners, including Cadence Design Systems, Inc., Magma Design Automation, Inc., Mentor Graphics Corporation, and Synopsys, Inc. They include training guides and sample test cases to provide a step-by-step explanation on how the hierarchical design flow works.

Design Center Alliance

If a customer requires assistance in designing its semiconductors, we are able to recommend design partners from among our extensive design services network. This network consists of design companies that we have successfully worked with in the past. In addition, we are also able to offer our own internal design team members to help our clients to complete their designs.

Mask-making Services

Many of our foundry customers utilize our mask-making services.

While most of our mask-making services are for customers that also utilize our wafer fabrication services as part of our overall foundry service, we also produce masks for other domestic and overseas fabs as a separate revenue-generating service. Our mask shop also cooperates with our research and development department to develop new technologies and designs.

Our mask-making facility, which is located in Shanghai, includes a 3,750 square meters clean room with up to class I specifications. At present, our mask shop offers both five-inch by five-inch, six-inch by six-inch, and seven-inch round reticles. Our facility is capable of producing binary masks, optical proximity correction masks and phase shift masks. Our mask facility also offers mask repair services. As of December 31, 2008, we had 183 personnel employed in our mask shop.

We also offer a multi-project wafer service that allows the cost of manufacturing one mask set to be shared among several customers. See Customers and Markets for more details regarding this service.

Intellectual property protection is a key focus of our mask-making services. See Intellectual Property for more details regarding the intellectual property protection measures we have instituted in our mask facility.

Wafer Probing, Assembly and Testing Services

We have our own probing facilities in Shanghai and Beijing that provide test program development, probe card fabrication, wafer probing, failure analysis, and failure testing. We also outsource these services to our partners for those customers that request them.

Our probing facility in Shanghai occupies a clean room space of 3,000 square meters, and our probing facility in Beijing occupies a clean room space of 1,400 square meters. Both facilities are rated at class 1,000 cleanliness and are equipped with advanced testers, probers and laser repair machines for logic, memory, and mixed-signal products. The probing facility in Beijing supports testing of Beijing s 12-inch wafers and Tianjin s 8-inch wafers. We employ more than 200 personnel to provide these probing services. We have testing equipment for memory, logic and mixed signal applications, including some equipment that has been consigned to our Shanghai facility by our customers. This consigned testing equipment has been specially designed and built by our customers in order to probe their particular products at our facility.

Our facility with United Test and Assembly Center Ltd. is located in Chengdu, China and provides both assembly and testing services for 8-inch and 12-inch wafers. This facility focuses on memory and discrete devices. Our facility in Chengdu occupies a total area of 215,000 square meters. Construction area is 40,668 square meters, including approximately 11,000 square meters of clean room area. We have also established a network of partners that provide additional probing services, as well as assembly and testing services, for our customers that request these additional

services. We have relationships with assembly and testing partners, including Amkor Assembly & Test (Shanghai) Co., Ltd. and ST Assembly Test Services Ltd., which have helped to enhance the range of services that we are able to offer our customers.

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Customers and Markets

Our customers include IDMs, fabless semiconductor companies and systems companies. The following table sets forth the breakdown of our sales by customer type for 2006, 2007 and 2008:

	For the year ended December 31,					
	2006		2007		2008	
Customer Type	Sales	Percentage	Sales	Percentage	Sales	Percentage
	(in US$ thousands, except percentages)					
Fabless semiconductor companies	601,200	41.00%	720,416	46.50%	768,707	56.80%
Integrated device manufacturers	737,275	50.30%	634,607	40.90%	341,933	25.30%
Systems companies and others	126,848	8.70%	194,742	12.60%	243,072	17.90%
Total	1,465,323	100.00%	1,549,765	100.00%	1,353,711	100.00%

We categorize our sales geographically based on the headquarter of customer operations and is not related to shipment destination. The following table sets forth the geographical distribution of our sales and percentage of sales for 2006, 2007 and 2008:

	For the year ended December 31,					
	2006		2007		2008	
Region	Sales	Percentage	Sales	Percentage	Sales	Percentage
	(in US$ thousands, except percentages)					
United States	602,506	41.10%	657,603	42.40%	766,708	56.70%
Europe	440,328	30.00%	328,710	21.20%	92,573	6.80%
Asia Pacific (excluding Japan and Taiwan)(1)	168,608	11.50%	227,973	14.70%	269,611	19.90%
Taiwan	153,058	10.50%	183,114	11.80%	185,849	13.70%
Japan	100,823	6.90%	152,365	9.90%	38,970	2.90%
Total	$ 1,465,323	100.00%	$ 1,549,765	100.00%	1,353,711	100.00%

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We have a global and diversified customer base that includes IDMs. Although we are not dependent on any single customer, a significant portion of our sales is attributable to a relatively small number of our customers. Our sales could be significantly reduced if any of these customers cancels or reduces its orders, significantly changes its product delivery schedule or demands lower prices.

Our President and Chief Executive Officer, Richard Ru Gin Chang, and his wife together hold shareholding interests of less than 0.1% in one of our five largest customers in 2006, 2007 and 2008, Texas Instruments.

During the first quarter of 2008, the Company reached an agreement with our customers to completely exit the commodity DRAM business. The conversion of DRAM capacity into logic production was completed on schedule in the fourth quarter. As a result, our Beijing 300mm logic capacity has placed us in a better position to serve our global and China customers. In connection with the decision to exit the commodity DRAM business, we recorded an impairment loss of $105.8 million on long-lived assets during the first quarter of 2008.

The following table sets forth a breakdown of our sales by application type for 2006, 2007 and 2008:

	For the year ended December 31,					
	2006		2007		2008	
Application Type[(1)]	**Sales**	**Percentage**	**Sales**	**Percentage**	**Sales**	**Percentage**
	(in US$ thousands, except percentages)					
Computing	498,135	34.00%	402,262	26.00%	106,184	7.80%
Communications	618,911	42.20%	695,645	44.90%	696,399	51.50%
Consumer	280,873	19.20%	323,230	20.90%	430,282	31.80%
Others	67,404	4.60%	128,628	8.20%	120,846	8.90%
Total	$ 1,465,323	100.00%	$ 1,549,765	100.00%	1,353,711	100.00%

(1) Computing consists of integrated circuits such as hard disk drive controllers, DVD-ROM/CD-ROM driver integrated circuits, graphic processors and other components that are commonly used in personal digital assistants and desktop and notebook computers and peripherals.
Communications consists of integrated circuits used in digital subscriber lines, digital signal processors, wireless LAN, LAN controllers, LCD

drivers, handset components and caller ID devices. Consumer consists of integrated circuits used for DVD players, game consoles, digital cameras, smart cards and toys.

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The following table sets forth a breakdown of our sales by service type for 2006, 2007 and 2008:

	For the year ended December 31,					
	2006		2007		2008	
Service Type	Sales	Percentage	Sales	Percentage	Sales	Percentage
	(in US$ thousands, except percentages)					
Fabrication of memory wafers	476,970	32.60%	428,355	27.60%	71,935	5.30%
Fabrication of logic wafers[1]	923,411	63.00%	985,776	63.60%	1,139,535	84.20%
Other[2]	64,942	4.40%	135,634	8.80%	142,241	10.50%
Total	$ 1,465,323	100.00%	$ 1,549,765	100.00%	1,353,711	100.00%

(1) Includes copper interconnects and memory devices whose manufacturing process is similar to that for a logic device.

(2) Includes mask-making and probing, etc.

We have customer service and marketing offices located in California, Milan, Shanghai, and Tokyo and a representative office in Hong Kong. Our Shanghai office serves China and other non-Japan Asian markets, our California office serves the North American market, and our Milan and Tokyo offices serve the European and Japanese markets, respectively. We also sell some products through sales agents in selected markets.

We also provide our customers with the ability to share costs through our multi-project wafer processing shuttle service. This service allows customers to share costs with other customers by processing multiple designs on a single mask set.

We provide our customers with 24-hour online access to necessary information to conduct business with us. From our technical capabilities to a customer s order status, we provide an online solution for our customers. From wafer fabrication, wafer sorting and assembly to final testing and shipping, our data center electronically transfers data, work-in-progress tracking, yield/cycle-time reports, and quality/engineering data to customers.

Our sales cycle, meaning the time between our first contact with a customer in relation to a particular product and our first shipment of that product to the customer, typically lasts between three months to one year, depending on the type of process and product technology involved in the product we are requested to fabricate. Because of the fast-changing technology and functionality in integrated circuit design, foundry customers generally do not place purchase orders far in advance to fabricate a particular type of product. However, we engage in discussions with customers commencing in advance of the placement of purchase orders regarding customers expected fabrication requirements. See Risk Factors Risks Related to Our Financial Condition and Business Our sales cycles can be long, which could adversely

affect our operating results and cause our income stream to be unpredictable.

See Item 5 Operating and Financial Review and Prospects Sales for a description of the seasonality of our business.

Research and Development

Our research and development activities are principally directed toward the development and implementation of more advanced and lower cost process technology. We spent US$94.2 million in 2006, US$97.0 million in 2007, and US$102.2 million in 2008 on research and development expenses, which represented 6.4%, 6.3%, and 7.6% respectively, of our sales in those respective years. Our research and development costs are partially offset by related government subsidies and include non-recurring engineering costs associated with the ramp-up of a new wafer facility. We plan to continue to invest significant amounts in research and development in 2009 for our 65 and 45 nanometer manufacturing process.

The research and development efforts were focused primarily on our logic and system-on-chip (SOC) business. 2008 marked many milestones for SMIC. Early on in the year, Synopsis and SMIC released an enhanced 90-nanometer hierarchical, multi-voltage RTL-to-GDSII reference design flow that will benefit advanced synthesis with built-in capability of design-for-test and design-for-manufacturing. In April, working with a leading China domestic fabless, we developed a 90 nanometer digital photo frame chip, which is one of the most integrated multimedia SOC in the market. For advanced CMOS logic, the Company demonstrated a silicon success in our 45-nanometer process ahead of schedule, and also added new intellectual properties in 65 nanometer and 90 nanometer technology services. In addition, the Company successfully developed a 0.11 micron CMOS image sensor (CIS) process technology, one of the most advanced process technologies for CIS currently available in the industry. In Non-Volatile Memory (NVM) technology, the 0.13um ETox went into production in early 2008 and 90nm ETox is currently in risk production now. Our research and development in Micro-Electromechanical System (MEMS) areas also advanced to risk production for the 1st customer in 2008. Other areas of phase-change memory, HV, mix-signal-signal, and RF technologies were also successfully advanced for smaller size, less power, and lower cost to meet customer demands.

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We employ over 800 research and development personnel. This research and development team includes many experienced semiconductor engineers with advanced degrees from leading universities around the world, as well as top graduates from the leading universities in China. We believe this combination has enabled us to quickly bring our technology in line with the semiconductor industry technology roadmap and ensures that we will have skilled personnel to lead our technology advancement in the future.

Intellectual Property

While we continue to develop and patent our own technologies, we expect to have an ongoing need to obtain licenses for the proprietary technologies of third parties to enable us to manufacture certain advanced wafers for our customers. As of 2008 year-end, we have been granted five hundred fifty seven patents, and have more than one thousand nine hundred ninety three patent applications pending worldwide. We believe our competitors and other industry participants have numerous patents concerning wafer fabrication and related technologies in multiple countries.

We implement a variety of measures to protect the intellectual property and related interests of our company, customers and technology partners. We require our employees to execute a confidential information and invention assignment agreement relating to non-competition and intellectual property protection issues prior to commencing their employment at our company. Access to customer information is granted to employees strictly on a need-to-know basis both during and after mask tooling.

We have applied for trademarks relating to our corporate logo, English trade name SMIC , and Chinese trade name in the United States, China, Hong Kong and Taiwan. We have been granted registration of trademarks for our corporate logo in China, English trade name in China and Taiwan, and Chinese trade name in Hong Kong, United States and China (except a dispute in China for certain applied product/service category). There can be no assurance that other trademarks registration will be granted.

Competition

We compete internationally and domestically with dedicated foundry service providers, as well as with semiconductor companies that allocate a portion of their fabrication capacity to foundry operations. While the principal elements of competition in the wafer foundry market include technical competence, production speed and cycle time, time-to-market, research and development quality, available capacity, yields, customer service and price, we seek to compete on the basis of process technology capabilities, performance, quality and service, rather than solely on price. The level of competition differs according to the process technology involved.

Our competitors and potential competitors include other pure-play foundries such as TSMC, UMC and Chartered Semiconductor. TSMC has commenced commercial production at its fab in China, and UMC has established a relationship with a fab in commercial production in China. Another group of potential competitors consists of IDMs that have established their own foundry capabilities. These include Fujitsu Limited, IBM, Samsung Electronics Co., Ltd. and Toshiba. IDMs are primarily dedicated to fabricating integrated circuits for the end products of their respective affiliates. See Risk Factors Risks Related to Our Financial Condition and Business If we cannot compete successfully in our industry, particularly in China, our results of operations and financial condition will be adversely affected.

Quality and Reliability

We have implemented quality assurance measures relating to material quality control, monitoring of our in-line processes and wafer-level reliability control at every stage of our operations from technology development to production. By combining advanced quality assurance procedures and e-commerce technology, we monitor all processes, services and materials in our mask-making, wafer fabrication and probing facilities. These quality assurance measures include inspection of incoming materials, supplier and subcontractor management, manufacturing environmental control and monitoring, in-line defect monitoring, engineering change control, calibration monitoring, chemical analysis and visual inspection. Quality assurance measures also include on-going process and product reliability monitors and failure tracking for early identification of production problems.

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We incorporate reliability control in our entire production process and have adopted a system that enables us to track and record wafer-, package- and product-level reliability data throughout the development, qualification and production stages of the relevant process or device. This data enables us to identify problems at an early stage and provide an immediate diagnosis and solution, so as to further reduce our failure rate.

We achieved ISO 9001:2000 certification from the British Standards Institute with zero-defect performance for our Fab 1 in July 2002 and for our Fab 2 and Fab 3B in March 2003. The ISO 9001 quality standards were established by the International Standards Organization, an organization formed by delegates from member countries to establish international quality assurance standards for products and manufacturing processes. International Standards Organization certification is required in connection with sales of industrial products in many countries. To further enhance our quality management system, we obtained TS 16949:2002 certification from the British Standards Institute (BSI) in February 2004. This is an International Standards Organization quality management certification that relates to automobile applications and primarily measures a device s ability to handle extreme changes in temperature. In January 2005, we obtained TL9000 Quality Management System certification from BSI. This is a management certification relating to the telecommunications industry and evaluates research and development, production and installation and maintenance of communication product and services.

Raw Materials

Our fabrication processes uses many raw materials, primarily silicon wafers, chemicals, gases, and various types of precious and other metals. Raw material costs constituted 18.3% of our manufacturing costs in 2006, 21% of our manufacturing costs in 2007 and 19% of our manufacturing costs in 2008.

The three largest components of raw material costs raw wafers, chemicals and gases accounted for approximately 43%, 21% and 11%, respectively, of our raw material costs in 2006, approximately 47%, 20%, and 10%, respectively, of our raw material costs in 2007, and approximately 40%, 20%, and 9%, respectively, of our raw materials in 2008. Most of our raw materials generally are available from several suppliers, but substantially all of our principal materials requirements must currently be sourced from outside China.

The most important raw material used in our production is silicon in the form of raw wafers. In 2008, we purchased approximately 68.0% of our overall raw wafer requirements from our three major raw wafer suppliers. The prices of our principal raw material are not considered to be volatile.

For 2008, our largest and five largest raw materials suppliers accounted for approximately 8.0% and 32.3%, respectively, of our overall raw materials purchases. For 2007, our largest and five largest raw materials suppliers accounted for approximately 14.0% and 48.2%, respectively, of our overall raw materials purchases. For 2006, our largest and five largest raw materials suppliers accounted for approximately 14.7% and 46.1%, respectively, of our overall raw materials purchases. Having made all reasonable inquiry, we are not aware of any director or shareholder (which to the knowledge of our directors own more than 5% of our issued share capital) or their respective associates, which had shareholding interests in any of our five largest suppliers. Most of our materials are imported free of value-added tax and import duties due to concessions granted to our industry in China.

Electricity and Water

We use substantial amounts of electricity in our manufacturing process. This electricity is sourced from the Pudong Electricity Corporation (for Shanghai), the Beijing Municipal Electricity Department, the Tianjin Municipal Electricity Department, the PiXian Municipal Electricity Department (for Chengdu), and the Shenzhen PanGuShi Municipal Electricity Department. We maintain Uninterrupted Power Supply (UPS) systems and emergency back-up generators to power life safety and critical equipment and systems for emergencies.

The semiconductor manufacturing process uses extensive amounts of fresh water. We source our fresh water for our Shanghai mega-fab from Pudong Vivendi Water Corporation Limited, for our Beijing mega-fab from Beijing Waterworks Group Co. Ltd., for our Tianjin fab from the Tianjin Municipal Water Department, for our Chengdu facility from the Xipu Water Corporation, Ltd., and for our Shenzhen facility from Grand Industrial Zone Water Company of Shenzhen. Because Beijing and Tianjin are subject to potential water shortages in the summer, our fabs in Beijing and Tianjin are equipped with back-up reservoirs. We have taken steps to reduce fresh water consumption in our fabs and capture rainwater for use at our Beijing facilities, and our water recycling systems in each of our fabs allow us to recycle 40% to 70% of the water used during the manufacturing process. The Beijing site is also equipped

to use recycled/treated industrial waste water from the Beijing Economic and Technological Development Area for non-critical operations.

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Regulation

Integrated circuit industry in China is subject to substantial regulation by the Chinese government. This section sets forth a summary of the most significant Chinese regulations that affect our business in China.

Scope of Regulation

The *Several Policies to Encourage the Development of Software and Integrated Circuit Industry*, or the Integrated Circuit Policies, promulgated by the State Council of The People s Republic of China on June 24, 2000, together with other ancillary laws and regulations, regulates integrated circuit production enterprises, or ICPEs. The State Council issued the Integrated Circuit Policies in order to encourage the development of the software and integrated circuits industry in China. The Integrated Circuit Policies form the basis for a series of laws and regulations that set out in detail the preferential policies relating to ICPEs. Such laws and regulations include:

the *Notice of the Ministry of Finance, the State Administration of Taxation and the General Administration of Customs on Relevant Taxation Policy Encouraging the Further Development of the Software Industry and the Integrated Circuit Industry,* or the Integrated Circuit Notice, jointly issued by the Ministry of Finance, the State Administration of Taxation and the General Administration of Customs on September 22, 2000, as amended by the *Notice of the Ministry of Finance and the State Administration of Taxation on Approval Procedure Concerning Foreign Invested Enterprises Implementing Enterprise Income Tax Policies of the Software and Integrated Circuit Industry*, or the Approval Notice, jointly issued by the Ministry of Finance and the State Administration of Taxation on July 1, 2005;

the *Notice of the Ministry of Finance, the State Administration of Taxation on Taxation Policies Concerning the Tax Policies for Further Encouraging the Development of the Software and the Integrated Circuit Industry*, or the Further Development Taxation Notice, jointly issued by the Ministry of Finance and the State Administration of Taxation on October 10, 2002, as amended by *Notice of the Ministry of Finance, the State Administration of Taxation on Termination of Value-added Tax Refund Policies for Integrated Circuits*, or the Termination Notice, jointly issued by the Ministry of Finance and the State Administration of Taxation on October 25, 2004;

the *Notice of the Ministry of Finance on Taxation Policies Concerning the Import of Self-used Raw Materials and Consumables by Part of Integrated Circuit Production Enterprises*, or the Raw Materials Taxation Notice, issued by the Ministry of Finance on August 24, 2002;

the *Notice on Taxation Policies Concerning the Import of Construction Materials Specially used for Clean Rooms by Part of the Integrated Circuit Production Enterprises*, or the Construction Materials Taxation Notice, issued by the Ministry of Finance on September 26, 2002;

the *Notice by the Ministry of Finance and the State Administration of Taxation on Increasing Tax Refund Rate for Export of Certain Information Technology(IT) Products*, or the Export Notice, issued by the Ministry of Finance and the State Administration of Taxation on December 10, 2004;

the *Measures for the Accreditation of the Integrated Circuit Enterprise Encouraged by the State (For Trial Implementation)*, or the Accreditation Measures, jointly issued by the National Development and Reform Commission, the Ministry of Information Industry, the State Administration of Taxation and the General Administration of Customs on October 21, 2005; and

the *Interim Measures for the Management of the Special Fund for the Research and Development of the Integrated Circuit Industry,* or the Fund Measures, jointly issued by the Ministry of Finance, the Ministry of Information Industry and the National Development and Reform Commission on March 23, 2005.

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Preferential Industrial Policies Relating to ICPEs

ICPEs which are duly accredited in accordance with relevant laws and regulations may qualify for preferential industrial policies. Under the Integrated Circuit Policies, accreditation of ICPEs is determined by the competent examination and approval authorities responsible for integrated circuit projects after consultation with relevant taxation authorities. Under the Accreditation Measures, an integrated circuit enterprise refers to an independent legal entity duly established in the PRC (except for Hong Kong, Macao, and Taiwan) engaging in the fabrication, package, or testing of integrated circuit chips and the production of mono-crystalline silicon of six inches or above, excluding the integrated circuit design enterprise. The accreditation of ICPEs is included in the accreditation of the integrated circuit enterprises. Such accreditation is determined by the competent authorities consisting of the National Development and Reform Commission, the Ministry of Information Industry, the State Administration of Taxation and the General Administration of Customs, which jointly designate the China Semiconductor Industrial Association as the accreditation institution. Any enterprise qualified under the requirements set forth in the Accreditation Measures is entitled to apply to the China Semiconductor Association for the Accreditation of the ICPEs. The accreditation of ICPEs is annually reviewed. If the enterprise fails to apply for the annual review in time, it shall be deemed as giving up such accreditation and if the enterprise fails in the annual review, the accreditation will also be canceled.

SMIC Shanghai, SMIC Beijing, and SMIC Tianjin have been accredited as ICPEs and are entitled to the preferential industrial policies described below.

Encouragement of Domestic Investment in ICPEs

Pursuant to the *Interim Provisions on Promoting Industrial Structure Adjustment*, or the Interim Provisions, issued by the State Council on December 2, 2005, and the *Catalogue for the Guidance of Industrial Structure Adjustment*, or the Guidance Catalogue, which is the basis and criteria for implementing the Interim Provisions, issued by the National Development and Reform Commission and all the State Council Institutions on December 2, 2005, the Chinese government encourages (i) the design and fabrication of large scale integrated circuits with a line width of less than 1.2 micron, (ii) the fabrication of the equipment of large scale integrated circuit and (iii) the fabrication of mixed integrated circuits. Under the Interim Provisions, imported equipment that is used for a qualifying domestic investment project and that falls within such project s approved total investment amount is exempt from custom duties and import-linked value-added tax, except for such equipment listed in the *Catalogue of Import Commodities for Domestic Investment Projects Not Entitled to Tax Exemptions*, as stipulated by the State Council and amended in 2006.

Encouragement of Foreign Investment in ICPEs

Pursuant to the Integrated Circuit Policies and the *Guideline Catalogue of Foreign Investment Industries* promulgated jointly by the State Development and Reform Commission and the Ministry of Commerce on October 11, 2007, the following foreign investment categories are encouraged:

design of integrated circuits;

fabrication of large scale integrated circuits with a line width of less than 0.18 micron (including 0.18 micron);

fabrication of analog and analog digital integrated circuits with a line width of less than 0.8 micron (including 0.8 micron);

advanced packaging and testing of BGA, PGA, CSP, MCM;

fabrication of mixed integrated circuits.

Foreign investment in such encouraged projects may enjoy preferential treatment as stipulated by the laws and regulations.

Preferential Taxation Policies

Preferential Value-added Tax Policy

Under Article 1 of the Further Development Taxation Notice (October 10, 2002 No. 70 [2002] Cai-Shui), from January 1, 2002 to the end of 2010, the sale of integrated circuits (including monocrystalline silicon chips) is subject to a value-added tax levy of 17%. After the value-added tax is levied, the taxpayer is to be entitled to a refund for the portion exceeding 3% of the actual value-added tax burden. The tax refund was required to be used by the enterprise for the research and development of integrated circuits and to increase production.

Under the Termination Notice (No. 174 [2004] of the Ministry of Finance), as of April 1, 2005, implementation of Article 1 of the Further Development Taxation Notice was terminated.

Under the Export Notice (No. 200 [2004] Cai-Shui), as of November 1, 2004, the tax refund rate for exports of electronic integrated circuits and micro-assemblies is to increase from 13% to 17%.

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Preferential Enterprise Income Tax Policies

Under Article 42 of the Integrated Circuit Policies (No. 18 [2000] Guo-Fa),Article 2(3) of the Integrated Circuit (Notice No. 25 [2000] Cai-Shui*)* and Article 1 of the Notice by the Ministry of Finance and the State Administration of Taxation on Several Preferential Policies for Income Tax (No. 1 [2000] Cai-Shui*)*, ICPEs whose total investment exceeds Rmb 8,000 million (approximately US$967 million) or whose integrated circuits have a line-width of less than 0.25 micron are entitled to preferential tax treatment similar to that granted for foreign investment in the energy and communications industries. SMIC Shanghai, SMIC Beijing and SMIC Tianjin are entitled to a full exemption from FEIT for five years starting with the first year of positive accumulated earnings and a 50% reduction for the following five years or five year exemption and five year reduction .

From January 1, 2002 to the end of 2010, investors in ICPEs and integrated circuit packaging enterprises that reinvest their after-income-tax profits from ICPEs for the purpose of increasing the registered capital in the ICPEs, or to establish other ICPEs and integrated circuit packaging enterprises for a period of operation of not less than five years, are entitled to a refund of 40% of the total amount of enterprise income tax paid on the reinvested portion. If the investment is withdrawn before the period of operation reaches five years, the amount of enterprise income tax refunded shall be repaid. From January 1, 2002 to the end of 2010, domestic or foreign investors that reinvest their after income-tax profits from sources within China in order to establish ICPEs or integrated circuit package enterprises in China s western regions for a period of operation of not less than five years are entitled to a refund of 80% of total amount of enterprise income tax paid on the reinvested portion. If the investment is withdrawn before the period of operation reaches five years, the amount of enterprise income tax refunded shall be repaid.

On March 16, 2007, the National People s Congress, the PRC legislature, approved and promulgated a new tax law named Enterprise Income Tax Law, On December 6, 2007, the PRC State Council issued the Implementation Regulations of the Enterprise Income Tax Law, both of which became effective on January 1, 2008.The Enterprise Income Tax Law and its Implementation Regulations, or the new EIT law, FIEs and domestic companies are subject to a uniform tax rate of 25%. The new EIT law eliminates or modifies most of the tax exemptions, reductions and preferential treatments available under the previous tax laws and regulations. The State Council issued the Notice of the State Council on the Implementation of the Transitional Preferential Policies in respect of Enterprise Income Tax on December 26, 2007, enterprises that were established before March 16, 2007 and already enjoy preferential tax treatments will (i) in the case of preferential tax rates, continue to enjoy the tax rates which will be gradually increased to the new tax rates within five years from January 1, 2008 or (ii) in the case of preferential tax exemption or reduction for a specified term, continue to enjoy the preferential tax holiday until the expiration of such term. Thus, SMIC Shanghai, SMIC Beijing and SMIC Tianjin could fall into condition (ii) and may be entitled to the five year exemption and five year reduction as subject to the final recognition by the PRC tax authorities. While the new EIT Law equalizes the tax rates for FIEs and domestic companies, preferential tax treatment would continue to be given to companies in certain encouraged sectors and to entities classified as high and new technology enterprises supported by the PRC government, whether FIEs or domestic enterprises. According to the new EIT Law, entities that qualify as high and new technology enterprises especially supported by the PRC government are expected to benefit from a tax rate of 15% as compared to the uniform tax rate of 25%. Implementation Regulations of the Enterprise Income Tax Law, a high and new technology enterprise shall have core self-owned intellectual properties and its products shall be within the scope provided by the high-technology field highly supported by the State .

Under the new EIT law, dividends, interests, rent, royalties and gains on transfers of property payable by a foreign-invested enterprise in the PRC to its foreign investor who is a non-resident enterprise will be subject to a 10% withholding tax, unless such non-resident enterprise s jurisdiction of incorporation has a tax treaty with the PRC that provides for a reduced rate of withholding tax. The Cayman Islands, where SMIC is incorporated, does not have such a tax treaty with the PRC. If SMIC is considered a non-resident enterprise, this new 10% withholding tax imposed on SMIC s dividend income received from SMIC Shanghai, SMIC Beijing and SMIC Tianjin would reduce its net income and have an adverse effect on its operating results.

Under the new EIT law, an enterprise established outside the PRC with its de facto management body within the PRC is considered a resident enterprise and will be subject to the enterprise income tax at the rate of 25% on its worldwide income. The de facto management body is defined as the organizational body that effectively exercises overall

management and control over production and business operations, personnel, finance and accounting, and properties of the enterprise. It remains unclear how the PRC tax authorities will interpret such a broad definition. Substantially the majority of management members of SMIC are based in the PRC. If the PRC tax authorities subsequently determine that SMIC should be classified as a resident enterprise, then SMIC s worldwide income will be subject to income tax at a uniform rate of 25%, which may have a material adverse effect on SMIC s financial condition and results of operations. Notwithstanding the foregoing provision, the new EIT law also provides that, if a resident enterprise directly invests in another resident enterprise, the dividends received by the investing resident enterprise from the invested enterprise are exempted from income tax, subject to certain conditions. Therefore, if SMIC is classified as a resident enterprise, the dividends received from our PRC subsidiary may be exempted from income tax and the dividends paid to our non-PRC shareholders and gains derived by our non-PRC shareholders from transferring our shares or ADSs may be subject to 10% withholding tax. However, it remains unclear how the PRC tax authorities will interpret the PRC tax resident treatment of an offshore company, like SMIC, having indirect ownership interests in PRC enterprises through intermediary holding vehicles.

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Exemption of Customs Duties and Import-related Value-added Tax

Under the Integrated Circuit Policies (No. 18 [2000] Guo-Fa) and the Integrated Circuit Notice (No. 25 [2000] Cai-Shui), ICPEs whose total investment exceeds Rmb 8,000 million or whose integrated circuits have a line-width of less than 0.25 micron are exempt from customs duties and import-related value-added tax for the raw materials and consumables used for production purposes.

Under the Integrated Circuit Notice, integrated circuit technology, production equipment, and equipment and instruments specialized for use in fabricating integrated circuits that are imported by a duly accredited ICPE are, with the exception of commodities listed in the *Catalogue of Imported Commodities for Foreign Investment Projects Not Entitled to Tax Exemptions* and the *Catalogue of Imported Commodities for Domestic Investment Projects Not Entitled to Tax Exemptions* as stipulated by the Ministry of Finance and all the State Council Institutions and Departments and amended in 2006, exempt from customs duties and import-related value-added tax.

Under the Construction Materials Taxation Notice (No. 152 [2002] Cai-Shui), commencing January 1, 2001, the importation of construction materials, auxiliary equipment and spare parts for the production of integrated circuits, specifically for clean rooms (as listed in the annex to the Construction Materials Taxation Notice), by ICPEs whose total investment exceeds Rmb 8,000 million or whose integrated circuits have a linewidth of less than 0.25 micron is exempt from customs duties and import-related value-added tax.

Preferential Policies Encouraging Research and Development

The new Corporate Income Tax (CIT) has provided tax incentives in relation to technologies as a means to encourage advancement and adoption of technologies. Among these incentives is the 50% additional tax deduction of the research and development (R&D) expenses (generally known as R&D Super-Deduction). In December 2008, the State Administration of Taxation (SAT) issued a circular, Guoshuifa [2008] No.116 (Circular 116) with retrospective effective date from 1 January 2008, to provide the implementation rules for the R&D Super-Deduction. An enterprise is allowed to claim an additonal deduction of 50% of R&D expenses incurred for the development of new technologies, new products and new craftsmanship. If the R&D expenses result in an intangible asset, the enterprise is allowed to amortized the intangible asset based on 150% of the the capitalized R&D costs.

Legal Framework Concerning the Protection of Intellectual Property Relating to Integrated Circuits

China has formulated various laws and regulations on intellectual property protection in respect of integrated circuits including:

- the *Patent Law of the People s Republic of China*, adopted at the fourth meeting of the Standing Committee of the Sixth National People s Congress on March 12, 1984, effective April 1, 1985 and amended by the Ninth National People s Congress on August 25, 2000;

- the *Paris Convention for the Protection of Industrial Property* of the World Intellectual Property Organization, in which China became a member state as of March 19, 1985;

- the *General Principles of the Civil Law of the People s Republic of China* adopted at the fourth session of the Sixth National People s Congress on April 12, 1986, effective January 1, 1987. In this legislation, intellectual property rights were defined in China s basic civil law for the first time as the civil rights of citizens and legal persons;

- the *Copyright Law of the People s Republic of China*, adopted by the 15th meeting of the Seventh National People s Congress Standing Committee on September 7, 1990, effective June 1, 1991 and amended by the Ninth National People s Congress on October 27, 2000;

- the *Regulations for the Protection of the Layout Design of Integrated Circuits*, or the Layout Design Regulations, adopted April 2, 2001 at the thirty-sixth session of the executive meeting of the State Council, effective October 1, 2001; and

the World Intellectual Property Organization s *Washington Treaty on Intellectual Property in Respect of Integrated Circuits*, for which China was among the first signatory states in 1990.

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Protection of the Layout Design of Integrated Circuits

Under the Layout Design Regulations, layout design of an integrated circuit refers to a three dimensional configuration in an integrated circuit that has two or more components, with at least one of these being an active component, and part or all of the interconnected circuitry or the three-dimensional configuration prepared for the production of integrated circuits.

Chinese natural persons, legal persons or other organizations that create layout designs are entitled to the proprietary rights in the layout designs in accordance with the Layout Design Regulations. Foreign persons or enterprises that create layout designs and have them first put into commercial use in China are entitled to the proprietary rights in the layout designs in accordance with the Layout Design Regulations. Foreign persons or enterprises that create layout designs and that are from a country that has signed agreements with China regarding the protection of layout designs, or is a party to an international treaty concerning the protection of layout designs to which China is also a party, are entitled to the proprietary rights of the layout designs in accordance with the Layout Design Regulations.

Proprietary Rights in Layout Design of Integrated Circuits

Holders of proprietary rights in a layout design are entitled to the following proprietary rights:

to duplicate the whole protected layout design or any part of the design that is original; and

to make commercial use of the protected layout design, the integrated circuit containing the layout design, or commodities containing the integrated circuit.

Proprietary rights in layout designs become valid after being registered with the administrative department of the State Council responsible for intellectual property. Unregistered layout designs are not protected by the Layout Design Regulations.

The protection period of the proprietary rights in a layout design is ten years, commencing from the date of the application for registration of the layout design or the date that it is put into commercial use anywhere in the world, whichever is earlier. However, regardless of whether or not a layout design is registered, or whether or not it is put into commercial use, it is not protected after 15 years from the time of its creation.

Registration of a Layout Design

The administrative departments of the State Council responsible for intellectual property are responsible for the registration of layout designs and accepting applications for the registration of layout designs. If an application for a layout design registration is not made with the administrative department of the State Council responsible for intellectual property within two years after it has been put into commercial use anywhere in the world, the administrative department of the State Council responsible for intellectual property will not register the application. A holder of proprietary rights in a layout design may transfer the proprietary rights or give permission for other parties to use the layout design.

Compulsory Licenses for Exploitation of Patents in Respect of Semiconductor Technology

Under the Patent Law and the Implementing Regulations of the Patent Law, after three years from the date of granting the patent rights, any person or enterprise that has made good faith reasonable proposals to the holder of proprietary rights seeking a license to those rights, but has been unable to obtain such license after an extended period of time, may request the administrative department responsible for patents under the State Council to grant a compulsory license for the relevant patent. However, where a compulsory license involves semiconductor technology, the implementation of a compulsory license is restricted to public and non-commercial uses, or to uses that counteract anti-competitive actions, as determined by judicial or administrative procedures.

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PRC Tax for Resident Enterprises

Under China s New EIT Law, we may be classified as a resident enterprise of China. This classification could result in unfavorable tax consequences to us and our non-PRC shareholders. The implementing rules of the New EIT Law define de facto management bodies as management bodies that exercises substantial and overall management and control over the production and operations, personnel, accounting, and properties of the enterprise. Currently no official interpretation or application of this new resident enterprise classification is available, therefore it is unclear how tax authorities will determine tax residency based on the facts of each case.

If the PRC tax authorities determine that our Cayman Islands holding company is a resident enterprise for PRC enterprise income tax purposes, a number of unfavorable PRC tax consequences could follow. First, we may be subject to enterprise income tax at a rate of 25% on our worldwide taxable income as well as PRC enterprise income tax reporting obligations. Second, although under the New EIT Law and its implementing rules dividends income between qualified resident enterprises is exempted income, it is not clear what is considered a qualified resident enterprise under the New EIT Law. Finally, it is possible that future guidance issued with respect to the new resident enterprise classification could result in a situation in which a 10% withholding tax is imposed on dividends we pay to our non-PRC shareholders and with respect to gains derived by our non-PRC shareholders from transferring our shares or ADSs. Similarly, these unfavorable consequences could apply to our other overseas intermediary holding companies if they are classified as a PRC resident enterprises.

Environmental Regulation

Our Chinese subsidiaries are subject to a variety of Chinese environmental laws and regulations promulgated by the central and local governments concerning examination and acceptance of environmental protection measures in construction projects, the use, discharge and disposal of toxic and hazardous materials, the discharge and disposal of waste water, solid waste, and waste gases, control of industrial noise and fire prevention. These laws and regulations set out detailed procedures that must be implemented throughout a project s construction and operation phases.

A key document that must be submitted for the approval of a project s construction is an environmental impact assessment report that is reviewed by the relevant environmental protection authorities. Upon completion of construction, and prior to commencement of operations, an additional examination and acceptance by the relevant environmental authority of such projects is also required. Within one month after receiving approval of the environmental impact assessment report, a semiconductor manufacturer is required to apply to and register with the competent environmental authority the types and quantities of liquid, solid and gaseous wastes it plans to discharge, the manner of discharge or disposal, as well as the level of industrial noise and other related factors. If the above wastes and noise are found by the authorities to have been managed within regulatory levels, renewable discharge registrations for the above wastes and noise are then issued for a specified period of time. SMIC Shanghai, SMIC Beijing, SMIC Tianjin, and SMIC Chengdu have all received approval with respect to their relevant environmental impact assessment reports and discharge registrations.

From time to time during the operation of our Chinese subsidiaries, and also prior to renewal of the necessary discharge registrations, the relevant environmental protection authority will monitor and audit the level of environmental protection compliance of these subsidiaries. Discharge of liquid, solid or gaseous waste over permitted levels may result in imposition of fines, imposition of a time period within which rectification must occur or even suspension of operations.

Enforceability Of Civil Liabilities

We are a Cayman Islands holding company. We are incorporated in the Cayman Islands because of the following benefits associated with being a Cayman Islands corporation:

- political and economic stability;
- an effective judicial system;
- a favorable tax system;
- the absence of exchange control or currency restrictions; and

the availability of professional and support services.

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However, the Cayman Islands have a less developed body of securities laws as compared to the United States and provides significantly less protection for investors. In addition, Cayman Islands companies may not have standing to sue before the federal courts of the United States. Substantially all of our assets are located outside the United States. In addition, most of our directors and officers are nationals and/or residents of countries other than the United States, and all or a substantial portion of our or such persons assets are located outside the United States. As a result, it may be difficult for a shareholder to effect service of process within the United States upon us or such persons or to enforce against them or against us, judgments obtained in United States courts, including judgments predicated upon the civil liability provisions of the securities laws of the United States or any state thereof.

Conyers Dill & Pearman, our counsel as to Cayman Islands law, Slaughter and May, our counsel as to Hong Kong law, and Fangda Partners, our counsel as to Chinese law, have advised us that there is uncertainty as to whether the courts of the Cayman Islands, Hong Kong and China, respectively, would:

- recognize or enforce judgments of United States courts obtained against us or our directors or officers predicated upon the civil liability provisions of the securities laws of the United States or any state thereof, or
- be competent to hear original actions brought in each respective jurisdiction, against us or our directors or officers predicated upon the securities laws of the United States or any state thereof.

Conyers Dill & Pearman has further advised us that a final and conclusive judgment in the federal or state courts of the United States under which a sum of money is payable, other than a sum payable in respect of taxes, fines, penalties or similar charges, may be subject to enforcement proceedings as a debt in the Courts of the Cayman Islands under the common law doctrine of obligation.

Organizational Structure

We operate primarily through three wholly owned subsidiaries in China. The chart below sets forth our significant operating subsidiaries or affiliates, including their jurisdictions of incorporation and principal activities:

Name of company	Place and date of incorporation/establishment	Attributable equity interest held	Principal Activity
Garrison Consultants Limited (Garrison)	Samoa April 3, 2000	100%	Consultancy services
Betterway Enterprises Limited (Better Way)	Samoa April 5, 2000	100%	Trading of semiconductor products
Semiconductor Manufacturing International (Shanghai) Corporation (SMIC Shanghai or SMIS)*#	PRC December 21, 2000	100%	Manufacturing and trading of semiconductor products
SMIC, Americas	United States of America June 22, 2001	100%	Marketing related activities
Semiconductor Manufacturing International (Beijing) Corporation (SMIC Beijing or SMIB)*#	PRC July 25, 2002	100%	Manufacturing and trading of semiconductor products
SMIC Japan Corporation*	Japan October 8, 2002	100%	Marketing related activities

SMIC Europe S.R.L.	Italy July 3, 2003	100%	Marketing related activities

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Name of company	Place and date of incorporation/establishment	Attributable equity interest held	Principal Activity
Semiconductor Manufacturing International (Tianjin) Corporation (SMIC Tianjin or SMIT)*#	PRC November 3, 2003	100%	Manufacturing and trading of semiconductor products
SMIC Commercial (Shanghai) Limited Company (formerly SMIC Consulting Corporation) *#	The PRC September 30, 2003	100%	Operation of a convenience store
Semiconductor Manufacturing International (AT) Corporation (AT)*	Cayman Islands July 26, 2004	57.3%	Investment holding
Semiconductor Manufacturing International (Chengdu) Corporation (SMIC Chengdu or SMICD) *#	The PRC December 28, 2004	57.3%	Manufacturing and trading of semiconductor products
Semiconductor Manufacturing International (Solar Cell) Corporation	Cayman Islands June 30, 2005	100%	Investment holding
SMIC Energy Technology (Shanghai) Corporation (Energy Science)*#	PRC September 9, 2005	100%	Manufacturing and trading of solar cells and modules
SMIC Development (Chengdu) Corporation*#	The PRC December 29, 2005	100%	Construction, operation, management of SMICD s living quarter, schools and supermarket
Magnificent Tower Limited	British Virgin Islands January 5, 2006	100%	Investment Holding
Semiconductor Manufacturing International (BVI) Corporation (SMIC (BVI))*	British Virgin Islands April 26, 2007	100%	Trading of semiconductor products
SMIC AT (HK) Company Limited (SMIC AT (HK))*	Hong Kong October 22, 2007	57.3%	Investment Holding
SMIC Solar Cell (HK) Company Limited (SMIC Solar Cell (HK))*	Hong Kong October 23, 2007	100%	Investment Holding
SMIC Shanghai (HK) Company Limited (SMIC SH (HK))*	Hong Kong November 1, 2007	100%	Investment Holding
		100%	Investment Holding

SMIC Beijing (HK) Company Limited (SMIC BJ (HK))*	Hong Kong November 2, 2007		
SMIC Tianjin (HK) Company Limited (SMIC TJ (HK))*	Hong Kong November 2, 2007	100%	Investment Holding
SMIC Shanghai (Cayman) Corporation (SMIC SH (Cayman))*	Cayman Islands November 8, 2007	100%	Investment Holding
SMIC Beijing (Cayman) Corporation (SMIC BJ (Cayman))*	Cayman Islands November 8, 2007	100%	Investment Holding

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Name of company	Place and date of incorporation/establishment	Attributable equity interest held	Principal Activity
SMIC Tianjin (Cayman) Corporation (SMIC TJ (Cayman))*	Cayman Islands November 8, 2007	100%	Investment Holding
SMIC (Wuhan) Development Corporation*#	PRC March 27, 2007	100%	Construction, operation, management of living quarter, schools
Admiral Investment Holdings Limited	British Virgin Islands October 10, 2007	100%	Investment Holding
SMIC Shenzhen (Cayman) Corporation	Cayman Islands January 21, 2008	100%	Investment Holding
SMIC Shenzhen (HK) Company Limited	Hong Kong January 29, 2008	100%	Investment Holding
SilTech Semiconductor Corporation	Cayman Islands February 13, 2008	100%	Investment Holding
SilTech Semiconductor (Hong Kong) Corporation Limited*	Hong Kong March 20, 2008	100%	Investment Holding
Semiconductor Manufacturing International (Shenzhen) Corporation*#	PRC March 20, 2008	100%	Manufacturing and trading of semiconductor products

Companies registered as wholly-owned foreign enterprises in the *People s Republic of China. (PRC), excluding for the purpose of this report, Hong Kong, Macau, and Taiwan.*

* For identification

purposes only.

Property, plant and equipment

Equipment

The quality and level of technology of the equipment used in the semiconductor fabrication process are important because they dictate the limits of the process technology that we use. Advances in process technology cannot be achieved without corresponding advances in equipment technology. The principal pieces of equipment used by us to fabricate semiconductors are scanners, cleaners and track equipment, inspection equipment, etchers, furnaces, wet stations, strippers, implanters, sputterers, CVD equipment, testers and probers. We source substantially all of our equipment from vendors located in the United States, Europe and Japan.

In implementing our capacity expansion and technology advancement plans, we expect to make significant purchases of equipment required for semiconductor fabrication. Some of the equipment is available from a limited number of vendors and/or is manufactured in relatively limited quantities, and in some cases has only recently become commercially available. Our ability to obtain certain kinds of equipment from outside of China may be subject to restrictions. See Risk Factors Risks Related to Conducting Operations in China Limits placed on exports into China could substantially harm our business and operating results.

We maintain our equipment through a combination of in-house maintenance and outside contracting to our equipment vendors. We decide whether to maintain ourselves, or subcontract the maintenance of, a particular piece of equipment based on a variety of factors, including cost, complexity and regularity of the required periodic maintenance and the availability of maintenance personnel in China. Most of our equipment vendors offer maintenance services through technicians based in China.

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Property

Our corporate headquarters and our mega-fab in Shanghai occupy 367,895 square meters of land, for which we hold valid land use rights certificates. These fabs currently occupy approximately 45% of this total land area. We also hold valid land use rights for the 240,140 square meters of land that comprise our Beijing site, approximately 75% of which will be occupied by the Beijing mega-fab. In 2005, we received land use rights certificates for 215,733 square meters of land in Tianjin, which is occupied by the Tianjin fab. We own all of the buildings and equipment for our fabs, except for certain customer-owned tooling provided to our Shanghai operations for test production on a consignment basis from our customers.

The following table sets forth the location, size and primary use of our real properties and whether such real properties are owned or leased.

Location	Size (Land/Building) (in square meters)	Primary Use	Owned[1] or Leased (Land/Building)
Zhangjiang High-Tech Park, Pudong New Area, Shanghai	367,895/164,795	Wafer fabrication	owned/owned
Beijing Economic and Technological Development Area	240,140/143,017	Wafer fabrication	owned/owned
Xiqing Economic Development Area, Tianjin	215,733/61,990	Wafer fabrication	owned/owned
Export Processing Zone (West Area), Chengdu	252,831/35,850	Assembly and Test	owned/owned
Japan	na/55	Marketing activities	na/leased
USA	na/743	Marketing activities	na/leased
Italy	na/280	Marketing activities	na/leased
Hong Kong[2]	na/300	Representative Office	na/owned

(1) With respect to land located in China, ownership refers to holding a valid land use rights certificate. All land within municipal zones in China is owned by the Chinese government. Limited liability companies, joint stock companies, foreign-invested enterprises, privately held companies and

individual natural persons must pay fees to be granted rights to use land within municipal zones. Legal use of land is evidenced and sanctioned by land use certificates issued by the local municipal administration of land resources. Land use rights granted for industrial purposes are limited to a term of no more than 50 years.

(2) In February 2006, we purchased approximately 300 square meter of property in Hong Kong through our indirect wholly-owned subsidiary, Magnificent Tower Limited, a company incorporated in the British Virgin Islands.

The construction of our 8-inch fab in Shenzhen began in 2008 in an effort to expand our production capacity and is expected to commence commercial production in 2010. We plan to gradually increase the capacity in the Shenzhen fab based on market conditions. This project will be financed through our operating cash flows as well as through external financing. See Risk Factors Risks Related to Our Financial Condition and Business Since our operating cash flows will not be sufficient to cover our planned capital expenditures, we will require additional external financing, which may not be available on acceptable terms or at all. Any failure to raise adequate funds in a timely manner could adversely affect our business and operating results, and Risk Factors Risks Related to Our Financial Condition and Business The construction and equipping of new fabs and the expansion of existing fabs are subject to certain risks that could result in delays or cost overruns, which could require us to expend additional capital and adversely affect our business and operating results.

Our right to continued use of the land is subject to our continued compliance with the land use agreement that each of our Chinese subsidiaries has executed. The Chinese government has reserved the right to revoke our land use rights for special eminent domain purposes, in which case the government will compensate us. In addition, pursuant to an amendment to its domestic bank loan agreements, SMIC Beijing and SMIC Tianjin have pledged a portion of its land use right to the lenders. See Item 5 Operating and Financial Review and Prospects Liquidity and Capital Resources. For a description concerning our capacity, capacity utilization rate and capacity expansion plans, please see Item 5-Operating and Financial Review and Prospects-Factors that Impact our Results of Operations.

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Risk Management and Insurance

Our safety management philosophy is based on incident prevention and frequent safety audits. Incident prevention is achieved through:

- mandatory staff and vendor safety training;
- compliance of equipment and facilities to safety criteria, including the Semiconductor Equipment and Materials International and Chinese National Fire Protection Association standards; and
- standard management procedures established by our environmental, health and safety committee.

Regularly scheduled safety audits are performed in accordance with established world standards, and we have been qualified under OHSAS 18001 internal auditing standards as of September 2003.

We have established a risk management committee and an emergency response center to respond to all emergencies. The facility monitoring and control system and security monitoring room located within our emergency response center are where all emergency responses begin. These rooms are equipped with 24-hour safety and security monitoring systems such as closed circuit television, gas monitoring systems, chemical dispensing systems, very early smoke detection apparatus, public announcement systems, and fire alarm systems.

Each department conducts emergency drills on a quarterly basis in accordance with our emergency response plan to address all possible emergency situations that could arise. These emergency scenarios include fires, gas leakages, chemical spills, and power losses.

We maintain insurance with respect to our facilities, equipment, and inventories. The insurance for the fabs and their equipment covers, subject to some limitations, various risks, including industrial accidents and natural disasters, generally up to their respective replacement values and loss due to business interruption. We have not made any significant claims under these insurance policies. Equipment and inventories in transit are also insured.

Environmental Matters

The semiconductor production process generates gaseous chemical wastes, liquid waste, waste water, and other industrial wastes in various stages of the fabrication process. We have installed various types of pollution control equipment for the treatment of gaseous chemical waste and liquid waste and equipment for the recycling of treated water in our fabs. Our operations are subject to regulation and periodic monitoring by PRC s State Environmental Protection Bureau, as well as local environmental protection authorities, including those under the Shanghai Pudong Municipal Government, the Beijing Municipal Government, the Tianjin Municipal Government, and the Chengdu Municipal Government, which may in some cases establish stricter standards than those imposed by the State Environmental Protection Bureau. The Chinese national and local environmental laws and regulations impose fees for the discharge of waste substances above prescribed levels, require the payment of fines for serious violations, and authorize the Chinese national and local governments to suspend any facility that fails to comply with orders requiring it to cease or remedy operations causing environmental damage. No such penalties have been imposed on us or any of our subsidiaries for violations of environmental pollution.

We believe our pollution control measures are effective, complying with the requirements applicable to the semiconductor industry in China and comparable to other countries. Waste generated from our operations, including acid waste, alkaline waste, flammable waste, toxic waste, oxidizing waste, and self-igniting waste, are collected and sorted for proper disposal. Furthermore, we have in many cases implemented waste reduction steps beyond the scope of current regulatory requirements. In addition, we continuously investigate methods to lower our energy consumption, including making existing processes more efficient and introducing green energy**.**

The ISO14001 standard is a voluntary standard and part of a comprehensive series of standards for environmental management published by the International Standards Organization. The ISO14001standard cover environmental management principles, systems and supporting techniques. Starting in August 2002, all operating fabs have since achieved ISO14001 certification.

Furthermore, by March of 2007, these fabs have been third-party certified to be compliant with the RoHS (Restriction of the use of certain Hazardous Substances in electrical and electronic equipment) Directive of the European Union, which bans the use of various chemicals determined to be harmful to the environment. Once the Shenzhen facility is

in operation, it too will undergo certification for ISO14001 and RoHS compliance.

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Item 4A. Unresolved Staff Comments

Not applicable.

Item 5. Operating and Financial Review and Prospects

Overview

We were founded in April 2000. In 2000 and 2001, our company was in its development stage and did not have any sales. During this period, we established our management structure, acquired land use rights, constructed, equipped and commenced the ramp-up of production at our 8-inch wafer facilities in Shanghai which are referred to as the Shanghai mega-fab, and began our research and development activities. The first fab in the Shanghai mega-fab and the portion of our second fab, commenced commercial production in January 2002. The remaining portion of our second fab and a third fab commenced commercial production in January 2003. In January 2004, we acquired an 8-inch fab in Tianjin, China, which we refer to as our Fab 7, from MCEL, a wholly owned subsidiary of Motorola. The first fab in the Beijing mega-fab commenced commercial production in March of 2005. As of December 31, 2008, we had reached total wafer fabrication capacity of 160,500 8-inch wafer equivalents per month. Our wafers shipped and sales increased from 1,614,888 wafers and US$1,465.3 million for 2006 to 1,849,957 wafers and US$1,549.8 million for 2007 and decreased to 1,611,208 wafers and US$1,353.7 million for 2008.

We manage our business and measure our results of operations based on a single operating segment. We anticipate a slight increase to aggregate capacity by the end of 2009 subject to market conditions. As we increase our capacity and corresponding wafer production, we benefit from economies of scale. When our capacity utilization is high, these economies of scale enable us to reduce our per wafer production cost and improve our margins. On the other hand, when our capacity utilization rate is low, our unused capacity results in higher per wafer production cost and decreased margins.

Factors that Impact Our Results of Operations

Cyclicality of the Semiconductor Industry

The semiconductor industry is highly cyclical due mainly to the cyclicality of demand in the markets of the products that use semiconductors. As these markets fluctuate, the semiconductor market also fluctuates. This fluctuation in the semiconductor market is exacerbated by the tendency of semiconductor companies, including foundries, to make capital investments in plant and equipment during periods of high demand since it may require several years to plan, construct and commence operations at a fab. Absent sustained growth in demand, this increase in capacity often leads to overcapacity in the semiconductor market, which in the past has led to a significant underutilization of capacity and a sharp drop in semiconductor prices. The semiconductor industry is generally slow to react to declines in demand due to its capital-intensive nature and the need to make commitments for equipment purchases well in advance of the planned expansion.

Substantial Capital Expenditures

The semiconductor foundry industry is characterized by substantial capital expenditures. This is particularly true for our company as we have recently constructed and equipped fabs and are continuing to construct and equip new fabs. In connection with the construction and ramp-up of our capacity since our inception, we incurred capital expenditures of US$912 million, US$860 million, and US$666 million in 2006, 2007, and 2008 respectively. We depreciate our manufacturing machinery and equipment on a straight-line basis over an estimated useful life of five to seven years. We recorded depreciation and amortization of US$919.6 million, US$706.3, and US$761.8 million in 2006, 2007, and 2008 respectively.

The semiconductor industry is also characterized by rapid changes in technology, frequently resulting in obsolescence of process technologies and products. As a result, our research and development efforts are essential to our overall success. We spent approximately US$94.2 million in 2006, US$97.0 million in 2007, and US$102.2 million in 2008 for research and development, which represented 6.4%, 6.3%, and 7.6% respectively, of our sales for 2006, 2007, and 2008. Our research and development costs are partially offset by related government subsidies and include non-recurring engineering costs associated with the ramp-up of a new wafer facility. In 2008, we continued to equip our new 12-inch fab at the Shanghai mega-fab.

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We currently expect that our capital expenditures in 2009 will be approximately US$190 million to be adjusted based on market conditions, which we plan to fund through our operating cash flows and bank loans in order to expand our operations. If necessary, we will also explore other forms of external financing. In addition, our actual expenditures may exceed our planned expenditures for a variety of reasons, including changes in our business plan, our process technology, market conditions, equipment prices, or customer requirements. We will monitor the global economy, the semiconductor industry, the demands of our customers, and our cash flow from operations to adjust our capital expenditure plans.

Capacity Expansion

We have expanded, and plan to continue to expand, our capacity through internal growth and acquisitions. An increase in capacity may have a significant effect on our results of operations, both by allowing us to produce and sell more wafers and achieve higher sales, and as a cost component in the form of acquisition costs and depreciation expenses. We anticipate a slight increase to aggregate capacity by the end of 2009 subject to market conditions.

Pricing

We price our foundry services on either a per wafer or a per die basis, taking into account the complexity of the technology, the prevailing market conditions, the order size, the cycle time, the strength and history of our relationship with the customer, and our capacity utilization. Since a majority of our costs and expenses are fixed or semi-fixed, fluctuations in the average selling prices of semiconductor wafers have historically had a substantial impact on our margins. The average selling price of the wafers we shipped increased 0.2% from US$838 per wafer in 2007 to US$840 per wafer in 2008.

The following table sets forth a percentage breakdown of wafer sales by process technology for the years ended December 31, 2006, 2007 and 2008 and each of the quarters in the year ended December 31, 2008:

	For the year ended December 31,		For the three months ended				For the year ended December 31,
Process Technologies	**2006**	**2007**	**March 31, 2008**	**June 30, 2008**	**September 30, 2008**	**December 31, 2008**	**2008**
				(based on sales in US$)			
0.13 micron and below	49.60%	53.10%	44.70%	41.30%	44.50%	45.50%	43.90%
0.15 micron	5.70%	2.90%	4.30%	2.10%	2.00%	2.20%	2.70%
0.18 micron	35.70%	30.50%	32.10%	37.70%	33.90%	32.50%	34.10%
0.25 micron	2.00%	0.70%	0.50%	0.60%	0.50%	0.60%	0.60%
0.35 micron	7.00%	12.80%	18.40%	18.30%	19.10%	19.20%	18.70%
Total	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%

Change in Process Mix and Technology Migration

Because the price of wafers processed with different technologies varies significantly, the mix of wafers that we produce is among the primary factors that affect our sales and profitability. The value of a wafer is determined principally by the complexity of the process technology used to fabricate the wafer. In addition, production of devices with higher levels of functionality and greater system-level integration requires more fabrication steps, and these devices generally sell for higher prices.

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Prices for wafers of a given level of technology generally decline over the relevant process technology life cycle. As a result, we and our competitors are continuously in the process of developing and acquiring advanced process technologies and migrating our customers to use such technologies to maintain or improve our profit margins. This technology migration requires continuous investment in research and development and technology-related acquisitions, and we expect to continue to spend a substantial amount of capital on upgrading our technologies.
Our initial sales after commencing commercial operations in 2002 consisted mainly of DRAM fabricated and sold on a foundry basis, as well as commodity-type DRAM fabricated using technology licensed from a third party and sold by us to distributors. This commodity-type DRAM was fabricated during our start-up phase in order to test and ramp up our facilities and train our personnel. As our business has grown and our fabs have matured, we have produced proportionately less commodity-type DRAM and more logic products and memory products utilizing more advanced technologies, which generally command a higher margin. During the first quarter of 2008, the Company reached an agreement with our customers to completely exit the commodity DRAM business. The conversion of DRAM capacity into logic production was completed on schedule in the fourth quarter. As a result, our Beijing 300mm logic capacity has placed us in a better position to serve our global and China customers. In connection with the decision to exit the commodity DRAM business, we recorded an impairment loss of $105.8 million on long-lived assets during the first quarter of 2008.
The following table sets forth a breakdown of our sales by service type for 2006, 2007 and 2008:

	For the year ended December 31,					
	2006		2007		2008	
Service Type	**Sales**	**Percentage**	**Sales**	**Percentage**	**Sales**	**Percentage**
	(in US$ thousands, except percentages)					
Fabrication of memory wafers	476,970	32.60%	428,355	27.60%	71,935	5.30%
Fabrication of logic wafers[(1)]	923,411	63.00%	985,776	63.60%	1,139,535	84.20%
Other[(2)]	64,942	4.40%	135,634	8.80%	142,241	10.50%
Total	$ 1,465,323	100.00%	$ 1,549,765	100.00%	1,353,711	100.00%

(1) Includes copper interconnects and memory devices whose manufacturing process is similar to that for a logic device.

(2) Includes mask-making and probing, etc.

Capacity Utilization Rates

Operations at or near full capacity have a significant positive effect on our profitability because a substantial percentage of our cost of sales is of a fixed nature. In 2006, 2007 and 2008, approximately 59%, 47%, and 46% respectively, of our cost of sales consisted of depreciation expenses, which are fixed costs. If we increase our utilization rates, the number of wafers we fabricate will increase, and therefore our average fixed costs per wafer will decrease. Therefore, our capacity utilization rates have a significant effect on our margins. Our utilization rates have varied from period to period due to capacity ramp-ups and fluctuations in customer orders. Our annual capacity utilization rate was 89.6% in 2006, 91.0% in 2007, and 86.0% in 2008. Factors affecting utilization rates are the overall industry conditions, the level of customer orders, the complexity of the wafers and of the mix of wafers produced, mechanical failures and other operational disruptions such as the expansion of capacity or the relocation of equipment, and our ability to manage the production facilities and product flows efficiently.

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Our capacity is determined by us based on the capacity ratings for each piece of equipment, as specified by the manufacturers of such equipment, adjusted for, among other factors, actual output during uninterrupted trial runs, expected down time due to set up for production runs and maintenance, and expected product mix. Because these factors include subjective elements, our measurement of capacity utilization rates may not be comparable to those of our competitors.

Yield Rates

Yield per wafer is the ratio of the number of functional dies on that wafer to the maximum number of dies that can be produced on that wafer. A significant portion of our services, particularly our memory semiconductor wafer fabrication services, is priced on a per die basis.

We continuously upgrade the process technologies that we use. At the beginning of each technology migration, the yield utilizing the new technology is generally lower, sometimes substantially lower, than the yield under the then-current technology. This is because it requires time to stabilize, optimize and test a new process technology. We do not ship wafers to a customer until we have achieved that customer s minimum yield requirements. Yield is generally improved through the expertise and cooperation of our research and development personnel, process engineers, and equipment suppliers.

Critical Accounting Policies

The methods, estimates and judgments we use in applying our accounting policies have a significant impact on the results we report in our financial statements. Some of our accounting policies require us to make difficult and subjective judgments, often as a result of the need to make estimates of matters that are inherently uncertain. Below we have summarized our accounting policies that we believe are both important to the portrayal of our financial results and involve the need to make estimates about the effect of matters that are inherently uncertain. We also have other policies that we consider to be key accounting policies. However, these policies do not meet the definition of critical accounting estimates because they do not generally require us to make estimates or judgments that are difficult or subjective.

Inventory

Inventories are stated at the lower of cost or market. Market represents the net realizable value for finished goods and work-in-progress. Inventory cost is determined using standard cost and an allocation of the cost variances arising in the period of production, which approximates actual costs determined on the weighted average basis. We determine the standard cost of each wafer based on estimates of the materials, labor, and other costs incurred in each process step associated with the manufacture of our products. We allocate labor and overhead costs to each step in the wafer production process based on normal fab capacity, with costs arising from abnormal under-utilization of capacity expensed when incurred. The unit cost of a wafer generally decreases as fixed overhead charges, such as depreciation expense on the facility and semiconductor equipment, are allocated over a larger number of units produced.

We estimate the net realizable value for such finished goods and work-in-progress based primarily upon the latest invoice prices and current market conditions. If the market value of a good drops below its carrying value, we record a write-off to cost of sales for the difference between the carrying cost and the market value. During the years ended December 31, 2006, 2007 and 2008, the Company recorded inventory write downs of US$16.1 million, US$22.7 million, and US$40.8 million, respectively, to reflect a decline in the estimated market value of the inventory we held. We carry out an inventory review at each quarter-end.

Depreciation and Amortization

We operate in a capital-intensive business. We periodically review and assess the estimated useful life of our assets based on expected use by the Company, taking into account effects of obsolescence, demand, and other economic factors. The net book value of our plant and equipment, including land use rights, at December 31, 2008 was US$3,038 million. Depreciation of manufacturing buildings and related improvements is provided on a straight-line basis over the estimated useful life of 25 years and commences from the date the facility is ready for its intended use. Depreciation of our manufacturing machinery and equipment, as well as our facility, machinery and equipment, is provided on a straight-line basis over the estimated useful life, commencing from the date that the equipment is placed into productive use. A 5 to 7 year useful life is used for manufacturing machinery and equipment while a 10 year useful life is used for facility, machinery and equipment. Amortization of land use rights is over the term of the land

use right agreement, which ranges from 50 to 70 years. Amortization of intangible assets is computed using the straight-line method over the expected useful life of the assets ranging from 3 to 10 years. The estimated useful life and dates that the equipment is placed into productive use reflects our estimate of the periods that we intend to derive future economic benefits from the use of our plant and equipment and land use rights.

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Long-lived Assets

The Company assesses the impairment of long-lived assets when events or changes in circumstances indicate that the carrying value of the assets or the asset group may not be recoverable. Factors that we consider in deciding when to perform an impairment review include, but are not limited to significant under-performance of a business or product line in relation to expectations, significant negative industry or economic trends, and significant changes or planned changes in our use of the assets. An impairment analysis is performed at the lowest level of identifiable independent cash flows for an asset or asset group. We make subjective judgments in determining the independent cash flows that can be related to specific asset group based on our asset usage model and manufacturing capabilities. We measure the recoverability of assets that will continue to be used in our operations by comparing the carrying value of the asset group to our estimate of the related total future undiscounted cash flows. If an asset group s carrying value is not recoverable through the related undiscounted cash flows, the impairment loss is measured by comparing the difference between the asset group s carrying value and its fair value, based on the best information available, including market prices or discounted cash flow analysis.

In order to remain technologically competitive in our industry, we have entered into technology transfer and technology license arrangements with third parties in an attempt to advance our process technologies. The payments made for such technology licenses are recorded as an intangible asset or as a deferred cost and amortized on a straight-line basis over the estimated useful life of the asset. We routinely review the remaining estimated useful lives of these intangible assets and deferred costs. We also evaluate these intangible assets and deferred costs for impairment whenever events or changes in circumstances indicate that their carrying amounts may not be recoverable. We have continued to construct, acquire, and expand our manufacturing facilities since our inception. We will continue to review impairment factors as described above and, as a result, impairment charges may be necessary in the future as circumstances change.

During the first quarter of 2008, the Company reached an agreement with our customers to completely exit the commodity DRAM business. The conversion of DRAM capacity into logic production was completed on schedule in the fourth quarter. As a result, our Beijing 300mm logic capacity has placed us in a better position to serve our global and China customers. In connection with the decision to exit the commodity DRAM business, we recorded an impairment loss of $105.8 million on long-lived assets during the first quarter of 2008.

As of March 31, 2008 the sensitivity of the fair values to an independent change of one point in the discount rate were as follows:

Reporting Unit	Excess of carrying value over estimated fair value (in millions)	Impact of one point change in the discount rate (in millions)	
		+1 point	-1 point
SMIB	-105.8	-129.2	-81.4

Revenue Recognition

We manufacture semiconductor wafers for our customers based on the customers designs and specifications pursuant to manufacturing agreements and purchase orders. We also sell certain semiconductor standard products to customers. Customers do not have any rights of return except pursuant to warranty provisions, which returns have been minimal. We typically perform tests of our products prior to shipment to identify yield of acceptable products per wafer. Occasionally, product tests performed after shipment identify yields below the level agreed with the customer. In those circumstances, the customer arrangement may provide for a reduction to the price paid or for its costs to ship replacement products. We estimate the amount of sales returns and the cost of replacement products based on the historical trend of returns and warranty replacements relative to sales and any current information regarding specific customer yield issues that may exceed historical trends. We recognize revenue upon shipment and title transfer, if all other criteria have been met. We also provide certain services such as mask making and probing and revenue is

recognized when our services are completed.

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Share-based Compensation Expense

Our share-based employee compensation plans are described in more detail under Share Ownership. We grant stock options to our employees and we record a compensation charge for the excess of the fair value of the stock at the measurement date over the amount an employee must pay to acquire the stock. We amortize share-based compensation using the straight-line method over the vesting periods of the related options, which are generally four years.

We grant stock options to our employees and certain non-employees. Prior to January 1, 2006, we accounted for share-based compensation in accordance with Accounting Principles Board Opinion No. 25, (APB 25), Accounting for Stock Issued to Employees, and related interpretations. We also followed the disclosure requirements of SFAS No. 123, Accounting for Stock-Based Compensation , as amended by SFAS 148, Accounting for Stock-Based Compensation-Transition and Disclosure. As a result, no expense was recognized for options to purchase our ordinary shares that were granted with an exercise price equal to fair market value at the day of the grant prior to January 1, 2006. Effective January 1, 2006, we adopted the provisions of Statement of Financial Accounting Standards No. 123(R), (SFAS 123(R)) Share-Based Payment, which establishes accounting for equity instruments exchanged for services. Under the provisions of SFAS 123(R), share-based compensation cost is measured at the grant date, based on the fair value of the award, and is recognized as an expense over the employee s requisite service period (generally the vesting period of the equity grant). We elected to adopt the modified prospective transition method as provided by SFAS 123(R) and, accordingly, financial statement amounts for the prior periods presented in this report have not been restated to reflect the fair value method of expensing share-based compensation. As a result of adopting SFAS 123 (R) on January 1, 2006, we recognized a benefit of US$5.2 million as a result of the cumulative effect of a change in accounting principle, in relation to the forfeiture rate applied on the unvested portion of the stock options. Our total actual share-based compensation expense for the year ended December 31, 2006, 2007 and 2008 was US$23.5, US$20.6, and US$11.6 million respectively.

The fair value of options and shares issued pursuant to our option plans at the grant date was estimated using the Black-Scholes option pricing model. This model was developed for use in estimating the fair value of traded options that have no vesting restrictions and are fully transferable. In addition, option-pricing models require the input of highly subjective assumptions, including the expected stock price volatility. We use projected volatility rates based upon the company s historical volatility rates. Because our employee stock options issued under our 2001 Stock Plan, 2001 Regulation S Stock Plan, 2001 Preference Shares Stock Plan and 2001 Regulation S Preference Shares Stock Plan had characteristics significantly different from those of publicly traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, in management s opinion, the existing models do not necessarily provide a reliable single measure of the fair value of our stock options.

Inflation

Although there can be no assurance as to the impact in future periods, we believe that, to date, inflation in China has not had a material impact on our results of operations. Inflation in China was approximately 1.5%, 4.8%, and 5.9% in 2006, 2007, and 2008, respectively.

Income Tax

As an exempted company incorporated in the Cayman Islands, we are exempt from Cayman Islands taxation. Our Chinese subsidiaries are subject to taxation pursuant to Enterprise Income Tax Law and various local income tax laws. Under relevant regulations and after approval by the local Tax Bureau, our Shanghai, Beijing and Tianjin subsidiaries will become entitled to a full exemption from foreign enterprise income tax, or FEIT, for five years starting with the first year of positive accumulated earnings, and a 50% reduction for the following five years. The tax holiday enjoyed by our Shanghai subsidiary took effect in 2004 when SMIS completed its first profit-making year. As of December 31, 2008, both Beijing and Tianjin entities were in loss positions and as a result the tax holiday had not yet taken effect.

According to PRC tax regulations, the Company s Chengdu subsidiary is entitled to a full exemption from FEIT for two years starting with the first year of positive accumulated earnings and a 50% reduction for the following three years. As of December 31, 2008, SMICD was still in a loss position. Pursuant to the New EIT Law, the tax holiday began in 2008 at the statutory tax rate of 25% despite the fact that SMICD had yet to be profitable.

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Our other subsidiaries are subject to their respective jurisdictions income tax laws, including Japan, United States, and Europe. Our income tax obligations to date have been minimal.

We account for income taxes in accordance with SFAS No. 109, Accounting for Income Taxes. SFAS No. 109 requires an asset and liability approach for financial accounting and reporting for income tax purposes. Under the asset and liability method, deferred income taxes are recognized for temporary differences, net operating loss carry-forwards and credits by applying enacted statutory tax rates applicable to future years. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized. We conduct this analysis on a quarterly basis. As of December 31, 2008, the Company has recognized deferred tax assets including $55.5 million from net operating loss carry forward and $59.2 million from temporary difference between the tax and book base of certain fixed assets. We provided full valuation allowance on net operating loss carry forward as we believe it is more likely than not that it would not to be realized. The temporary difference generated from depreciation of fixed assets relates specially to one of the Company s subsidiaries and this subsidiary has achieved profitability in prior years and is expected to continue to be profitable based on the current forecast. We have recognized $20.3 million valuation allowance based on the analysis on available positive and negative evidences, including profitability, utilization and production efficiency, industry cyclical risk and technology development risk.

Effective January 1, 2007, the Company adopted FASB Interpretation No. 48 Accounting for Uncertainty in Income Taxes an Interpretation of FASB Statement 109 (FIN 48), which prescribes a more-likely-than-not threshold for financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. This interpretation also provides guidance on de-recognition of income tax assets and liabilities, classification of current and deferred income tax assets and liabilities, accounting for interest and penalties associated with tax positions, accounting for income taxes in interim periods and income tax disclosures.

On March 16, 2007, the National People s Congress, the PRC legislature, approved and promulgated a new tax law named Enterprise Income Tax Law, On December 6, 2007, the PRC State Council issued the Implementation Regulations of the Enterprise Income Tax Law, both of which became effective on January 1, 2008. The Enterprise Income Tax Law and its Implementation Regulations, or the new EIT law, FIEs and domestic companies are subject to a uniform tax rate of 25%. The new EIT law eliminates or modifies most of the tax exemptions, reductions and preferential treatments available under the previous tax laws and regulations. The State Council issued the Notice of the State Council on the Implementation of the Transitional Preferential Policies in respect of Enterprise Income Tax on December 26, 2007, enterprises that were established before March 16, 2007 and already enjoy preferential tax treatments will (i) in the case of preferential tax rates, continue to enjoy the tax rates which will be gradually increased to the new tax rates within five years from January 1, 2008 or (ii) in the case of preferential tax exemption or reduction for a specified term, continue to enjoy the preferential tax holiday until the expiration of such term. Thus, SMIC Shanghai, SMIC Beijing and SMIC Tianjin could fall into condition (ii) and may be entitled to the five year exemption and five year reduction as subject to the final recognition by the PRC tax authorities. While the EIT Law equalizes the tax rates for FIEs and domestic companies, preferential tax treatment would continue to be given to companies in certain encouraged sectors and to entities classified as high and new technology enterprises companies supported by the PRC government, whether FIEs or domestic companies. According to the new EIT Law, entities that qualify as high and new technology enterprises especially supported by the PRC government are expected to benefit from a tax rate of 15% as compared to the uniform tax rate of 25%. Implementation Regulations of the Enterprise Income Tax Law, a high and new technology enterprise shall have core self-owned intellectual properties and its products shall be within the scope provided by the high-technology field highly supported by the State .

Under the new EIT law, dividends, interests, rent, royalties and gains on transfers of property payable by a foreign-invested enterprise in the PRC to its foreign investor who is a non-resident enterprise will be subject to a 10% withholding tax, unless such non-resident enterprise s jurisdiction of incorporation has a tax treaty with the PRC that provides for a reduced rate of withholding tax. The Cayman Islands, where SMIC is incorporated, does not have such a tax treaty with the PRC. If SMIC is considered a non-resident enterprise, this new 10% withholding tax imposed on SMIC s dividend income received from SMIC Shanghai, SMIC Beijing and SMIC Tianjin would reduce its net income and have an adverse effect on its operating results.

Under the new EIT law, an enterprise established outside the PRC with its de facto management body within the PRC is considered a resident enterprise and will be subject to the enterprise income tax at the rate of 25% on its worldwide income and foreign tax credit may be applicable. The de facto management body is defined as the organizational body that effectively exercises overall management and control over production and business operations, personnel, finance and accounting, and properties of the enterprise. It remains unclear how the PRC tax authorities will interpret such a broad definition. Substantially the majority of management members of SMIC are based in the PRC. If the PRC tax authorities subsequently determine that SMIC should be classified as a resident enterprise, then SMIC s worldwide income will be subject to income tax at a uniform rate of 25%, which may have a material adverse effect on SMIC s financial condition and results of operations. Notwithstanding the foregoing provision, the new EIT law also provides that, if a resident enterprise directly invests in another resident enterprise, the dividends received by the investing resident enterprise from the invested enterprise are exempted from income tax, subject to certain conditions. Therefore, if SMIC is classified as a resident enterprise, the dividends received from our PRC subsidiary may be exempted from income tax. However, it remains unclear how the PRC tax authorities will interpret the PRC tax resident treatment of an offshore company, like SMIC, having indirect ownership interests in PRC enterprises through intermediary holding vehicles.

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On February 22, 2008, the PRC government promulgated Caishui (2008) No.1, the Notice of the Ministry of Finance and State Administration of Tax concerning Certain Enterprise Income Tax Preferential Policies (Caishui No.1). Pursuant to Caishui No.1, integrated circuit production enterprises whose total investment exceeds RMB8,000 million (approximately $1,095 million) or whose integrated circuits have a line width of less than 0.25 micron are entitled to preferential tax rate of 15%. If the operation period is more than 15 years, those enterprises are entitled to a full exemption from income tax for five years starting from the first profitable year after utilizing all prior years tax losses and 50% reduction for the following five years. SMIS, SMIB and SMIT have met such accreditation requirements.

Foreign Currency Fluctuations

Our sales are generally denominated in U.S. dollars and our operating expenses and capital expenditures are generally denominated in U.S. dollars, Japanese Yen, Euros and Renminbi. Accordingly, we are affected by fluctuations in exchange rates between the U.S. dollar and each of the Japanese Yen, the Euro and the Renminbi. See Risk Factors Risks Related to Conducting Operations in China Devaluation or appreciation in the value of the Renminbi or restrictions on convertibility of the Renminbi could adversely affect our operating results and Risk Factors Risks Related to Our Financial Condition and Business Exchange rate fluctuations could increase our costs, which could adversely affect our operating results and the value of our ADSs for a discussion of the effects on our company of fluctuating exchange rates and Item 11-Quantative and Qualitative Disclosures About Market Risk-Foreign Exchange Rate Fluctuation Risk for a discussion of our efforts to minimize such risks.

Recent Accounting Pronouncements

In December 2007, the FASB issued SFAS No. 141, Business Combinations: (Revised 2007) (SFAS 141R). SFAS 141R is relevant to all transactions or events in which one entity obtains control over one or more other businesses. SFAS 141R requires an acquirer to recognize any assets and non-controlling interest acquired and liabilities assumed to be measured at fair value as of the acquisition date. Liabilities related to contingent consideration are recognized and measured at fair value on the date of acquisition rather than at a later date when the amount of the consideration may be resolved beyond a reasonable doubt. This revised approach replaces SFAS 141 s cost allocation process in which the cost of an acquisition was allocated to the individual assets acquired and liabilities assumed based on their respective fair value. SFAS 141R requires any acquisition-related costs and restructuring costs to be expensed as incurred as opposed to allocating such costs to the assets acquired and liabilities assumed as previously required by SFAS 141. Under SFAS 141R, an acquirer recognizes liabilities for a restructuring plan in purchase accounting only if the requirements of SFAS 146, Accounting for Costs Associated with Exit or Disposal Activities , are met. SFAS 141R allows for the recognition of pre-acquisition contingencies at fair value only if these contingencies are likely to materialize. If this criterion is not met at the acquisition date, then the acquirer accounts for the non-contractual contingency in accordance with recognition criteria set forth under SFAS 5, Accounting for Contingencies , in which case no amount should be recognized in purchase accounting. SFAS 141R is effective as of the beginning of an entity s first fiscal year that begins after December 15, 2008. The adoption of SFAS 141R will change the Company s accounting treatment for business combination on a prospective basis beginning on January 1, 2009.

In December 2007, the FASB issued SFAS No. 160, Non-controlling Interests in Consolidated Financial Statements an Amendment of ARB No. 51 (SFAS 160). This Statement amends ARB 51, Consolidated Financial Statements, to establish accounting and reporting standards for the non-controlling interest in a subsidiary and for the deconsolidation of a subsidiary. It clarifies that a non-controlling interest in a subsidiary is an ownership interest in the consolidated entity and should be reported as equity on the financial statements. SFAS 160 requires consolidated net income to be reported at amounts that include the amounts attributable to both the parent and the non-controlling interest. Furthermore, disclosure of the amounts of consolidated net income attributable to the parent and to the non-controlling interest is required on the face of the financial statements. SFAS 160 is effective as of the beginning of an entity s first fiscal year that begins after December 15, 2008. The Company will incorporate the presentation requirements outlined by SFAS No. 160 on January 1, 2009.

In March 2008, the FASB issued SFAS No. 161, Disclosures about Derivative Instruments and Hedging Activities an amendment of FASB Statement No. 133 (SFAS 161). SFAS 161 enhances the required disclosures under SFAS 133, Accounting for Derivative Instruments and Hedging Activities , in order to provide the investing community additional transparency in an entity s financial statements and to more adequately disclose the impact investments in derivative

instruments and use of hedging have on financial position, operating results and cash flows. SFAS 161 is effective for fiscal years and interim periods beginning after November 15, 2008, with early application allowed. SFAS 161 does not change the accounting treatment for derivative instruments and will change the Company s disclosure for derivative instruments and hedging activities on January 1, 2009.

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In April, 2008, the FASB issued FSP. FAS 142-3, Determination of the Useful Life of Intangible Assets (FSP 142- 3). In determining the useful life of acquired intangible assets, FSP 142-3 removes the requirement to consider whether an intangible asset can be renewed without substantial cost of material modifications to the existing terms and conditions and, instead, requires an entity to consider its own historical experience in renewing similar arrangements. FSP 142-3 also requires expanded disclosure related to the determination of intangible asset useful lives. FSP 142-3 is effective for fiscal years beginning after December 15, 2008. The guidance for determining the useful life of a recognized intangible asset must be applied prospectively to intangible assets acquired after the effective date. Early adoption is prohibited. The adoption of FSP 142-3 will not have a material impact on the Company s consolidated financial position or result of operations.

In November 2008, the Emerging Issues Task Force issued EITF No. 08-6, Equity Method Investment Accounting Considerations (EITF 08-6) that addresses how the initial carrying value of an equity method investment should be determined, how an impairment assessment of an underlying indefinite-lived intangible asset of an equity method investment should be performed, how an equity method investee s issuance of shares should be accounted for, and how to account for a change in an investment from the equity method to the cost method. EITF 08-6 shall be effective in fiscal years beginning on or after December 15, 2008, and interim periods within those fiscal years. EITF 08-6 shall be applied prospectively with early application prohibited. The impact of adopting EITF 08-6 will not have a material impact on our consolidated financial condition or results of operations.

Incentives from the Chinese government

The chart below sets forth a brief summary of the material incentives received by our Chinese subsidiaries from the Chinese government. Our Shanghai, Beijing, and Tianjin subsidiaries are qualified as integrated circuit production enterprises under the Chinese government s *Several Policies to Encourage the Development of Software and Integrated Circuit Industry*. Under these policies, any company that engages in the semiconductor industry in China and has a total investment size in excess of 8,000 million Renminbi (approximately US$964 million) and fabricates integrated circuits that have a linewidth of less than 0.25 micron are entitled to the last three benefits listed below. For a more detailed discussion of these incentives, see Item 4 Information on the Company Regulation.

Incentive	**SMIC Shanghai, SMIC Beijing, and SMIC Tianjin**
Preferential Value-added Tax Policies	17% VAT rate. 17% tax refund rate for exports reduced to 13% as of January 1, 2004. 13% tax refund rate for exports increased to 17% as of November 1, 2004.
Preferential Enterprise Income Tax Policies	Five-year full exemption and five-year 50% reduction upon approval from the local tax bureau.
Preferential Customs Duties and Import-related VAT Policies	Exemption from customs duties with respect to its equipment, spare parts and raw materials. Exemption from import-related VAT with respect to its equipment, spare parts and raw materials. Exemption from VAT for imported equipment will no longer apply as of July 1, 2009 and a 17% VAT rate will apply.

Operating Results

Sales

We generate our sales primarily from fabricating semiconductors. We also derive a relatively small portion of our sales from the mask-making, wafer probing, and other services that we perform for third parties separately from our foundry services.

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In 2008, fabless semiconductor companies accounted for 56.8%, IDMs accounted for 25.3% and systems and other companies accounted for 17.9%, respectively, of our sales. Although we are not dependent on any single customer, a significant portion of our net sales is attributable to a relatively small number of our customers. In 2006, 2007, and 2008 our five largest customers accounted for approximately 59.5%, 60.0%, and 58.2% of our sales, respectively.

Cost of sales

Our cost of sales consists principally of:

- depreciation and amortization;
- overhead, including maintenance of production equipment, indirect materials, including chemicals, gases and various types of precious and other metals, utilities and royalties;
- direct materials, which consist of raw wafer costs;
- labor, including amortization of deferred stock compensation for employees directly involved in manufacturing activities; and
- production support, including facilities, utilities, quality control, automated systems and management functions.

Our depreciation expenses attributable to cost of sales were US$786.7 million in 2006, US$657.8 million in 2007, and US$663.1 million in 2008.

Operating expenses (income)

Our operating expenses (income) consist of:

- *Research and development expenses*. Research and development expenses consist primarily of salaries and benefits of research and development personnel, materials costs, depreciation and maintenance on the equipment used in our research and development efforts, contracted technology development costs, and the costs associated with the ramp-up of new fabs but are partially offset by related government subsidies.
- *General and administrative expenses*. General and administrative expenses consist primarily of salaries and benefits for our administrative, finance and human resource personnel, commercial insurance, fees for professional services, foreign exchange gains and losses from operating activities. Foreign exchange gains and losses relate primarily to period-end translation adjustments due to exchange rate fluctuations that affect payables and receivables directly related to our operations.
- *Selling and marketing expenses*. Selling and marketing expenses consist primarily of salaries and benefits of personnel engaged in sales and marketing activities, costs of customer wafer samples, other marketing incentives and related marketing expenses.
- *Amortization of acquired intangible assets.* Amortization of acquired intangible assets consist primarily of the cost associated with the purchase of technology, licenses, and patent licenses.
- *Income from sale of plant and equipment and other fixed assets.* In 2008, the Company sold plant, equipment and other fixed assets with a carrying value of US$7,542,561 for US$10,419,736, which resulted in a gain on disposal of US$2,877,175.

Other income (expenses)

Our other income (expenses) consists of:

- interest income, which has been primarily derived from cash equivalents and short-term investments and interest on share purchase receivables;
- interest expenses, net of capitalized portions and government interest subsidies, which have been primarily attributable to our bank loans and the imputed interest rate on an outstanding interest-free promissory note; and
- other income and expense items, such as those relating to the employee living quarters and school; and foreign exchange gains and losses relating to financing and investing activities, including forward contracts.

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Comparisons of Results of Operations

Consolidated Financial Data

The summary consolidated financial data presented below as of and for the years ended December 31, 2006, 2007, and 2008 are derived from, and should be read in conjunction with, and are qualified in their entirety by reference to, our audited consolidated financial statements, including the related notes, included elsewhere in this annual report. The summary consolidated financial data as of and for the years ended December 31, 2004 and 2005 is derived from our audited consolidated financial statements not included in this annual report. The summary consolidated financial data presented below has been prepared in accordance with U.S. GAAP.

	For the year ended December 31,				
	2004	**2005**	**2006**	**2007**	**2008**
	(in US$ thousands, except for per share, per ADS data, percentages, and operating data)				
Statement of Operations Data:					
Sales	$ 974,664	$ 1,171,319	$ 1,465,323	$ 1,549,765	**$ 1,353,711**
Cost of sales[(1)]	716,225	1,105,134	1,338,155	1,397,038	**1,412,851**
Gross profit (loss)	258,439	66,185	127,168	152,727	**(59,140)**
Operating expenses:					
Research and development	74,113	78,865	94,171	97,034	**102,240**
General and administrative	54,038	35,701	47,365	74,490	**58,841**
Selling and marketing	10,384	17,713	18,231	18,716	**20,661**
Litigation settlement	16,695				
Amortization of acquired intangible assets	14,368	20,946	24,393	27,071	**32,191**
Impairment loss of long-lived assets					**106,741**
Income from sale of plant and equipment and other fixed assets			(43,122)	(28,651)	**(2,877)**
Total operating expenses	169,598	153,225	141,038	188,659	**317,797**

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	For the year ended December 31,				
	2004	2005	2006	2007	2008
	(in US$ thousands, except for per share, per ADS data, percentages, and operating data)				
Income (loss) from operations	88,841	(87,040)	(13,870)	(35,932)	**(376,937)**
Other income (expenses):					
Interest income	10,587	11,356	14,916	12,349	**11,542**
Interest expense	(13,698)	(38,784)	(50,926)	(37,936)	**(50,767)**
Foreign currency exchange gain (loss)	8,218	(3,355)	(21,912)	11,250	**3,230**
Other, net	2,441	4,462	1,821	2,238	**7,429**
Total other income (expense), net	7,548	(26,322)	(56,101)	(12,100)	**(28,566)**
Income (loss) before income tax	96,389	(113,362)	(69,971)	(48,032)	**(405,503)**
Income tax current	(186)	(285)	24,928	29,720	**(26,433)**
Minority interest		251	(19)	2,856	**(7,851)**
Loss from equity investment		(1,379)	(4,201)	(4,013)	**(444)**
Net (loss) income before cumulative effect of a change in accounting principle	96,203	(114,775)	(49,263)	(19,468)	**(440,231)**
Cumulative effect of a change in accounting principle			5,154		
Net (loss) income	96,203	(114,775)	(44,109)	(19,468)	**(440,231)**
Deemed dividend on preference shares[2]	18,840				
Income (loss) attributable to holders of ordinary shares	$ 77,363	$ (114,775)	$ (44,109)	$ (19,468)	**(440,231)**
Income (loss) per ordinary share, basic	$ 0.01	$ (0.00)	$ (0.00)	$ (0.00)	**$ (0.02)**
Income (loss) per ordinary share, diluted	$ 0.00	$ (0.00)	$ (0.00)	$ (0.00)	**$ (0.02)**
Ordinary shares used in calculating basic income (loss) per ordinary share[4]	14,199,163,517	18,184,429,255	18,334,498,923	18,501,940,489	**18,682,544,866**
Ordinary shares used in calculating	17,934,393,066	18,184,429,255	18,334,498,923	18,501,940,489	**18,682,544,866**

diluted income (loss) per ordinary share[3][4]										
Income (loss) per ADS, basic[5]	$	0.27	$	(0.32)	$	(0.12)	$	(0.05)	**$**	**(1.18)**
Income (loss) per ADS, diluted[5]	$	0.22	$	(0.32)	$	(0.12)	$	(0.05)	**$**	**(1.18)**

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	For the year ended December 31,				
	2004	**2005**	**2006**	**2007**	**2008**
	(in US$ thousands, except for per share, per ADS data, percentages, and operating data)				
ADS used in calculating basic income (loss) per ADS[5]	283,983,270	363,688,585	366,689,978	370,038,810	**373,650,897**
ADS used in calculating diluted income (loss) per ADS[5]	358,687,861	363,688,585	366,689,978	370,038,810	**373,650,897**
Other Financial Data:					
Gross margin	26.50%	5.70%	8.70%	9.90%	**-4.40%**
Operating margin	9.10%	-7.40%	-0.90%	-2.30%	**-27.80%**
Net margin	9.90%	-9.80%	-3.00%	-1.30%	**-32.50%**
Operating Data:					
Wafers shipped (in 8 equivalents)					
Total	943,463	1,347,302	1,614,888	1,849,957	**1,611,208**
ASP[6]	1,033	869	907	838	**840**

(1) Including amortization of deferred stock compensation for employees directly involved in manufacturing activities.

(2) Deemed dividend represents the difference between the sale and conversion prices of warrants to purchase convertible preference shares we issued and their respective fair market values.

(3) Anti-dilutive preference shares, options and warrants were excluded from the weighted average ordinary shares outstanding for the diluted per share calculation. For 2005, 2006, 2007, and 2008 basic income (loss) per share did not differ from diluted loss per share.

(4) All share information has been adjusted retroactively to reflect the 10-for-1 share split effected upon completion of the global offering of our ordinary shares in March 2004 (the Global Offering).

(5) Fifty ordinary shares equals one ADS.

(6) Total sales/total wafers shipped.

Comparisons of the Years Ended December 31, 2006, 2007 and 2008

Year Ended December 31, 2008 Compared to Year Ended December 31, 2007

Sales. Sales decreased by 12.7% from US$1,549.8 million for 2007 to US$1,353.7 million for 2008, primarily due to the transition of DRAM production to logic production in the Beijing fab and the sharp market downturn experienced in the fourth quarter. However, consistent with our stated strategy of focusing on the non-DRAM business, non-DRAM revenue has grown by 14.3% for the same period. The number of wafers the Company shipped decreased by 12.9%, from 1,849,957 8-inch wafer equivalents to 1,611,208 8-inch wafer equivalents, while the number of logic

only wafer shipments increased by 24.9% between the two periods. The average selling price of the wafers the Company shipped remained relatively flat, with a slight increase of 0.2% from US$838 per wafer to US$840 per wafer. Due to the exit from the commodity DRAM business, the percentage of wafer revenues that used 0.13 micron and below process technology decreased from 53.1% to 43.9% between these two periods. However, if DRAM revenue is excluded, the percentage of wafer revenues that used 0.13 micron and below process technology increased from 24.9% to 38.2% between these two periods.

Cost of sales and gross profit. Cost of sales increased by 1.1% from US$1,397.0 million for 2007 to US$1,412.9 million for 2008. Out of the total cost of sales for 2008, US$663.1 million was attributable to depreciation of plant and equipment and another US$28.4 million was attributable to amortization of deferred costs and share-based compensation costs. Out of the total cost of sales for 2007, US$657.8 million was attributable to depreciation of plant and equipment and another US$33.8 million was attributable to amortization of deferred costs and share-based compensation costs. The Company had a gross loss of US$59.1 million for 2008 compared to a gross profit of US$152.7 million in 2007. Gross margins were -4.4% in 2008 compared to 9.9% in 2007. The decrease in gross margins was due to the transition of DRAM production to logic production in the Beijing fab which resulted in lower utilization, as well as the write down of DRAM inventories and the sharp market downturn experienced in the fourth quarter.

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***Operating expenses and loss from operations*.** Operating expenses increased by 68.4% from US$188.7 million for 2007 to US$317.8 million for 2008 primarily due to the impairment charge recorded in 2008 in connection with the decision to exit the commodity DRAM business. The Company received less income from the sale of equipment and fixed assets, which income was US$28.7 million in 2007 compared to US$2.9 million in 2008.

As described in Note 13. Acquired intangible assets, net , the amortization of acquired intangible assets increased from US$27.1 million for 2007 to US$32.2 million for 2008.

Research and development expenses increased by 5.4% from US$97.0 million for 2007 to US$102.2 million for 2008. The Company received an increase in government subsidies for research and development expenses in 2008; however, expenses associated with 45-nanometer and 65-nanometer technology development, as well as expenses incurred for the Shanghai 12-inch project, also increased in 2008.

General and administrative expenses decreased by 21.1% to US$58.8 million for 2008 from US$74.5 million for 2007, primarily due to a decrease in legal fees as well as a foreign exchange gain from operating activities of US$8.2 million recorded in 2008, while a foreign exchange loss from operating activities of US$3.1 million was recorded in 2007.

Selling and marketing expenses increased by 10.7% from US$18.7 million for 2007 to US$20.7 million for 2008, due to an increase in sales and marketing activities.

During the first quarter of 2008, the Company reached an agreement with certain customers to discontinue production of DRAM products and subsequently the Company decided to exit the commodity DRAM business. The Company considered these actions to be an indicator of impairment in regard to plant and equipment of the Company s Beijing facilities. The Company recorded an impairment loss of $105.8 million during the first quarter of 2008, equal to the excess of the carrying value over the fair value of the plant and equipment utilizing a discounted cash flow approach. For the purpose of the analysis, a discount rate of 9% has been used on the expected cash flows to be generated over the remaining useful lives of primary manufacturing machinery and equipments of approximately 5 years.

As a result, the Company s loss from operations was US$376.9 million in 2008 compared to loss from operations of US$35.9 million in 2007. Operating margin was negative 27.8% and 2.3%, respectively, for these two years.

Other income (expenses). Other expenses increased from US$12.1 million in 2007 to US$28.6 million in 2008 primarily due to an increase in interest expense. This increase in interest expense, from US$37.9 million in 2007 to US$50.8 million in 2008, was primarily due to a decrease in interest subsidy. Foreign exchange gain from non-operating activities decreased from US$11.3 million in 2007 to US$3.2 million in 2008. Total foreign exchange gain, combining the operating and non-operating activities, was US$11.4 million in 2008 as compared to US$8.1 million in 2007.

Net loss. Due to the factors described above, the Company recorded a net loss of US$440.2 million in 2008 compared to a net loss of US$19.5 million for 2007.

Year Ended December 31, 2007 Compared to Year Ended December 31, 2006

Sales. Sales increased by 5.8% from US$1,465.3 million for 2006 to US$1,549.8 million for 2007, primarily as a result of the increase in the Company s manufacturing capacity and ability to use such capacity to increase sales. The number of wafers the Company shipped increased by 14.6%, from 1,614,888 8-inch wafer equivalents to 1,849,957 8-inch wafer equivalents, between these two periods. The average selling price of the wafers the Company shipped decreased by 7.6% from US$907 per wafer to US$838 per wafer primarily due to the decline in DRAM average selling price. The percentage of wafer revenues that used 0.13 micron and below process technology increased from 49.6% to 53.1% between these two periods.

***Cost of sales and gross profit*.** Cost of sales increased by 4.4 % from US$1,338.2 million for 2006 to US$1,397.0 million for 2007. This increase was primarily due to the significant increase in wafer shipments as well as subcontracting costs associated with turn-key services. The Company had a gross profit of US$152.7 million for 2007 compared to a gross profit of US$127.2 million in 2006. Gross margins were 9.9 % in 2007 compared to 8.7 % in 2006. The increase in gross margins was primarily due to a decrease in depreciation expenses.

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***Operating expenses and loss from operations*.** Operating expenses increased by 33.8% from US$141.0 million for 2006 to US$188.7 million for 2007 primarily due to the combination of a $27.1M increase in general and administrative expenses and a $14.5 million decrease of income received from the sale of plant and equipments, from $43.1 million in 2006 compared to $28.7 million in 2007.

As described in Note 11. Acquired intangible assets, net , the amortization of acquired intangible assets increased from US$24.4 million for 2006 to US$27.1 million for 2007.

Research and development expenses increased by 3.0% from US$94.2 million for 2006 to US$97.0 million for 2007. This increase in research and development expenses resulted primarily from an increase in material and other production related expenses associated with 65nm technology development and the start-up costs associated with the new Shanghai 12-inch project.

General and administrative expenses increased by 57.2% to US$74.5 million for 2007 from US$47.4 million for 2006, primarily due to an increase in personnel related expenses, legal fees and tax related expenses.

Selling and marketing expenses increased by 2.7% from US$18.2 million for 2006 to US$18.7 million for 2007, due to an increase in sales and marketing personnel expenses.

As a result, the Company s loss from operations was US$35.9 million in 2007 compared to loss from operations of US$13.9 million in 2006. Operating margin was negative 2.3% and 0.9%, respectively, for these two years.

Other income (expenses). Other expenses decreased from US$56.1 million in 2006 to US$12.1 million in 2007. This decrease was primarily attributable to the decrease in interest expense from US$51.0 million in 2006 to US$37.9 million in 2007, and the decrease in foreign exchange loss from US$21.9 million in 2006 to a gain of US$11.2 million in 2007.

Net loss. Due to the factors described above, the Company had a net loss of US$19.5 million in 2007 compared to a net loss of US$44.1 million for 2006.

Liquidity and Capital Resources

The following table sets forth a condensed summary of our audited statements of cash flows for the periods indicated:

	For the year ended December 31,		
	2006	2007	2008
	(in US$ thousands)		
Net cash provided by operating activities:			
Net loss before cumulative effect of change in accounting principle	$ (49,263)	$ (19,468)	$ (440,231)
Depreciation and amortization	919,616	706,277	761,809
Total	769,649	672,465	569,782
Net cash used in investing activities:			
Purchase of property, plant and equipment	(882,581)	(717,171)	(669,055)
Total	(917,369)	(643,344)	(761,713)
Net cash provided by (used in) financing activities:			
Proceeds from short-term borrowings	255,004	201,658	422,575
Proceeds from long-term debt	785,345	262,248	285,930
Total	(74,440)	76,637	173,314
Net increase (decrease) in cash and cash equivalents	$ (222,177)	$ 105,664	$ (19,054)

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Operating Activities

As of December 31, 2008, we had US$450.2 million in cash and cash equivalents. These cash and cash equivalents are held in the form of United States dollars, Japanese Yen, European Euros, and Chinese Renminbi. Our net cash provided by operating activities in 2008 was US$569.8 million, which was primarily due to the loss attributable to holders of ordinary shares of US$440.2 million, a decrease of US$76.7 million in inventories, a decrease of US$99.0 million in accounts receivable and an increase of US$76.8 million in accounts payable relating to the purchase of materials and inventories, and the add-back of US$761.8 million in depreciation and amortization relating to commercial production.

As of December 31, 2007, we had US$469.3 million in cash and cash equivalents. These cash and cash equivalents are held in the form of United States dollars, Japanese Yen, European Euros, and Chinese Renminbi. Our net cash provided by operating activities in 2007 was US$672.5 million, which was primarily due to the loss attributable to holders of ordinary shares of US$19.5 million, a decrease of US$26.9 million in inventories, an increase of US$46.2 million in accounts receivable due to an increase in sales and an increase of US$19.9 million in accounts payable relating to the purchase of materials and inventories, and the add-back of US$706.3 million in depreciation and amortization relating to commercial production.

As of December 31, 2006, we had US$363.6 million in cash and cash equivalents. These cash and cash equivalents are held in the form of United States dollars, Japanese Yen, European Euros, and Chinese Renminbi. Our net cash provided by operating activities in 2006 was US$769.6 million, which was primarily due to the loss attributable to holders of ordinary shares of US$44.1 million, an increase of US$83.9 million in inventories due to the increase in commercial production, an increase of US$10.9 million in accounts receivable due to an increase in sales and an increase of US$24.7 million in accounts payable relating to the purchase of materials and inventories, and the add-back of US$919.6 million in depreciation and amortization relating to commercial production.

Investing Activities

Our net cash used in investing activities was US$761.7 million in 2008, US$643.3 million in 2007, and US$917.4 million in 2006. This was primarily attributable to purchases of plant and equipment and land use rights for our mega-fabs in Shanghai and Beijing, and Tianjin fab in these periods as well as costs associated with the Shanghai fab construction.

Financing Activities

Our net cash provided by financing activities in 2008 was US$173.3 million. This was primarily derived from US$422.6 million in proceeds from short-term borrowings, US$285.9 million in proceeds from long-term debt, US$328.3 million in the repayment of short-term borrowings, and US$345.8 million in the repayment of long-term debt.

Our net cash used in financing activities in 2007 was US$76.6 million. This was primarily derived from US$201.7 million in proceeds from short-term borrowings, US$262.2 million in proceeds from long-term debt, US$165.7 million in the repayment of short-term borrowings, and US$195.6 million in the repayment of long-term debt. In addition, US$168.1 million came from proceeds from the issuance of ordinary shares.

Our net cash used in financing activities in 2006 was US$74.4 million. This was primarily derived from US$255.0 million in proceeds from short-term borrowings, US$785.3 million in proceeds from long-term debt, US$449.5 million in the repayment of short-term borrowings, and US$635.6 million in the repayment of long-term debt.

In 2009, the Company has already acquired new credit facilities totaling approximately US$240 million.

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Capital Expenditures

We incurred capital expenditures of US$912 million, US$860 million, and US$666 million in 2006, 2007 and 2008, respectively. We currently expect our capital expenditures in 2009 to total approximately US$190 million, to be adjusted based on market conditions. We have financed our substantial capital expenditure requirements through the proceeds received in our global offering, several rounds of private financing, cash flows from operations, and bank borrowings. Once a fab is in operation at acceptable capacity and yield rates, it can provide significant cash flows. Any transfer of funds from our company to our Chinese subsidiaries, either as a shareholder loan or as an increase in registered capital, is subject to registration or approval of Chinese governmental authorities, including the relevant administration of foreign exchange and/or the relevant examining and approval authority. In addition, it is not permitted under Chinese law for our Chinese subsidiaries to directly lend money to each other. Therefore, it is difficult to change our capital expenditure plans once the relevant funds have been remitted from our company to our Chinese subsidiaries. These limitations on the free flow of funds between us and our Chinese subsidiaries could restrict our ability to act in response to changing market conditions and reallocate funds from one Chinese subsidiary to another in a timely manner.

The global economy has deteriorated and there has been unprecedented financial market volatility. These conditions have resulted in a reduction in demand in the foundry industry, which in turn have resulted in declines in orders or in some instances, customers requesting for a deferment of deliveries on existing orders. Our cash flows from operations have historically exceeded operating income, reflecting our significant non-cash depreciation expenses. Our operating cash flows may not be sufficient to meet our capital expenditure requirements in 2009. If our operating cash flows are insufficient, we plan to fund the expected shortfall through bank loans. If necessary, we will also explore other forms of external financing.

We cannot predict the timing, strength or duration of any economic deterioration or subsequent economic recovery, worldwide, or in the foundry industry. If the current economic or market conditions persist or deteriorate further, our business, financial condition and results of operations could be materially and adversely affected. Therefore there can be no assurance that our business will generate and continue to generate sufficient cash flow to fund our liquidity needs in the future as cash flow generation may be affected by, among other factors, sales levels, capacity utilization, industry business conditions as well as global economic conditions.

Commitments

As of December 31, 2008, we had commitments of US$7.4 million for facilities construction obligations for our Shanghai, Beijing, Tianjin fabs and living quarters, and our testing facility and living quarters in Chengdu and US$52.2 million to purchase machinery and equipment for the Shanghai, Beijing, and Tianjin fabs, and the testing facility in Chengdu.

For additional information, see Item 5 Operating and Financial Review and Prospects Factors that Impact Our Results of Operations Substantial Capital Expenditures and Capacity Expansion.

As of December 31, 2008, our outstanding long-term liabilities primarily consisted of US$897.1 million in secured bank loans, of which US$360.6 million is classified as the current portion of long-term loans. The long-term loans are repayable in installments that commenced in 2006, with the last payment in August 2012.

2006 Loan Facility (SMIC Shanghai). In June 2006, Semiconductor Manufacturing International (Shanghai) Corporation (SMIC Shanghai) entered into a USD denominated long-term facility arrangement for US$600.0 million with a consortium of international and PRC banks. Of this principal amount, US$393.0 million was used to repay the principal amount outstanding under SMIC Shanghai s bank facilities from December 2001 and January 2004. The remaining principal amount was used to finance future expansion and general corporate requirement for SMIC Shanghai. As of December 31, 2007, SMIC Shanghai had fully drawn down on this loan facility. The principal amount is repayable starting from December 2006 in ten semi-annual installments. As of December 31, 2008, SMIC Shanghai had repaid US$334.0 million according to the repayment schedule. In 2008, the interest rate on the loan ranged from 2.47% to 5.76%. The interest expense incurred in 2006, 2007 and 2008 was US$13.5 million, US$17.3 million, and US$17.0 million, of which US$1.6 million, US$3.3 million, and US$5.4 million was capitalized as additions to assets under construction in 2006, 2007 and 2008, respectively.

The total outstanding balance of this long-term facility is collateralized by certain plant and equipment located in SMIC Shanghai 8-inch fabs at the original cost of US$1,871 million as of December 31, 2008.

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The long-term loan agreement entered into in June 2006 contains the following covenants:
Any of the following in respect of SMIC Shanghai would constitute an event of default during the term of the loan agreement (unless otherwise waived by the lenders to such agreement):
Financial covenants for the Borrower (SMIC Shanghai) including:
1. Consolidated Tangible Net Worth of no less than US$1,200 million;
2. Consolidated Total Borrowings to Consolidated Tangible Net Worth of:
(a) no more than 60% for periods up to and including December 31, 2008; and
(b) no more than 45% thereafter;
3. Consolidated Total Borrowings to trailing preceding four quarters EBITDA not to exceed 1.50x.
4. Debt Service Coverage Ratio of no less than 1.5x. Debt Service Coverage Ratio means trailing four quarters EBITDA divided by scheduled principal repayments and interest expense for all bank borrowings (including hire purchases, leases and other borrowed monies) for the same period.
Financial covenants for the Guarantor (the Company) including:
1. Consolidated Tangible Net Worth of no less than US$2,300 million;
2. Consolidated Net Borrowings to Consolidated Tangible Net Worth of:
(a) no more than 50% for period up to and including June 30, 2009;
(b) no more than 40% thereafter.
3. Consolidated Net Borrowings to trailing four quarters EBITDA of:
(a) no more than 1.50x for periods up to and including June 30, 2009;
(b) no more than 1.30x thereafter.
The Company and its related subsidiary have complied with these covenants (unless otherwise waived by the lenders to such agreement) as of December 31, 2008.
2005 Loan Facility (SMIC Beijing). In May 2005, Semiconductor Manufacturing International (Beijing) Corporation (SMIC Beijing) entered into a five year USD denominated loan facility in the aggregate principal amount of US$600.0 million, with a syndicate of financial institutions based in the PRC. This five-year bank loan was used to expand the capacity of SMIC Beijing s fabs. The drawdown period of this facility was twelve months from the sign off date of the agreement. As of December 31, 2006, SMIC Beijing had fully drawn-down US$600.0 million on this loan facility. The interest rate on this loan facility in 2008 ranged from 3.46% to 6.38%. The principal amount is repayable starting in December 2007 in six semi-annual installments. As of December 2008, SMIC Beijing had repaid an aggregated amount of US$300.0 million according to the repayment schedule. The interest expense incurred in 2006, 2007 and 2008 was US$28.5 million, US$42.2 million, and US$25.6 of which US$0.5 million, US$2.3 million, and US$1.6 million was capitalized as additions to assets under construction in 2006, 2007 and 2008, respectively.
The total outstanding balance of SMIC Beijing USD syndicate loan is collateralized by certain plant and equipment at the original cost of US$1,047.0 million as of December 31, 2008.
Any of the following in respect of SMIC Beijing would constitute an event of default during the term of the loan agreement (unless otherwise waived by the lenders to such agreement):
1. Where [Net profit + depreciation + amortization + financial expenses (increase of accounts receivable and advanced payments + increase of inventory increase in accounts payable and advanced receipts)]/ financial expenses < 1; and
2. (Total liability borrowings from shareholders, including principal and interest)/Total assets > 60% (when SMIC Beijing s capacity is less than 20,000 12-inch wafers per month); and (Total liability -borrowings from shareholders, including principal and interest)/Total assets > 50% (when SMIC Beijing s capacity exceeds 20,000 12-inch wafers per month).
SMIC Beijing has complied with these covenants (unless otherwise waived by the lenders to such agreement) as of December 31, 2008.

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2005 EUR Loan Facility. On December 15, 2005, the Company entered into a EUR denominated long-term loan facility agreement in the aggregate principal amount of EUR 85 million (equivalent to approximately US$105 million) with ABN Amro Bank N.V. Commerz Bank N.V., Shanghai Branch. The drawdown period of the facility ends on the earlier of (i) thirty six months after the execution of the agreement or (ii) the date on which the loans have been fully drawn down. Each draw down made under the facility shall be repaid in full by us in ten equal semi-annual installments starting from May 6, 2006.

As of December 31, 2008, SMIC Tianjin had drawdown EUR15.1 million and repaid an aggregate amount of EUR 9.1 million. As of December 31, 2008, the remaining balance is EUR6.0 million, with the approximate US dollar equivalent of US$8.6 million. In 2008, the interest rate on the loan ranged from 3.59% to 5.87%. The interest expense incurred in 2006, 2007 and 2008 was US$0.3 million, US$0.7 million and US$0.6 million of which US$0.07 million, US$0.06 million and US$0.1 million was capitalized as additions to assets under construction in 2006, 2007 and 2008, respectively.

The total outstanding balance of the facility is collateralized by certain SMIC Tianjin plant and equipment at the original cost of US$21.8 million as of December 31, 2008.

As of December 31, 2008, SMIC Shanghai had drawdown EUR56.9 million and repaid an aggregate amount of EUR12.1 million. As of December 31, 2008, the remaining balance is EUR 44.8 million, with the approximate US dollar equivalent of US$63.4 million. In 2008, the interest rate on the loan ranged from 3.01% to 6.12%. The interest expenses incurred in 2007 and 2008 were US$0.3 million and US$2.1 million of which US$0.02 million and US$0.7 million was capitalized additions to assets under construction in 2007 and 2008, respectively.

The total outstanding balance of the facility is collateralized by certain SMIC Shanghai s plant and equipment at the original cost of US$114.5 million as of December 31, 2008.

2006 Loan Facility (SMIC Tianjin). In May 2006, SMIC Tianjin entered into a loan facility in the aggregate principal amount of US$300.0 million from a consortium of international and Chinese banks. The Company has guaranteed SMIC Tianjin s obligations under this facility. As of December 31, 2008 SMIC Tianjin had drawn down US$259.0 million from the facility. The principal amount is repayable starting from February 2010 in six semi-annual installments. In 2008, the interest rate on the loan ranged from 3.11% to 6.03%. The interest expenses incurred in 2007 and 2008 were US$0.3 million and US$9.1 million, of which US$0.02 million and US$1.8 million were capitalized as additions to assets under construction in 2007 and 2008, respectively.

The total outstanding balance of the facility is collateralized by certain plant and equipment with an original cost of US$627.4 million as of December 31, 2008, which are located in our Tianjin fab, except for the manufacturing equipment purchased using the EUR denominated loan, and our land use rights and plant in proportion to the principal amount outstanding under this facility and the EUR denominated loan.

Any of the following in respect of SMIC Tianjin would constitute an event of default during the term of the loan agreement (unless otherwise waived by the lenders to such agreement):

1. [Net profit + depreciation + amortization + financial expenses (increase of accounts receivable and advanced payments + increase of inventory increase in accounts payable and advanced receipts)]/ financial expenses < 1; and
2. The ratio of total debt to total assets is more than 60% during the ramp up period of SMIC Tianjin and more than 40% after the facility is at full capacity.

SMIC Tianjin has complied with these covenants (unless otherwise waived by the lenders to such agreement) as of December 31, 2008.

Short-term Credit Agreements. As of December 31, 2008, we had ten short-term credit agreements that provided total credit facilities up to US$267.8 million on a revolving credit basis. As of December 31, 2008, we had drawn down US$201.2 million under these credit agreements and US$66.6 million is available for future borrowings. The outstanding borrowings under the credit agreements are unsecured. The interest expense incurred in 2008 was US$9.4 million. The interest rate on the loans ranged from 1.88% to 8.75% in 2008.

Please see Item 8 Financial Information Dividends and Dividend Policy on our ability to pay dividends on our ordinary shares.

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Please see Item 11 Quantitative and Qualitative Disclosures About Market Risk regarding the risk of loss related to adverse changes in market prices, including foreign currency exchange rates and interest rates of financial instruments.

Research and Development, Patents and Licenses, etc.

Our research and development activities are principally directed toward the development and implementation of more advanced and lower cost process technology. We spent US$94.2 million in 2006, US$97.0 million in 2007, and US$102.2 million in 2008 on research and development expenses, which represented 6.4%, 6.3%, and 7.6%, respectively, of our sales in those respective years. Our research and development costs are partially offset by related government subsidies of US$9.9 million, US$3.1 million and US$56.2 million in 2006, 2007 and 2008, respectively and include non-recurring engineering costs associated with the ramp-up of a new wafer facility. We plan to continue to invest significant amounts in research and development in 2009 for our 65 and 45 nanometer manufacturing process.

The research and development efforts were focused primarily on our logic and system-on-chip (SOC) business. 2008 marked many milestones for SMIC. Early in the year, Synopsis and SMIC released an enhanced 90-nanometer hierarchical, multi-voltage RTL-to-GDSII reference design flow that will benefit advanced synthesis with built-in capability of design-for-test and design-for-manufacturing. In April, working with a leading Chinese domestic fabless, we developed a 90 nanometer digital photo frame chip, which is one of the most integrated multimedia SOC in the market. For advanced CMOS logic, the Company demonstrated a silicon success in our 45-nanometer process ahead of schedule, and also added new intellectual properties in 65 nanometer and 90 nanometer technology services. In addition, the Company successfully developed a 0.11 micron CMOS image sensor (CIS) process technology. In Non-Volatile Memory (NVM) technology, the 0.13um ETox went into production in early 2008 and 90nm ETox is currently in risk production. Our research and development in Micro-Electromechanical System (MEMS) areas also advanced to risk production for the first customer in 2008. Other areas of phase-change memory, HV, mix-signal-signal, and RF technologies were also successfully advanced for smaller size, less power, and lower cost to meet customer demands.

We employ over 800 research and development personnel. This research and development team includes many experienced semiconductor engineers with advanced degrees from leading universities around the world, as well as top graduates from the leading universities in China. We believe this combination has enabled us to quickly bring our technology in line with the semiconductor industry technology roadmap and ensures that we will have skilled personnel to lead our technology advancement in the future.

Trend Information

See Item 5 Operating and Financial Review and Prospects Factors that Impact Our Results of Operations for a discussion of the most significant recent trends affecting our operations.

Off-Balance Sheet Arrangements

We have not entered into any off-balance sheet transactions.

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Tabular Disclosure of Contractual Obligations

Set forth in the table below are the aggregate amounts, as of December 31, 2008, of our future cash payment obligations under our existing debt arrangements on a consolidated basis:

		Payments due by period			
Contractual obligations	**Total**	**Less than 1 year**	**1 3 years**	**3 5 years**	**After 5 years**
			(consolidated)		
			(in US$ thousands)		
Secured Long-Term Debt[1]	897,147	360,629	536,518		
Operating Lease Obligations[2]	9,721	6,056	270	441	2,954
Purchase Obligations[3]	59,594	59,594			
Other Long-Term Obligations[4]	120,204	78,446	37,204	4,554	
Total Contractual Obligations	$ 1,086,666	$ 504,725	$ 573,992	$ 4,995	$ 2,954

(1) Interest was computed using rates in effect on December 31, 2008 within the range of 2.47% to 6.38%.

(2) Represents our obligations to make lease payments to use the land on which our fabs are located in Shanghai and other office equipment we have leased.

(3) Represents commitments for construction or purchase of semiconductor equipment, and other property or services.

(4) Includes the settlement with TSMC and the other long-term

liabilities relating to certain license agreements.

Item 6. Directors, Senior Management and Employees

Directors and Senior Management

Members of our board of directors are elected by our shareholders. As of May 31, 2009, our board of directors consists of seven directors and one alternate director.

The following table sets forth the names of our directors and executive officers, including our founder, as of May 31, 2009. Our executive officers are appointed by, and serve at the discretion of, our board of directors.

Name	Age	Position
Directors		
Yang Yuan Wang	74	Chairman, Independent Non-executive Director
Richard Ru Gin Chang	61	Founder, President, Chief Executive Officer and Executive Director
Zhou Jie	41	Non-executive Director
Wang Zheng Gang	58	Non-executive Director (Alternate director to Zhou Jie)
Tsuyoshi Kawanishi	80	Independent Non-executive Director
Lip-Bu Tan	49	Independent Non-executive Director
Jiang Shang Zhou	62	Independent Non-executive Director
Edward S Yang	71	Independent Non-executive Director
Senior Managers		
Morning Wu	52	Acting Chief Financial Officer and Chief Accounting Officer
Marco Mora	51	Chief Operating Officer
Chiou-Feng Chen	52	Vice President of Corporate Marketing & Sales Office
Anne Wai Yui Chen	47	Company Secretary, Hong Kong Representative and Chief Compliance Officer

Chairman of the Board, Independent Non-executive Director

Yang Yuan Wang is currently the Chairman and has been a Director since 2001. Professor Wang has more than 41 years of experience related to the semiconductor industry. He is the Chairman of SMIC Shanghai, SMIC Beijing, SMIC Chengdu, SMIC Tianjin, SMIC Energy Technology (Shanghai) Corporation and is also a director of SMIC Shenzhen. He is also the Chief Scientist of the Institute of Microelectronics, Peking University, and Academician of Chinese Science Academy. He is a fellow of the Chinese Academy of Sciences, The Institute of Electrical and Electronics Engineers (USA), The Institute of Electrical Engineers (UK) and Chinese Institute of Electronics (China).

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Founder, President, Chief Executive Officer and Executive Director

Richard Ru Gin Chang founded our company in April 2000 and is currently President, Chief Executive Officer and Executive Director. Dr. Chang is also a director of SMIC Shanghai, SMIC Beijing, SMIC Tianjin, SMIC Shenzhen and SMIC Energy Technology (Shanghai) Corporation, and each of their direct and indirect parent companies. He is also a director of SMIC Japan Corporation, SMIC, Americas, SilTech Semiconductor (Hong Kong) Corporation Limited, Admiral Investment Holdings Limited and Magnificent Tower Limited, Semiconductor Manufacturing International (AT) Corporation and its two wholly owned subsidiaries including SMIC Chengdu. Dr. Chang has more than 30 years of semiconductor experience in foundry operations, wafer fabrication and research and development. From 1998 to 1999, Dr. Chang was President of Worldwide Semiconductor Manufacturing Corp., or WSMC, after joining the company in 1997. Prior to joining WSMC, Dr. Chang worked for 20 years at Texas Instruments Incorporated, where he helped build and manage the technology development and operations often semiconductor fabs and integrated circuit operations in the United States, Japan, Singapore, Italy and Taiwan. Dr. Chang received a PhD in Electrical Engineering from Southern Methodist University and a master s degree in Engineering Science from the State University of New York. In December 2003, Dr. Chang was selected by the China Center of Information Development as one of the ten China IT Economic People of 2003 for his role in influencing and contributing to the development of China s information technology industry. In September 2004, Dr. Chang received The Magnolia Silver Award. The award recognizes Dr. Chang s contributions to Shanghai s economy, social development and international interchange and cooperation. In April 2005, Dr. Chang received The International Scientific and Technological Cooperation Award of The People s Republic of China. In February 2006, he was elected the 2004-2005 China Semiconductor Industry Leader. Semiconductor International China named Dr. Chang its Fab Person of the Year in 2007, and SEMI China recognized him with its 2008 Industry Outstanding Contribution award. Semiconductor International China named Dr. Chang its Fab Person of the Year in 2007, and SEMI China recognized him with its 2008 Industry Outstanding Contribution award.

Non-executive Director

Zhou Jie has been a Director since 2009. Mr. Zhou is an executive director and the executive deputy CEO of Shanghai Industrial Holdings Limited. He is also an executive director and the executive vice president of Shanghai Industrial Investment (Holdings) Co. Ltd., and a director of Shanghai Industrial Pharmaceutical Investment Co. Ltd., Chia Tai Qingchunbao Pharmaceutical Co. Ltd., Shanghai Sunway Biotech Co. Ltd. and The Wing Fat Printing Co. Ltd., a non-executive director of Shanghai Fudan-Zhangjiang Bio-Pharmaceutical Co. Ltd. and the chairman of the supervisory committee of Bright Dairy and Food Co. Ltd. Mr. Zhou graduated from Shanghai Jiaotong University with a master s degree in management science and engineering. He was the deputy general manager of the investment banking head office of Shanghai Wanguo Holdings Ltd. (now Shenyin & Wanguo Securities Co. Ltd.), and had held the positions of the chairman and general manager of Shanghai S.I. Capital Co. Ltd. He has over 10 years experience in investment banking and capital markets operation.

Wang Zheng Gang has been a Director since 2007 and he is currently the alternate director to Mr. Zhou Jie. Mr. Wang is the chief representative of the Shanghai Representative Office of Shanghai Industrial Holdings Limited and chairman of SIIC Management (Shanghai) Ltd. He is also the vice chairman of Bright Dairy and Food Co. Ltd, a director of Shanghai Urban Development (Holdings) Co. Ltd., Shanghai Hu-Ning Expressway (Shanghai Section) Co. Ltd. and Shanghai SIIC South Pacific Hotel Co. Ltd. He was the head of Shanghai Dongfeng Rubber No. 2 Factory, Principal of Shanghai Dongfeng Farm, vice chairman and general manager of Shanghai Agricultural Industrial and Commercial Corp. Ltd. and a director and general manager of SIIC Africa Enterprise Ltd. and general manager of the enterprise management department of Shanghai Industrial Investment (Holdings) Co. Ltd. He graduated from the School of Management of Fudan University with a master s degree in economics and has over 31 years experience in enterprise management.

Independent Non-executive Directors

Tsuyoshi Kawanishi has been a Director since 2001 and is also the chairman of SMIC Japan Corporation. Mr. Kawanishi has more than 50 years of experience in the electronics industry with Toshiba Corporation, where he served as, among other positions, senior executive vice president and senior advisor. Mr. Kawanishi currently serves on the board of directors of Asyst Technologies, Inc., FTD Technology Pte. Ltd. and T.C.S. Japan, and acts as an

advisor to Accenture Ltd., Kinetic Holdings Corporation and a number of private companies. Mr. Kawanishi is also the chairman of the Society of Semiconductor Industry Seniors in Japan and the Chairman of the SIP Consortium of Japan**.**

Lip-Bu Tan has been a Director since 2002 and is a director of SMIC Tianjin. Mr.Tan is the Founder and Chairman of Walden International, an international venture capital firm founded in 1984. Mr. Tan is also President and Chief Executive Officer of Cadence Design Systems, Inc. Mr. Tan is currently a director of Cadence Design Systems Inc., Flextronics International Ltd., Global Semiconductor Alliance and SINA Corporation and several other private companies. He holds an M.S. in Nuclear Engineering from the Massachusetts Institute of Technology, an M.B.A. from the University of San Francisco and a B.S. from Nanyang University, Singapore.

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Jiang Shang Zhou has been a Director since 2006. Mr. Jiang is currently a committee member of the Shanghai Municipal Standing Committee of Chinese People s Political Consultative Conference, a specialized committee member of the Shanghai Municipal Advisory Committee for Descion-making, and an officer of and a director commissioner of Shanghai State Owned Assets Planning and Investment Committee. Mr. Jiang was also the deputy secretary general of Shanghai Government, officer of the Shanghai Chemical Industrial District Leader Team Office, officer of Shanghai International Automobile City Leader Team Office and officer of the Shanghai Fuel Cell Electric Vehicles (863 major project) Leader Team Office. Mr. Jiang received his bachelor s degree from Tsinghua University in telecommunications and his master s and doctorate degree in information technology from the department of electrical engineering of the Swiss Federal Institute of Technology Zurich Communication System Group.

Edward S Yang has been a Director since 2009. Since 1961, Professor Yang has been involved in semiconductors and IC as an engineer, research scientist, and educator. Professor Yang received his Master of Science in Electrical Engineering from Oklahoma State University in 1961 and PhD from Yale University in 1966. Professor Yang was the Chairman of the Department of Electrical Engineering at Columbia University from 1986 to 1990 and from 1992 to 1995. Under his leadership, research laboratories in Telecommunications, Microelectronics, Photonics, and IC at Columbia University were established. Professor Yang joined the University of Hong Kong (HKU) as Chair Professor of Microelectronics in 1997. At HKU, he founded the Hong Kong Jockey Club MRI Engineering Centre and E-Business Technology Institute. Professor Yang was appointed as the chief executive officer of the Hong Kong Applied Science and Technology Research Institute (ASTRI) in 2007. At ASTRI, he initiated the new Industrial Collaboration Program and Internship for fresh university graduates. In 2009, he stepped down as ASTRI s chief executive officer but remains as its senior advisor. Professor Yang has 7 US patents and published more than 200 journal papers and two popular textbooks that were translated into Chinese, Japanese, Italian and Korean. He is a fellow of the Institute of Electrical and Electronics Engineers. Professor Yang also served as an independent non-executive director of Fulbond Holdings Limited (Stock Code: 1041), the shares of which are listed on the Main Board of HKSE, from March 30, 2001 to January 3, 2007.

Senior Management

Morning Wu joined our company as Associate Vice President of Finance and Accounting in January 2003 and was appointed as Acting Chief Financial Officer and Chief Accounting Officer on March 28, 2005. Ms. Wu has over 27 years of experience in the investment and finance field. Prior to joining us, Ms. Wu held management positions with First Taiwan Securities Inc. and Grand Cathay Securities Co. Ltd. Her responsibilities at these companies included strategic planning, mergers & acquisitions and designing and monitoring risk management systems. She holds a license for Accounting and Auditor with the Senior Civil Service Examination of Taiwan. Ms. Wu obtained a bachelor s degree in Accounting from the National Chengchi University, Taiwan and received a master s degree in Accounting from the National Taiwan University.

Marco Mora joined our company in 2000 as Vice President of Operations and was named the Chief Operating Officer in November 2003. Mr. Mora has more than 22 years of experience in the semiconductor industry. Prior to joining us, Mr. Mora held management positions with STMicroelectronics N.V., Texas Instruments Italia S.p.A, Micron Technology Italia S.p.A and WSMC. Mr. Mora received a master s degree in Physics from the University of Milan.

Chiou-Feng Chen joined the Company in 2006 as Vice President of Special Technology Development and was appointed as Vice President of Corporate Marketing & Sales in 2009. Mr. Chen has over 20 years of experience in the semiconductor industry. Prior to Joining SMIC, Mr. Chen held various management positions with Taiwan Semiconductor Manufacturing Company, SYNTEK Design Technology Ltd., Silicon Storage Technology, Inc., Integrated Memory Technologies, and Inc., Actrans System Inc. Mr. Chen obtained a master degree and a doctorate degree in Electronic Engineering from National Chiao-Tung University, Taiwan.

Company Secretary

Anne Wai Yui Chen joined our company in 2001 and is our Hong Kong Representative, Company Secretary and Chief Compliance Officer. Ms. Chen is admitted as a solicitor in Hong Kong, England and Wales and Australia and was admitted as an advocate and solicitor in Singapore. She had served as a deputy adjudicator of the Small Claims Tribunal in Hong Kong in 1999 and is the President of the Hong Kong Federation of Women Lawyers from 2000 to

2002 and since 2008. Prior to joining us in 2001, she had been a practicing solicitor in Hong Kong since 1987.
Except as described below in Item 10 - Additional Information Material Contracts Share Purchase Agreement with Datang , no shareholder has a contractual right to designate a person to be elected to our board of directors.

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There are no family relationships among any of our directors and executive officers, including our founder.

Director and Executive Compensation

The aggregate cash compensation that we paid to all of our executive officers as of December 31, 2008 for services rendered to us and our subsidiaries during 2008 was approximately US$914,073. Of this amount, we paid our president and chief executive officer US$218,398 in salary, housing allowances, other allowances and benefits in kind in 2008. We currently do not provide cash compensation to directors that are not employees.

We do not provide pension, retirement or similar benefits to our executive officers and directors except statutorily required benefits.

In 2008, the Board did not grant options or restricted share units to any director as compensation for their service on the Board.

On April 25, 2004, the compensation committee approved a profit-sharing plan for the benefit of our employees, including our executive officers. Under our profit-sharing plan, a participant who is an employee of the company at the end of a fiscal quarter will be eligible to receive a percentage of our profits for that quarter. No compensation was received by our executive officers in 2006, 2007 and 2008 as a result of their participation in this plan.

Board Practices

Board of Directors

As of December 31, 2008, our board of directors consisted of seven directors. Directors may be elected to hold office until the expiration of their respective terms upon a resolution passed at a duly convened shareholders meeting by holders of a majority of our outstanding shares being entitled to vote in person or by proxy at such meeting. Our board is divided into three classes with no more than one class eligible for re-election at any annual shareholders meeting. The Class I directors were elected for a term of three years beginning from June 2, 2008, which is the date of the 2008 annual general meeting of our shareholders. The Class II directors were elected for a term of three years beginning from May 30, 2006, the date of the 2006 annual general meeting our shareholders. The Class III directors were elected for a term of three years beginning from May 23, 2007, which is the date of the 2007 annual general meeting of our shareholders.

The following table sets forth the names and classes of our current directors:

Class I	Class II	Class III
Richard Ru Gin Chang	Lip-Bu Tan	Tsuyoshi Kawanishi
Edward S Yang	Jiang Shang Zhou	Yang Yuan Wang
		Zhou Jie
		Wang Zheng Gang (alternate director to Zhou Jie)

Please see Item 7 Related Party Transactions Indemnification Agreements and Service Contracts for a description of the service contracts we have entered into with our directors.

Committees of Our Board of Directors

Our board of directors has an audit committee and a compensation committee. The composition and responsibilities of these committees are described below.

Audit Committee. As of December 31, 2008, the members of the audit committee were Lip-Bu Tan (chairman of audit committee), Jiang Shang Zhou and Yang Yuan Wang. None of the members of the audit committee has been an executive officer or employee of the company or any of its subsidiaries. See Related Party Transactions for a description of transactions between us and the members of the audit committee. In addition to acting as audit committee member of SMIC, Mr. Lip-Bu Tan currently also serves on the audit committee of two other publicly traded companies, namely SINA Corporation and Flextronics International Ltd. In accordance with section 303A.07(a) of the Listed Company Manual of the New York Stock Exchange, the Board considered and determined that such simultaneous service would not impair the ability of Mr. Tan to effectively serve on our audit committee.

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The responsibilities of the audit committee include, among other things:

- making recommendations to the board of directors concerning the appointment, reappointment, retention, evaluation, oversight and termination of compensating and overseeing the work of our independent auditor, including reviewing the experience, qualifications and performance of the senior members of the independent auditor team, and pre-approving all non-audit services to be provided by our independent auditor;
- approving the remuneration and terms of engagement of our independent auditor;
- reviewing reports from our independent auditor regarding its internal quality-control procedures and any material issues raised in the most recent review or investigation of such procedures and regarding all relationships between us and the independent auditor;
- pre-approving the hiring of any employee or former employee of our independent auditor who was a member of the audit team during the preceding two years;
- reviewing our annual and interim financial statements, earnings releases, critical accounting policies and practices used to prepare financial statements, alternative treatments of financial information, the effectiveness of our disclosure controls and procedures and important trends and developments in financial reporting practices and requirements;
- reviewing the planning and staffing of internal audits, the organization, responsibilities, plans, results, budget and staffing of our internal audit department and the quality and effectiveness of our internal controls;
- reviewing our risk assessment and management policies;
- reviewing any legal matters that may have a material impact and the adequacy and effectiveness of our legal and regulatory compliance procedures;
- establishing procedures for the treatment of complaints received by us regarding accounting, internal accounting controls, auditing matters, potential violations of law and questionable accounting or auditing matters; and
- obtaining and reviewing reports from management, our internal auditor and our independent auditor regarding compliance with applicable legal and regulatory requirements.

During 2008, the audit committee reviewed:

- the financial reports for the year ended December 31, 2007 and the six month period ended June 30, 2008;
- the quarterly earnings releases and any updates thereto;
- the report and management letter submitted by our outside auditors summarizing the findings of and recommendations from their audit of our financial reports;
- our budget for 2008;
- the findings and recommendations of our outside consultants regarding our compliance with the requirements of the Sarbanes-Oxley Act;
- the effectiveness of our internal control structure in operations and financial reporting integrity and compliance with applicable laws and regulations in collaboration with the Internal Audit Department and reported to the Board;
- the findings of our risk management committee which assesses risks relating to the company and those of the compliance office, which monitors our compliance with the corporate governance code and insider trading policy;
- the audit fees for our outside auditors; and
- our outside auditors engagement letters

The audit committee reports its work, findings, and recommendations to the board of directors during each quarterly board meeting.

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The audit committee meets in person at least on a quarterly basis and on such other occasions as may be required to discuss and vote upon significant issues affecting the audit policy of the company. The regular meeting schedule for a year is planned in the preceding year. The Company s Secretary assists the chairman of the audit committee in preparing the agenda for meetings and assists the audit committee in complying with relevant rules and regulations. The relevant papers for the audit committee meetings are dispatched to audit committee members in accordance with applicable rules and regulations governing the company. Members of the audit committee may include matters for discussion in the agenda if the need arises. Upon the conclusion of the audit committee meeting, minutes are circulated to the members of the audit committee for their comment and review prior to their approval of the minutes at the following or the subsequent audit committee meeting.

At each quarterly audit committee meeting, the audit committee reviews with the acting chief financial officer and our outside auditors, the financial statements for the financial period and the financial and accounting principles, policies and controls of the company and its subsidiaries. In particular, the Committee discusses (i) the changes in accounting policies and practices, if any; (ii) the going concern assumptions, (iii) compliance with accounting standards and applicable rules and other legal requirements in relation to financial reporting and (iv) our internal controls relating to financial reporting. Upon the recommendation of the audit committee, the Board will approve the financial statements.

Compensation Committee. As of December 31, 2008, the members of our compensation committee were Lip-Bu Tan (chairman of compensation committee) and Tsuyoshi Kawanishi. Effective as of February 5, 2009, Zhou Jie is also a member of the compensation committee. None of these members of the compensation committee has been an executive officer or employee of the company or any of its subsidiaries. See Related Party Transactions for a description of transactions between us and the members of the compensation committee.

The responsibilities of the compensation committee include, among other things:

- approving and overseeing the total compensation package for our executive officers and any other officer, evaluating the performance of and determining and approving the compensation to be paid to our chief executive officer and reviewing the results of our chief executive officer s evaluation of the performance of our other executive officers;
- reviewing and making recommendations to our board of directors with respect to director compensation, including equity-based compensation;
- administering and periodically reviewing and making recommendations to the board of directors regarding the long-term incentive compensation or equity plans made available to the directors, employees and consultants;
- reviewing and making recommendations to the board of directors regarding executive compensation philosophy, strategy and principles and reviewing new and existing employment, consulting, retirement and severance agreements proposed for the company s executive officers; and
- ensuring appropriate oversight of our human resources policies and reviewing strategies established to fulfill our ethical, legal and human resources responsibilities.

In 2007, the compensation committee reviewed the total compensation package for Richard Ru Gin Chang , who is the president and chief executive officer, and awarded Richard Ru Gin Chang an annual salary of US$157,477. No changes were made to Richard Ru Gin Chang s annual salary for 2008.

In addition to reviewing the remuneration of the non-executive directors and the members of our management, the compensation committee reviewed and approved the granting of stock options and restricted share units pursuant to the terms of the Option Plans in 2008. The compensation committee also reviewed and approved on at least a quarterly basis any exception to the compensation guidelines and leave of absence policy of the Company.

The compensation committee reports its work, findings and recommendations to the board of directors during each quarterly board meeting.

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The compensation committee meets in person at least on a quarterly basis and on such other occasions as may be required to discuss and vote upon significant issues affecting our compensation policy. The regular meeting schedule for a year is planned in the preceding year. The Company s Secretary assists the chairman of the compensation committee in preparing the agenda for meetings and assists the compensation committee in complying with relevant rules and regulations. The relevant papers for the compensation committee meeting are distributed to compensation committee members in accordance with relevant rules and regulations applicable to us. Members of the compensation committee may include matters for discussion in the agenda if the need arises. Upon the conclusion of the compensation committee meeting, minutes are circulated to the members of the compensation committee for their comment and review prior to their approval of the minutes at the following or a subsequent compensation committee meeting.

Employees

The following table sets forth, as of the dates indicated, the number of our employees serving in the capacities indicated:

	As of December 31,		
Function	**2006**	**2007**	**2008**
Managers	871	916	1,015
Professionals[(1)]	3,790	4,096	4,465
Technicians	4,804	4,806	4,837
Clerical staff	583	287	281
Total[(2)]	10,048	10,105	10,598

(1) Professionals include engineers, lawyers, accountants and other personnel with specialized qualifications, excluding managers.

(2) Includes 275, 276 and 50 temporary and part-time employees in 2006, 2007 and 2008, respectively.

The following table sets forth, as of the dates indicated, a breakdown of the number of our employees by geographic location:

	As of December 31,		
Location of Facility	**2006**	**2007**	**2008**

Shanghai	6,400	6,292	6,632
Beijing	1,827	1,877	1,674
Tianjin	1,073	874	958
Chengdu	715	1,023	1,259
Shenzhen			33
United States	16	18	16
Europe	7	8	11
Japan	7	9	8
Hong Kong	3	4	7
Total	10,048	10,105	10,598

Our employees are not covered by any collective bargaining agreements.

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Share Ownership

The table below sets forth the ordinary shares beneficially owned by each of our directors and options to purchase ordinary shares as of May 31, 2009:

	Current	Options to Purchase Ordinary Shares		Awards of Restricted
Name of Director	**Shareholding**	**Number of Options**	**Exercise Price**	**Share Units**
Richard Ru Gin Chang	81,219,500(1)(2)	16,600,000(3)	US$ 0.0348-US$0.31	500,000
Tsuyoshi Kawanishi		3,500,000(3)	US$ 0.0348 -US$0.22	
Lip-Bu Tan		2,000,000(3)	US$ 0.0348-US$0.22	
Yang Yuan Wang		2,000,000(3)	US$ 0.0348-US$0.22	
Jiang Shang Zhou		1,000,000(3)	US$ 0.0348	
Edward S Yang	750,000	1,000,000(3)	US$ 0.0348	
Zhou Jie				
Wang Zheng Gang				
Henry Shaw (former independent non-executive director who resigned as of January 13, 2009)				

Notes:

1. Pursuant to a Charitable Pledge Agreement dated December 1, 2003, Richard Ru Gin Chang and his spouse, Scarlett K. Chang (collectively, the Donors) have pledged to transfer 10,000,000 of such ordinary shares as a charitable gift to The Richard and Scarlett Chang Family Foundation, a Delaware nonprofit nonstock corporation organized exclusively for religious,

charitable, scientific, literary and education purposes within the meaning of Section 501(c)(3) of the US Internal Revenue Code of 1986, as amended, such transfer to be made in full at or prior to the death of the surviving Donor. In addition, 2,639,550 of such ordinary shares are jointly held by Richard Ru Gin Chang and his spouse, Scarlett K. Chang.

2. 20,000,000 of the ordinary shares held as a corporate interest. These ordinary shares are held by Jade Capital Company, LLC, a Delaware limited liability company (the LLC), of which Richard Ru Gin Chang and his spouse, Scarlett K. Chang (collectively, the Members), are the sole members. It is the current intent of the Members that all or a portion of the net income of the LLC be used for philanthropic purposes, including but not

limited to contributions to charitable organizations that are tax-exempt under Section 501(c)(3) of the US Internal Revenue Code of 1986, as amended.

3. Each of Richard R. Chang, Tsuyoshi Kawanishi, Lip-Bu Tan, Yang Yuan Wang, Jiang Shang Zhou and Edward S Yang were granted an option to purchase 1,000,000 Ordinary Shares at a price per Ordinary Shares of US$0.0348. These options will be fully vested on February 17, 2011 and will expire on the earlier of February 17, 2019 or 120 days after termination of the director s service to the Board. As at May 31, 2009, these options have not been exercised.

The share holdings set forth above excludes shares beneficially owned by entities affiliated with our directors. Each of our directors disclaims beneficial ownership of the shares beneficially owned by such affiliated entity, except to the extent of such director s pecuniary interest therein as disclosed above.

The exercise price for our options is denominated in Hong Kong dollars. This annual report translates the Hong Kong dollar exercise prices for our options into U.S. dollars based on exchange rates that were in effect as of the applicable option grants dates

On July 11, 2002, the compensation committee issued Mr. Kawanishi an option to purchase 500,000 ordinary shares pursuant to the terms of the 2001 Stock Option Plan. This option will expire on July 11, 2012. On January 15, 2004,

the board issued him an option to purchase 1,000,000 ordinary shares pursuant to the terms of the 2001 Stock Option Plan. This option will expire on January 15, 2014. The exercise prices of the options are US$0.05 and US$0.10, respectively.

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On November 10, 2004, the Board granted to each independent non-executive director and non-executive director as of such date, an option to purchase 500,000 ordinary shares at a price per ordinary share of US$0.22. These options vested on March 19, 2005 and will expire on November 10, 2009. Lai Xing Cai (who resigned as non-executive director on February 6, 2006) has declined this option. As of December 31, 2008, no director has exercised such options. The option granted to Mr. Yen-Pong Jou (who retired as an independent non-executive director at the 2006 AGM) lapsed and cancelled on September 27, 2006. The options granted to Dr Albert Yu (who resigned as an Independent Non-executive Director on June 2, 2008) lapsed on September 30, 2008. The options granted to Dr Ta-Lin Hsu (who resigned as an Independent Non-executive Director on September 30, 2008) lapsed on January 29, 2009. The options granted to Mr. Henry Shaw (who resigned as an Independent Non-executive Director on January 13, 2009) will lapse on May 13, 2009.

On April 7, 2004, the compensation committee issued to Richard Ru Gin Chang an option to purchase 100,000 ordinary shares. The exercise price per ordinary share underlying the option was US$0.31. The option will expire on April 7, 2014. On May 11, 2005, the compensation committee issued to Richard Ru Gin Chang an option to purchase 15,000,000 ordinary shares and an award of 2,000,000 restricted share units. The exercise price per ordinary share underlying the option is US$0.196. The option and the award of restricted share units will expire on May 11, 2015. As of December 31, 2008, 1,500,000 RSUs had been issued and vested and 500,000 RSUs had been vested but remained unissued.

On September 29, 2006, the Board granted to each director an option to purchase 500,000 ordinary shares at a price per ordinary share of US$0.132. These options were vested as to 50% on each of May 30, 2007 and May 30, 2008 respectively and will expire on the earlier of September 29, 2016 or 120 days after termination of the director s service to the Board. As of December 31, 2008, these options have not been exercised. Fang Yao (who resigned as non-executive director on August 30, 2007) and Jiang Shang Zhou have declined such options. The options granted to Dr.Albert Yu (who resigned as an Independent Non-executive Director on June 2, 2008) lapsed on September 30, 2008. The options granted to Dr. Ta-Lin Hsu (who resigned as an Independent Non-executive Director on September 30, 2008) lapsed on January 29, 2009. The options granted to Mr. Henry Shaw (who resigned as an Independent Non-executive Director on January 13, 2009) will lapse on May 13, 2009.

In 2007, the Board did not grant options or restricted share units to any director as compensation for their service on the Board.

In 2008, the Board did not grant options or restricted share units to any director as compensation for their service on the Board.

On February 17, 2009, the Board granted an option to purchase 1,000,000 ordinary shares to each of Richard R. Chang, Tsuyoshi Kawanishi, Lip-Bu Tan, Yang Yuan Wang, Jiang Shang Zhou and Edward S Yang as compensation for their service on the Board.

The compensation committee has issued each of our executive officers options to purchase ordinary shares pursuant to our 2001 Regulation S Stock Option Plan, 2001 Regulation S Preference Shares Stock Plan and the 2004 Stock Option Plan and restricted share units that represent rights to receive ordinary shares pursuant to our 2004 Equity Incentive Plan. The exercise price of the options range from US$0.01 to US$0.35. The options expire between November 10, 2009 and September 29, 2016. The restricted share units expire between July 26, 2015 and September 29, 2016. The majority of the options and restricted share units are subject to a four-year vesting period. Each executive officer owns less than 1% of the total outstanding shares of the company.

2001 Stock Plan and 2001 Regulation S Stock Plan

On March 28, 2001, our board of directors and shareholders adopted our 2001 Stock Plan and our 2001 Regulation S Stock Plan. Under these plans, our directors, employees and consultants are eligible to acquire ordinary shares pursuant to options. At the time of adoption, 250,000,000 post-split ordinary shares were reserved for issuance under the 2001 Stock Plan and 470,000,000 post-split ordinary shares were reserved for issuance under the 2001 Regulation S Stock Plan. On August 27, 2003, our shareholders approved an increase in the number of authorized shares reserved under the plans of 3,438,900 post-split ordinary shares, increasing the total number of authorized shares reserved under the plans to 723,438,900 post-split ordinary shares. On August 27, 2003, September 22, 2003 and December 4, 2003, our shareholders approved additional increases in the number of shares reserved under our

2001 Regulation S Stock Plan of up to 325,000,000, 21,499,990 and 235,089,480 post-split ordinary shares, respectively, which amounts were to be adjusted from time to time to equal 10% of the post-split ordinary shares issuable upon the conversion of all Series C convertible preference shares and Series D convertible preference shares then outstanding. As of December 31, 2008, there were 998,675,840 post-split ordinary shares authorized for issuance under the plans, 285,423,228 post-split ordinary shares subject to outstanding options under the plans and 398,867,596 post-split ordinary shares outstanding from the exercise of options granted under the plans. These plans terminate on December 4, 2013 but may be terminated earlier by our board of directors.

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Stock options granted under the 2001 Stock Plan may be incentive stock options, or ISOs, which are intended to qualify for favorable U.S. federal income tax treatment under the provisions of Section 422 of the U.S. Internal Revenue Code of 1986, as amended, or U.S. Internal Revenue Code, or non-qualified stock options, or NSOs, which do not so qualify. Stock options granted under the 2001 Regulation S Stock Plan are NSOs. The aggregate fair market value of the ordinary shares represented by any given optionee s ISOs that become exercisable in any calendar year may not exceed US$100,000. Stock options in excess of this limit are treated as NSOs.

The board of directors, the compensation committee, and the non-executive option grant committee administer the 2001 Stock Plan and 2001 Regulation S Stock Plan. The compensation committee selected the eligible persons above a certain compensation grade to whom options were granted and determined the grant date, amounts, exercise prices, vesting periods and other relevant terms of the stock options, including whether the options will be ISOs or NSOs. The non-executive option grant committee selected the eligible persons below a certain compensation grade to whom options were granted and determined the grant date, amounts, exercise prices, vesting periods and other relevant terms of stock options within parameters established by the compensation committee and subject to compensation committee ratification. The exercise price of ISOs granted under the 2001 Stock Plan and NSOs granted to residents of California under the 2001 Stock Plan may not be less than 100% and 85%, respectively, of the fair market value of our ordinary shares on the grant date. The exercise price of NSOs not granted to residents of California under either our 2001 Stock Plan or our 2001 Regulation S Stock Plan can be determined by the board of directors, the compensation committee or the non-executive option grant committee in their discretion.

Stock options granted under the 2001 Stock Plan and 2001 Regulation S Stock Plan may be exercised at any time after they vest, and, in certain instances, prior to vesting. Shares purchased when an option is exercised prior to vesting are subject to our right of repurchase to the extent unvested in the event of the termination of service of the optionee. In the event of the termination of service of an optionee, the unvested portion of a stock option is forfeited and the vested portion terminates six months after a termination of service due to the death or permanent disability of the optionee or 30 days after termination of service for any other reason or such longer periods as may be provided for in option agreements with our optionees. Stock options are generally not transferable during the life of the optionee.

In the event of a change of control (as defined in the plans) or a merger of our company, each outstanding stock option may be assumed or an equivalent stock option or right may be substituted by the successor corporation. In the event that no such substitution or assumption occurs, the outstanding stock options will automatically vest and become exercisable for a period of 15 days, after which the stock options will terminate.

We have not issued stock options under the 2001 Stock Plan or the 2001 Regulation S Stock Plan since the completion of the global offering.

2001 Preference Shares Stock Plan and 2001 Regulation S Preference Shares Stock Plan

On April 12, 2001, our board of directors and shareholders adopted our 2001 Preference Shares Stock Plan and our 2001 Regulation S Preference Shares Stock Plan. Under these plans, our directors, employees and consultants were eligible to acquire Series A convertible preference shares prior to the completion of the global offering and ordinary shares upon or following the completion of the global offering, pursuant to options. At the time of adoption, 16,000,000 Series A preference shares and ten times that number of ordinary shares (on a post-split basis) were reserved for issuance under the 2001 Preference Shares Stock Plan, and 20,000,360 Series A convertible preference shares and ten times that number of ordinary shares (on a post-split basis) were reserved for issuance under the 2001 Regulation S Preference Shares Stock Plan. On August 19, 2002, our shareholders approved an increase in the number of shares issuable under the plans of 18,000,180 Series A convertible preference shares, increasing the total number of authorized shares reserved under the plans to 54,000,540 Series A convertible preference shares. On August 27, 2003, our shareholders approved a net decrease in the number of shares issuable under the plans of 343,890 Series A convertible preference shares, decreasing the total number of authorized shares reserved under the plans to 53,656,650 Series A convertible preference shares. Upon the conversion of our preference shares into ordinary shares in connection with the global offering, options granted under the 2001 Preference Shares Stock Plan and the 2001 Regulation S Preference Shares Stock Plan converted into options to purchase ordinary shares. As of December 31, 2008, there were 52,344,600 ordinary shares subject to outstanding options under the plans, and there were 400,747,130 ordinary shares outstanding from the exercise of options granted under the plans. Our board of directors

has elected not to grant any further options under these plans.

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Stock options granted under the 2001 Preference Shares Stock Plan may be ISOs or NSOs. Stock options granted under the 2001 Regulation S Preference Shares Stock Plan are NSOs. The aggregate fair market value of the shares represented by any given optionee s ISOs that become exercisable in any calendar year may not exceed US$100,000. Stock options in excess of this limit are treated as NSOs.

The board of directors, the compensation committee and the non-executive option grant committee administer the 2001 Preference Shares Stock Plan and 2001 Regulation S Preference Shares Stock Plan. The compensation committee selected the eligible persons above a certain compensation grade to whom options were granted and determined the grant date, amounts, exercise prices, vesting periods and other relevant terms of the stock options, including whether the options will be ISOs or NSOs. The non-executive option grant committee selected the eligible persons below a certain compensation grade to whom options were granted and determined the grant date, amounts, exercise prices, vesting periods and other relevant terms of stock options within parameters established by the compensation committee and subject to compensation committee ratification. The exercise price of ISOs granted under the 2001 Preference Shares Stock Plan and NSOs granted to residents of California under the 2001 Preference Shares Stock Plan may not be less than 100% and 85%, respectively, of the fair market value of our Series A convertible preference shares on the grant date. The exercise price of NSOs not granted to California residents under either our 2001 Preference Shares Stock Plan or our 2001 Regulation S Preference Shares Stock Plan can be determined by the board of directors, the compensation committee or the non-executive option grant committee in their discretion.

Stock options granted under the 2001 Preference Shares Stock Plan and 2001 Regulation S Preference Shares Stock Plan may be exercised at any time after they vest, and, in certain instances, prior to vesting. Shares purchased when an option is exercised prior to vesting are subject to our right of repurchase to the extent unvested in the event of the termination of service of the optionee. In the event of the termination of service of an optionee, the unvested portion of a stock option is forfeited and the vested portion terminates six months after a termination of service due to the death or permanent disability of the optionee or 30 days after termination of service for any other reason or such longer periods as may be provided for in option agreements with our optionees. Stock options are generally not transferable during the life of the optionee.

In the event of a change of control (as defined in the plans) or a merger of our company, each outstanding stock option may be assumed or an equivalent stock option or right may be substituted by the successor corporation. In the event that no such substitution or assumption occurs, the outstanding stock options will automatically vest and become exercisable for a period of 15 days, after which the stock options will terminate.

We have not issued stock options under the 2001 Preference Shares Stock Plan or the 2001 Regulation S Preference Shares Stock Plan since the completion of the global offering.

2004 Global Equity Incentive Compensation Program

The Company s shareholders adopted the Stock Option Plan, the EIP and the Employee Stock Purchase Plan (the ESPP , together with the Stock Option Plan and the EIP, the Option Plans) to attract and retain its employees.

Stock Option Plan

The following is a summary of the principal terms of the Stock Option Plan conditionally adopted by the Company by way of shareholders resolution dated February 16, 2004 and Directors resolutions passed on January 16, 2004. Adoption of the Stock Option Plan took effect on March 18, 2004 being the first date of dealings in the ordinary shares.

Summary of the terms of the Stock Option Plan

(a) Purpose of the Stock Option Plan

The purposes of the Stock Option Plan are to attract, retain and motivate employees and Directors of, and other service providers to the Company, to provide a means, on and after the Global Offering, of compensating them through the grant of stock options for their contribution to the Company s growth and profits, and to allow such employees, Directors and service providers to participate in such growth and profitability.

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(b) Who may join

The Compensation Committee may, at its discretion, invite any employee, officer or other service provider of (including, but not limited to, any professional or other adviser of, or consultant or contractor to) the Company whether located in China, the United States or elsewhere to take up options to subscribe for ordinary shares at a price calculated in accordance with sub-paragraph (e) below. The Compensation Committee may also grant stock options to a Director who is not an employee of the Company (Non Employee Director).

(c) Stock Options

Stock options granted under the Stock Option Plan (Stock Options) shall entitle a participant (Participant) of the Stock Option Plan to purchase a specified number of ordinary shares or ADSs (the Plan Shares) during a specified period at a price calculated in accordance with sub-paragraph (e) below. Three types of Stock Options may be granted under the Plan, an Incentive Stock Option, a Non-Qualified Stock Option or a Director Option. An Incentive Stock Option is a stock option that falls within the meaning of Section 422 of the U.S. Internal Revenue Code of 1986 and may only be granted to employees of the Company and its subsidiaries from time to time. A Non-Qualified Stock Option is a stock option that is not an Incentive Stock Option. A Director Option is a Non-Qualified Stock Option granted to a Non-Employee Director.

The Company shall issue an Award Document to each Participant of the Stock Option Plan who is granted a Stock Option. The Award Document shall set out the terms and provisions of the grant of a Stock Option to a Participant including applicable vesting dates or the attainment of specified performance goals (as determined by the Compensation Committee or the Administrator (as defined below), as the case may be) by the Participant. The Company may allow a Participant to exercise his or her Stock Options prior to vesting, provided the Participant agrees to enter into a repurchase agreement in respect of the Stock Option with the Company. The Compensation Committee may also (i) accelerate the vesting of a Stock Option, (ii) set the date on which any Stock Option may first become exercisable, or (iii) extend the period during which a Stock Option remains exercisable, except that no Stock Options may be exercised after the tenth anniversary of the date of grant.

The Stock Option Plan does not provide for any payment upon application or acceptance of an option.

(d) Administration of the Stock Option Plan

The Compensation Committee shall be responsible for the administration of the Stock Option Plan. Its responsibilities include granting Stock Options to eligible individuals, determining the number of Plan Shares subject to each Stock Option, and determining the terms and conditions of each Stock Option.

The Compensation Committee is not obliged to grant Stock Options to Participants in uniform terms. Accordingly, the terms and conditions which may be imposed may vary between Participants. Any determination by the Compensation Committee in relation to the carrying out and administering of the Stock Option Plan shall be final and binding. No member of the Compensation Committee shall be liable for any action or determination made in good faith, and the members of the Compensation Committee shall be entitled to indemnification and reimbursement in the manner provided in the Articles.

The Compensation Committee may delegate some or all of its authority under the Stock Option Plan to an individual or individuals (each an Administrator) who may either be one or more of the members of the Committee or one or more of the officers of the Company. An individual s status as an Administrator shall not affect his or her eligibility to participate in the Stock Option Plan. The Compensation Committee shall not delegate its authority to grant Stock Options to executive officers of the Company.

(e) Exercise Price

The exercise price per Plan Share purchasable under a Stock Option shall be fixed by the Committee at the time of grant or by a method specified by the Compensation Committee at the time of grant, but in no event shall be less than the Fair Market Value of a Plan Share on the date such Stock Option is granted.

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The Fair Market Value of a Share will be the higher of (i) the closing price of the ordinary shares on the HKSE s daily quotation sheet on the applicable date of grant (which must be a business day), and (ii) the average closing price of the ordinary shares on the HKSE (as stated in the relevant daily quotation sheets of the HKSE) for the five business days immediately preceding the date of grant.

The Fair Market Value of the ADSs shall be the highest of (i) the closing price of the ADSs on the NYSE on the applicable date of grant, and (ii) the average closing price of the ADSs on the NYSE for the five business days immediately preceding the date of grant.

(f) Limit of the Stock Option Plan

The number of ordinary shares that may be issued under the Stock Option Plan and the ESPP (the Global Limit) shall not exceed ten percent of the issued and outstanding ordinary shares immediately following the closing of the Global Offering (i.e., 1,317,000,000).

The number of ordinary shares which may be issued pursuant to any outstanding Stock Options granted and yet to be exercised under the Stock Option Plan and all outstanding purchase rights granted under the Employee Stock Purchase Plan or other employee stock purchase plan of the Company must not exceed in aggregate 30 percent of the issued and outstanding ordinary shares in issuance from time to time.

(g) Individual Limit

The total number of ordinary shares underlying Stock Options or other options granted by the Company to, and the total number of ordinary shares that may be purchased under one or more purchase rights granted under the Employee Stock Purchase Plan or any other employee stock purchase plan granted by the Company by, a Participant (including both exercised and outstanding Stock Options) in any twelve-month period may not exceed at any time one percent (1%) (or 0.1 percent in the case of an independent Non-executive Director) of the then issued and outstanding ordinary shares unless otherwise allowed under the Listing Rules.

(h) Exercise of Option

A Stock Option shall vest, and be exercised, in accordance with the terms of the Stock Option Plan, the relevant Award Document and any rules and procedures established by the Compensation Committee for this purpose. However, the term of each Stock Option shall not exceed ten years from the date of grant.

(i) Director Options

Each non-employee Director may be granted Stock Options to purchase ordinary shares (or an equivalent of ADSs) on the terms set out in the relevant Award Document.

The Directors shall exercise all authority and responsibility with respect to Stock Options granted to Directors subject to the requirements of the Listing Rules.

All non-employee Directors Stock Options shall only vest provided that the Director has remained in service as a Director through such vesting date. The unvested portion of a Stock Option granted to a Director shall be forfeited in full if the Director s service with the Board ends for any reason prior to the applicable vesting date.

Following termination of a non-employee Director s service on the Board, such non-employee Director (or his or her estate, personal representative or beneficiary, as the case may be) shall be entitled to exercise those of his or her Stock Options which have vested as of the date of such termination within 120 days following such termination.

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(j) Termination or Lapse of Option
A Stock Option shall terminate or lapse automatically on:
(i) the expiry of ten years from the date of grant;
(ii) the termination of a Participant s employment or service with the Company for a reason set out in sub-paragraph (l) below;
(iii) save as to any contrary directions of the Compensation Committee, in the event of a complete liquidation or dissolution of the Company, all Stock Options outstanding at the time of the liquidationor dissolution shall terminate without further action by any person;
(iv) the sale or other divestiture of a subsidiary, division or operating unit of the Company (where the Participant is employed by such subsidiary, division or operating unit); and
(v) termination of the service relationship with a service provider (where the Participant is a service provider of the Company).
(k) Rights are personal to Participant
A Stock Option is personal to the Participant and shall be exercisable by such Participant or his Permitted Transferee (as defined below) only. An option shall not be transferred other than by will, by the laws of descent and distribution or pursuant to a domestic relations order. The Compensation Committee may also, at its discretion and subject to such terms and conditions as it shall specify, permit the transfer of a Stock Option for no consideration to a Participant s family members or to a trust or partnership established for the benefit of such family members (collectively Permitted Transferees). Any Stock Option transferred to a Permitted Transferee shall be further transferable only by will or the laws of descent and distribution or, for no consideration, to another Permitted Transferee of the Participant.
(l) Termination of employment or service
If a Participant s employment or service with the Company is terminated for the following reasons:
(i) the failure or refusal of the Participant to substantially perform the duties required of him or her as an employee or officer of, or service provider to, the Company;
(ii) any material violation by the Participant of any law or regulation applicable to any business of the Company, or the Participant s conviction of, or a plea of nolo contendae to, a felony, or any perpetration by the Participant of a common law fraud against the Company; or
(iii) any other misconduct by the Participant that is materially injurious to the financial condition, business or reputation of the Company,
Then all Stock Options granted to the Participant, whether or not then vested, shall immediately laspe.
The Compensation Committee may permit any Incentive Stock Option to convert into a Non-Qualified Stock Option as of a Participant s termination of employment for purposes of providing such Participant with the benefit of any extended exercise period applicable to Non-Qualified Stock Options when the contract of employment of the holder of Incentive Stock Option terminates.
(m) Change in control of the Company
The Compensation Committee may specify at or after the date of grant of a Stock Option the effect that a Change in Control (as defined in the Stock Option Plan) will have on such Stock Option. The Compensation Committee may also, in contemplation of a Change in Control, accelerate the vesting, exercisability or payment of Stock Options to a date prior to the Change in Control, if the Compensation Committee determines that such action is necessary or advisable to allow the participants to realise fully the value of their share options in connection with such Change in Control.

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(n) Change in the capital structure of the Company

In the event of an alteration in the capital structure of the Company (which includes a capitalization issue, reduction of capital, consolidation, sub-division of Plan Shares, or rights issue to purchase Plan Shares at a price substantially below market value), the Compensation Committee may equitably adjust the number and kind of Plan Shares authorised for issuance in order to preserve, the benefits or potential benefits intended to be made available under the Stock Option Plan. In addition, upon the occurrence of any of the foregoing events, the number of outstanding Stock Options and the number and kind of shares subject to any outstanding Stock Option and the purchase price per share under any outstanding Stock Option shall be equitably adjusted so as to preserve the benefits or potential benefits intended to be made available to Participants.

(o) Period of the Stock Option Plan

The Stock Option Plan shall remain in force for a period of ten years commencing on the date of Shareholders approval of the Plan.

(p) Amendments and Termination

The Stock Option Plan may be altered, amended in whole or in part, suspended and terminated by the Board at any time provided alterations or amendments of a material nature or any change to the terms of the Stock Options granted must be approved by the shareholders of the Company, unless such alteration or amendment takes effect automatically under the terms of the Stock Option Plan. For the avoidance of doubt, any alteration or amendment pursuant to the exercise of any authority granted under the Stock Option Plan shall be deemed to take effect automatically under the terms of the Share Option Plan. Any alteration or amendment must be in accordance with the requirements of the Listing Rules or permitted by the HKSE.

If the Stock Option Plan is terminated early by the Board, no further Stock Options may be offered but unless otherwise stated in the Plan, Stock Options granted before such termination shall continue to be valid and exercisable in accordance with the Stock Option Plan.

(q) Voting and dividend rights

No voting rights shall be exercisable and no dividends shall be payable in relation to Stock Options that have not been exercised.

(r) Cancellation of Stock Options

Stock Options granted but not exercised may not be cancelled unless an offer to cancel share options has been made pursuant to Rule 13 of the Hong Kong Code on Takeovers and Mergers and the Hong Kong Securities and Futures commission has consented to such cancellation.

(s) Ranking of Ordinary Shares

The ordinary shares to be allotted upon the exercise of a Stock Option will be subject to the Articles for the time being in force and will rank pari passu with the Plan Shares in issue on the date of such allotment.

Employee Stock Purchase Plan

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The following is a summary of the principal terms of the ESPP conditionally adopted by the Company by way of shareholders resolutions dated February 16, 2004 and Directors resolutions passed on January 16, 2004.

Summary of the terms of the ESPP

(a) Purposes of the ESPP

The purposes of the ESPP are to attract, retain and motivate employees of the Company, to provide a means of compensating the employees for their contributions to the growth and profitability by permitting such employees to purchase the ADSs of the Company at a discount and receive favourable U.S. income tax treatment on a subsequent qualifying disposition of such ADSs.

(b) Who may join

Subject to any contrary directions given by the Compensation Committee, all full-time and regular parttime employees (the Employees) of the Company as at the first business day (the Offering Date) of a given period specified by the Committee (the Offering Period) shall be eligible to enroll in the ESPP. To be eligible to purchase ADSs, all Employees must maintain his or her employment status, without interruption, with the Company through the last day of each Offering Period (the Purchase Date)

(c) Offering Period

The ESPP shall be implemented by a series of Offering Periods. An eligible Employee of the Company may elect to participate in the ESPP for any Offering Period by completing the requisite documents. The Compensation Committee shall determine the starting and ending dates of each Offering Period but no Offering Period shall be shorter than 6 months or longer than 27 months.

(d) Employees Contributions under the ESPP

All amounts that a Participant contributes (Contributions) shall be credited to his or her account under the ESPP. Participants must elect to have payroll deductions made on each payday during the Offering Period in a dollar amount specified in the documents submitted by him or by her. The Compensation Committee may permit Participants to make supplemental Contributions into his or her account, on such terms and subject to such limitations as the Compensation Committee may decide. Participants may, on one occasion only during an Offering Period, decrease the rate of his or her Contributions to his or her account for the Offering Period, including a decrease to zero. The Participant may restore his or her Contributions to the original level, prior to the earlier of,

(i) six months after the effective date of any such decrease; and

(ii) the end of the relevant Offering Period.

(e) Grant of Purchase Right

Each eligible Employee who elects to participate in the ESPP in any given Offering Period shall be granted on the Purchase Date, a right to purchase the Plan Shares (the Purchase Right). The Purchase Right of a Participant shall be calculated in accordance with the following formula:

(i) dividing (A) the product of US$25,000 and the number of calendar years during all or part of which the Purchase Right shall be outstanding by (B) the closing price of the Plan Shares on the applicable exchange on which Plan Shares are trading (the Fair Market Value) on the applicable exchange of the Plan Shares on the Offering Date; and

(ii) subtracting from the quotient thereof (A) the number of Plan Shares that the Employee has purchased during the calendar year in which the Offering Date occurs under the ESPP or under any other employee stock purchase plan of the Company or any subsidiary of the Company which is intended to qualify under Section 423 of the U.S. International Revenue Code of 1986 plus (B) the number of Plan Shares subject on the Offering Date to any outstanding Purchase Rights granted to the Employee under any related Plan.

If application of the above formula would result in the grant of Purchase Rights covering, in the aggregate, more than the number of Plan Shares that the Compensation Committee has made available for the relevant Offering Period, then the Compensation Committee shall adjust the number of Plan Shares subject to the Purchase Right in order that, following such adjustment, the aggregate number of Plan Shares subject to the purchase Right shall remain within the applicable limit.

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All Purchase Rights outstanding at the tenth anniversary of the Plan shall remain outstanding through and may be exercised upon the relevant Purchase Date, but no additional Purchase Right shall be granted under the ESPP.

(f) Exercise of Purchase Right

Unless a Participant withdraws from the ESPP, his or her Purchase Right shall become exercisable automatically, on the Purchase Date of the relevant Offering Period for the number of Plan Shares obtained by dividing the accumulated Contributions credited to the Participant s account as of the Purchase Date by the applicable Purchase Price, being an amount not less than 85 percent of the Fair Market Value of the Plan Shares on the Offering Date or on the Purchase Date, whichever is lower (the Purchase Price).

The Compensation Committee may credit any Contributions that have been credited to a Participant s account under the ESPP with interest. Any interest credited to a Participant s account shall not be used to purchase ADSs and shall instead be paid to the Participant at the end of the relevant Offering Period.

If any portion of a Participant s accumulated Contributions is not used to purchase ordinary shares on a given Purchase Date, the remaining amount shall be held in the Participant s account and used for the purchase of Plan Shares under the next Offering Period, unless the Participant withdraws from the next Offering Period.

The exercise of the Purchase Right granted under the ESPP is not subject to any performance target.

(g) Limit of the ESPP

The number of ordinary shares that may be issued under the Stock Option Plan and the ESPP (the Global Limit) shall not exceed ten percent of the issued and outstanding ordinary shares immediately following the closing of the Global Offering (i.e., 1,317,000,000).

The number of ordinary shares that may be issued upon exercise of all outstanding Purchase Rights granted under the ESPP or other employee stock purchase plan of the Company or and any outstanding stock options granted under the Stock Option Plan or other stock option plan of the Company must not exceed, in the aggregate, thirty percent of the issued and outstanding ordinary shares in issuance from time to time.

(h) Period of the ESPP

The ESPP shall continue for a term of ten years from the date of its approval by the Shareholders unless terminated in accordance with sub-paragraph (i).

(i) Amendments and Termination of the ESPP

The Compensation Committee may at any time amend the ESPP in any respect or terminate the ESPP, except that, without the approval of the Company s shareholders at a meeting duly called, no amendment shall be made in relation to:

(i) increasing the number of ADSs approved for the ESPP; or

(ii) decreasing the Purchase Price per ADSs.

Any alterations or amendments of a material nature or any change to the terms of the Purchase Rights granted must be approved by the shareholders of the Company, unless such alteration or amendment takes effect automatically under the terms of the ESPP. For the avoidance of doubt, any alteration or amendment pursuant to the exercise of any authority granted under the ESPP shall be deemed to take effect automatically under the terms of the ESPP. Any amendment made to the ESPP must be in accordance with the requirements of the Listing Rules or permitted by the SEHK.

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If the ESPP is terminated by the Board prior to the tenth anniversary of the date of Board approval, unless the Compensation Committee has also terminated any Offering Period then in progress, Purchase Rights granted before such termination shall continue to be valid and exercisable in accordance with, and subject to, the terms and conditions of the Plan.

Rule 17.03(9) of the Listing Rules provide that the exercise price of any share option scheme operated by listed issuers may not be lower than effectively the market price of the ordinary shares. As a result of the capital-intensive nature of the Company s business, we have traditionally relied on share options, rather than cash, as an important means of remunerating its employees. This is common in the industry and we wish to continue this practice. Accordingly, we have applied to and obtained from the SEHK a waiver from strict compliance with Rule 17.03(9) of the Listing Rules such that the Company is allowed to continue to grant options over its ADSs to its employees under the ESPP at an exercise price which is at a discount (up to 15 percent discount) to the lower of market price at the commencement of the offering period or the market price on the purchase date.

Up and until December 31, 2008, the Company has not granted any purchase right under the ESPP.

Item 7. Major Shareholders and Related Party Transactions

Major Shareholders

The following table sets forth information regarding the beneficial ownership as of December 31, 2008 of our ordinary shares, by each shareholder who is known by us to beneficially own 5% or more of our outstanding shares as of such date.

Name of Shareholder	Number of Shares Held	Percentage Held
Shanghai Industrial Investment (Holdings) Company Limited (SIIC)	420,008,000(1)	1.88%
	1,833,269,340(2)	8.21%
Total:	2,253,277,340	10.09%
Datang Telecom Technology & Industry Holdings Co., Ltd.	3,699,094,300(3)	16.57%
Donald Smith & Co., Inc.	1,326,812,150(4)	5.94%

Notes:

(1) All such ordinary shares are held by SIIC Treasury (B.V.I.) Limited which is a wholly-owned subsidiary of SIIC. The voting rights of such shares are vested in Shanghai Industrial Holdings Limited (SIHL),

(2) All such shares are held by S.I. Technology Production Holdings Limited (SITPHL) which is a wholly-owned subsidiary of SIHL. SIHL is an indirect non-wholly owned subsidiary of SIIC which is holding SIHL s shares through its subsidiaries, which together are entitled to exercise or control the exercise of more than one-third of the voting power at the general meetings of SIHL. By virtue of Part XV of the Securities and Futures Ordinance (Cap. 571 of the laws of Hong Kong), SIIC and its subsidiaries namely, Shanghai Investment Holdings Limited and Shanghai Industrial Investment Treasury Company Limited are deemed to be

interested in the 1,833,269,340 Shares held by SITPHL. The Company s Director as at December 31, 2008, Wang Zheng Gang, is the Chief Representative of the Shanghai Representative Office of SIHL and the chairman of SIIC Management (Shanghai) Limited. It is the Company s understanding that voting and investment control over the Ordinary Shares beneficially owned by SIHL are maintained by the board of directors of SIHL.

(3) All such shares are held by Datang Holdings (Hongkong) Investment Company Limited which is a wholly-owned subsidiary of Datang Telecom Technology & Industry Holdings Co., Ltd. All such shares were purchased on

December 24, 2008 pursuant to the Share Purchase Agreement dated November 6, 2008 between us and Datang Telecom Technology & Industry Holdings Co., Ltd.

(4) According to the the Schedule 13G filed with the SEC on February 11, 2009 by Donald Smith & Co., Inc., all such shares are owned by advisory clients of Donald Smith & Co., Inc., no one of which, to the knowledge of Donald Smith & Co., Inc. owns more than 5% of the class. 1,326,812,150 ordinary shares were held in the form of 26,536,243 ADSs. Each ADS represents 50 ordinary shares.

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Each ordinary share is entitled to one vote on all matters upon which the ordinary shares are entitled to vote, including the election of directors. No shareholder has voting rights that are different from those of other shareholders.

As of December 31, 2008, 22,327,784,827 ordinary shares (inclusive of 63,087,191 ADS shares) of our company were outstanding. Of these ordinary shares, 3,154,359,550 shares were registered in the name of HSBC Nominees (Hong Kong) Limited, on behalf of J.P. Morgan Chase Bank, the depositary under the deposit agreement. J.P. Morgan has advised us that, as of December 31, 2008, these 63,087,191 ADSs, representing 3,154,359550 ordinary shares, were held of record by eight U.S. persons. We have no further information as to shares held or beneficially owned by U.S. persons. Each ADS represents 50 ordinary shares.

We do not believe that we are directly or indirectly owned or controlled by another corporation, by any foreign government or by any other natural or legal person severally or jointly.

Related Party Transactions

The following disclosure is for the purpose of fulfilling disclosure requirements pursuant to the Rules Governing the Listing of Securities on the HKSE (the HK Listing Rules) and the rules and regulations promulgated pursuant to the U.S. Securities and Exchange Act of 1934, as amended, only, and may contain disclosure of related party transactions not required to be disclosed in our financial statements under U.S. GAAP. This section is not applicable under U.S. GAAP since it is not related to financial data.

Indemnification Agreements and Service Contracts

Article 156 of our Articles of Association provides (amongst others) that we may indemnify any person who is made a party to any action, suit or proceeding by reason of the fact that the person is or was our director, officer, employee or agent, or is or was serving at our request as our director, officer, employee or agent at another entity, subject to certain limitations and applicable conditions.

We recognize the substantial increase in corporate litigation in general, subjecting directors, officers, employees, agents and fiduciaries to expensive litigation risks. We desire to attract and retain the services of highly qualified individuals to serve the company and, in part, in order to induce such individuals to continue to provide services to the company, we wish to provide for the indemnification and advancing of expenses of its directors as permitted by law and applicable regulations.

Original Indemnification Agreements. On or around March 18, 2004, upon completion of the Global Offering, we entered into identical indemnification agreements with each director whose appointment as director took effect immediately upon the Global Offering, whom we refer to as the Global Offering Directors, whereby we agreed to,inter alia, indemnify our Global Offering Directors in respect of liability arising from their capacity as our directors. We refer to these indemnification agreements as, collectively, the Original Indemnification Agreements. Pursuant to the Original Indemnification Agreements, we were obliged to indemnify each Global Offering Director, to the fullest extent permitted by law, against all costs, charges, expenses, liabilities, losses and obligations incurred in connection with any threatened, pending or completed action, suit, proceeding or alternative dispute resolution mechanism, or any hearing, inquiry or investigation which might lead to any of the foregoing (an "Applicable Claim) by reason of or arising out of any event or occurrence relating to the fact that he is or was a director of SMIC, or any of our subsidiaries, or is or was serving at our request at another corporation or enterprise, or by reason of any activity or inactivity while serving in such capacity(an "Indemnifiable Event). Our obligation to indemnify our Global Offering Directors pursuant to the Original Indemnification Agreements was subject to certain exceptions and limitations set out therein.

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New Indemnification Agreements; Service Contracts. At the annual general meeting of our shareholders on May 6, 2005, our shareholders, other than our directors, chief executive officer and their respective Associates (as defined in the HK Listing Rules) approved an amendment to the form of the Original Indemnification Agreements. As amended, we refer to the new form of Indemnification Agreements as the New Indemnification Agreements. The New Indemnification Agreements executed by each of the directors superseded the Original Indemnification Agreements which we had previously entered into with any existing directors. The New Indemnification Agreement reflected the then new requirements under Rules 14A.35 of the HK Listing Rules to set a term of no longer than three years and a maximum aggregate annual value for each connected transaction (as defined under the HK Listing Rules). The terms of the New Indemnification Agreements were the same as the Original Indemnification Agreements, except that the New Indemnification Agreements were subject to a term of three years and an annual cap. The annual cap in relation to the New Indemnification Agreements was not to exceed a maximum aggregate annual value as disclosed in our previous announcement. For the year ended December 31, 2008, no payment was made to any director under the New Indemnification Agreements.

Service Contracts. The New Indemnification Agreements remained in effect until the entering into between us and our directors of amended service contracts between October 7, 2008 and April 13, 2009 which include indemnity provisions. Five of our directors signed the amended service contracts in 2008, and the remaining directors signed the amended service contracts in 2009. Each of our executive officers also signed service contracts which include indemnity provisions in 2008 and 2009. We refer to the service contracts we have entered into with each of our directors and executive officers collectively as the Service Contracts. The indemnification provisions contained in the Service Contracts are substantially the same as the terms of the New Indemnification Agreements, except that the Service Contracts are not subject to a maximum term or to an annual cap. The indemnification provisions set forth in the Services Contracts will continue in effect with respect to Applicable Claims relating to Indemnifiable Events regardless of whether the relevant director or executive officer continues to serve as our director or executive officer or to serve at any other enterprise at our request. Except for these indemnification provisions, the Service Contracts do not provide for benefits upon termination of service or employment.

Strategic Cooperation Agreement

On December 24, 2008, upon completion of the Share Purchase Agreement pursuant to which Datang conditionally agreed to subscribe through a Hong Kong incorporated wholly owned subsidiary, and the Company conditionally agreed to allot and issue, shares representing 19.9% of the issued share capital of the Company prior to such issuance and approximately 16.6% following such issuance at a total purchase price of US$171.8 million, the Company and Datang entered into a strategic cooperation agreement (the Strategic Cooperation Agreement).

Pursuant to the Strategic Cooperation Agreement, the Company intends to give priority to the production requirements of Datang, while Datang intends to give priority to engage or employ the fabrication services of the Group. In addition, the Company and Datang would share their technological research and development resources, co-operate in the development of international markets and globalization of their businesses, and make joint efforts to apply for PRC national and local projects in connection with scientific research and industrialization relating to the integrated circuit sector.

The pricing for the transactions contemplated under the Strategic Cooperation Agreement will be determined based on market value. The Proposed Cap for the period commencing December 24, 2008 and ending on the day on which the Company s next annual general meeting will be held is US$100 million, which represents the maximum revenue expected to be generated by the Company from these transactions during such period.

For the year ended December 31, 2008, no transactions under the Strategic Cooperation Agreement took place between Datang and the Company (or any of its subsidiaries).

Item 8. Financial Information

Consolidated Statements and Other Financial Information

Please see Item 18. Financial Statements.

See Item 4 Information on the Company-Business Overview-Customers and Markets regarding the percentage of our sales which are exported from China.

Litigation

As is the case with many companies in the semiconductor industry, we have received from time to time communications from third parties asserting that our technologies, fabrication processes, design of the semiconductors made by us or use by our customers of semiconductors made by us may infringe upon patents or other intellectual property rights of others. Irrespective of the validity of such claims, we could incur significant costs in the defense thereof or could suffer adverse effects on our operations.

Beginning in December 2003 through August 2004, the Company became subject to several lawsuits brought by Taiwan Semiconductor Manufacturing Company, Limited (TSMC) relating to alleged infringement of certain patents and misappropriation of alleged trade secrets relating to methods for conducting semiconductor fab operations and manufacturing integrated circuits.

On January 30, 2005, the Company and TSMC exchanged signature pages later attached to a settlement agreement. Terms were added to the document subsequent to the exchange of signatures. The identification of the exact terms of the agreement were determined at a preliminary trial in 2009, as described below under Recent TSMC Legal Developments. As found by the California Superior Court, SMIC and TSMC agreed, without admission of liability, to dismiss all pending legal actions without prejudice between the two companies (the Settlement Agreement). The terms of the Settlement Agreement also were determined to include the following:

1) The Company and TSMC agreed to cross-license each other s patent portfolio for all semiconductor device products, effective from January 2005 through December 2010.

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2) TSMC covenanted not to sue the Company for trade secret misappropriation as alleged in TSMC s legal actions as it related to .15µm and larger processes subject to certain conditions (TSMC Covenant). The TSMC Covenant did not cover .13µm and smaller technologies after 6 months following execution of the Settlement Agreement (July 31, 2005). Excluding the .13µm and smaller technologies, the TSMC Covenant remains in effect indefinitely, terminable upon a breach by the Company.

3) The Company is required to deposit certain Company materials relating to .13µm and smaller technologies into an escrow account until December 31, 2006 or under certain circumstances for a longer period of time.

4) The Company agreed to pay TSMC an aggregate of $175 million in installments of $30 million for each of the first five years and $25 million in the sixth year. The Company has to date made all scheduled payments as set forth in the Settlement Agreement.

The Company believes the Court s ruling is erroneous. The ruling may be appealed by SMIC following the filing of a final judgment by the Court in this matter.

Recent TSMC Legal Developments:

On August 25, 2006, TSMC filed a lawsuit against the Company and certain subsidiaries, namely SMIC (Shanghai), SMIC (Beijing) and SMIC (Americas) in the Superior Court of the State of California, County of Alameda for alleged breach of a settlement agreement, alleged breach of promissory notes and alleged trade secret misappropriation by the Company. TSMC seeks, among other things, damages, injunctive relief, attorneys fees, and the acceleration of the remaining payments outstanding under that settlement agreement.

In the present litigation, TSMC alleges that the Company has incorporated TSMC trade secrets in the manufacture of the Company s 0.13 micron or smaller process products. TSMC further alleges that as a result of this claimed breach, TSMC s patent license is terminated and the covenant not to sue is no longer in effect with respect to the Company s larger process products. The Company has vigorously denied all allegations of misappropriation. The Court has made no finding that TSMC s claims are valid. The Court has set a trial date of September 8, 2009.

On September 13, 2006, the Company announced that in addition to filing a response strongly denying the allegations of TSMC in the United States lawsuit, it filed on September 12, 2006, a cross-complaint against TSMC seeking, among other things, damages for TSMC s breach of contract and breach of implied covenant of good faith and fair dealing.

On November 16, 2006, the High Court in Beijing, the People s Republic of China, accepted the filing of a complaint by the Company and its wholly-owned subsidiaries, namely, SMIC (Shanghai) and SMIC (Beijing), regarding the unfair competition arising from the breach of bona fide (i.e. integrity, good faith) principle and commercial defamation by TSMC (PRC Complaint). In the PRC Complaint, the Company is seeking, among other things, an injunction to stop TSMC s infringing acts, public apology from TSMC to the Company and compensation from TSMC to the Company, including profits gained by TSMC from their infringing acts.

On August 14, 2007, the Company filed an amended cross-complaint against TSMC seeking, among other things, damages for TSMC s breach of contract and breach of patent license agreement. TSMC thereafter denied the allegations of the Company s amended cross-complaint and subsequently filed additional claims that the Company breached a settlement agreement by filing an action in the Beijing High Court. The Company has denied these additional claims by TSMC.

On August 15-17, 2007, the California Court held a preliminary injunction hearing on TSMC s motion to enjoin use of certain process recipes in certain of the Company s 0.13 micron logic process flows.

On September 7, 2007, the Court denied TSMC s preliminary injunction motion, thereby leaving unaffected the Company s development and sales. However, the court required the Company to provide 10 days advance notice to TSMC if the Company plans to disclose logic technology to non-SMIC entities under certain circumstances, to allow TSMC to object to the planned disclosure.

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In May 2008, TSMC filed a motion in the California Court for summary adjudication against the Company on several of the Company s cross claims. The Company opposed the motion and on August 6, 2008, the Court granted in part and denied in part TSMC s motion.

On June 23, 2008, the Company filed in the California court a cross-complaint against TSMC seeking, among other things, damages for TSMC s unlawful misappropriation of trade secrets from SMIC to improve its competitive position against SMIC.

On July 10, 2008, the California Court held a preliminary injunction hearing on TSMC s motion to enjoin disclosure of information on certain process recipes in the Company s 0.30 micron logic process flows to 3rd parties. On August 8, 2008, the Court granted-in-part TSMC s motion and preliminarily enjoined SMIC from disclosing fourteen 0.30 ìm process steps. On October 3, 2008, SMIC filed a notice of appeal of the Court s August 8, 2008 Order with the California Court of Appeal. This appeal is currently pending.

During the pre-trial proceedings in the matter, as noted above under Overview of TSMC Litigation , questions arose regarding the actual terms of the 2005 Settlement Agreement between SMIC and TSMC. Accordingly, the California Court held a preliminary trial on January 13 to 16, 2009, limited to a determination of the terms of the Settlement Agreement and an interpretation of any requirements to meet and confer prior to institution of litigation. On March 10, 2009, the Court issued a Statement of Decision finding, in part, that an agreement between the parties was executed on January 30, 2005, and thereafter amended on February 2, 2005, as urged by TSMC. The Company believes the Court s ruling is erroneous. The ruling may be appealed by SMIC following the filing of a final judgment by the Court in this matter.

On May 1, 2009, the Company filed motions for summary adjudication against TSMC s claims for breach of promissory notes and violation of the California Uniform Trade Secrets Act. The motions will be heard by the Court on July 17, 2009.

The California Court has further scheduled a trial upon all liability issues related to a selected list of TSMC trade secret claims and SMIC trade secret claims to commence on September 8, 2009.

In the Company s action in the Beijing High People s Court, following an unsuccessful challenge to that Court s jurisdiction by TSMC, the Court has held evidentiary hearings on October 15, October 29, and November 25, 2008. The Court rendered its first-instance judgment on June 10, 2009. Claims of SMIC against TSMC were not supported by the Court in the first-instance judgment. The first-instance judgment is not final and either TSMC or SMIC may further appeal to the PRC Supreme People s Court according to the law.

Under the provisions of SFAS 144, the Company is required to make a determination as to whether or not this pending litigation represents an event that requires a further analysis of whether the patent license portfolio has been impaired. We believe that the lawsuit is at a discovery stage and we are still evaluating whether or not the litigation represents such an event. The Company expects further information to become available to us, which will aid us in making a determination. The outcome of any impairment analysis performed under SFAS 144 might result in a material impact to our financial position and results of operations. Because the case is in its discovery stage, the Company is unable to evaluate the likelihood of an unfavorable outcome or to estimate the amount or range of potential loss.

Dividends and Dividend Policy

At the end of 2008, the Company s accumulated deficit increased to US$748.5 million from an accumulated deficit of US$308.2 million at the end of 2007. The Company has not declared or paid any cash dividends on the ordinary shares. We intend to retain any earnings for use in the Company s business and do not currently intend to pay cash dividends on the ordinary shares. Dividends, if any, on the outstanding shares will be declared by and subject to the discretion of the Board and must be approved at the annual general meeting of shareholders. The timing, amount and form of future dividends, if any, will also depend, among other things, on:

- the Company s results of operations and cash flow;
- the Company s future prospects;
- the Company s capital requirements and surplus;

the Company s financial condition;

general business conditions;

contractual restrictions on the payment of dividends by the Company to its shareholders or by the Company s subsidiaries to the Company; and

other factors deemed relevant by the Board.

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The Company s ability to pay cash dividends will also depend upon the amount of distributions, if any, received by the Company from its wholly-owned Chinese operating subsidiaries. Under the applicable requirements of Chinese Company Law, the Company s subsidiaries in China may only distribute dividends after they have made allowances for:

- recovery of losses, if any;
- allocation to the statutory common reserve funds;
- allocation to staff and workers bonus and welfare funds; and
- allocation to a discretionary common reserve fund if approved by the Company s shareholders.

More specifically, these operating subsidiaries may only pay dividends after 10% of their net profit has been set aside as statutory common reserves and a discretionary percentage of their net profit has been set aside for the staff and workers bonus and welfare funds. These operating subsidiaries are not required to set aside any of their net profit as statutory common reserves if such reserves are at least 50% of their respective registered capital. Furthermore, if they record no net income for a year, they generally may not distribute dividends for that year.

Significant Changes

Please see the section entitled Litigation above.

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Item 9. The Offer and Listing

Our ordinary shares are principally traded on the Stock Exchange of Hong Kong under the stock code 981 Our ordinary shares began trading on the Stock Exchange of Hong Kong on March 18, 2004. Our American Depositary Shares, which began trading on the New York Stock Exchange on March 17, 2004, are traded under the symbol SMI. The table below sets forth the high and low closing prices on the Stock Exchange of Hong Kong and the New York Stock Exchange for the ordinary shares represented by the ADSs, since the completion of the global offering and for the most recent six months.

	Stock Exchange of Hong Kong Closing price per ordinary share				**New York Stock Exchange[1] Closing price per ADS**			
	High Price		**Low Price**		**High Price**		**Low Price**	
2005								
First Quarter	HK$	1.75*	HK$	1.48	US$	11.14	US$	9.35
Second Quarter	HK$	1.71	HK$	1.48	US$	10.93	US$	9.52
Third Quarter	HK$	1.75*	HK$	1.21	US$	11.33*	US$	7.83
Fourth Quarter	HK$	1.33	HK$	1.00*	US$	8.46	US$	6.68*
2006								
First Quarter	HK$	1.29*	HK$	1.02	US$	8.38*	US$	6.73
Second Quarter	HK$	1.21	HK$	1.00	US$	7.82	US$	6.36
Third Quarter	HK$	1.07	HK$	0.97	US$	6.88	US$	6.30
Fourth Quarter	HK$	1.03	HK$	0.87*	US$	6.46	US$	5.48*
2007								
First Quarter	HK$	1.24*	HK$	0.87	US$	8.30*	US$	5.87
Second Quarter	HK$	1.24	HK$	1.04	US$	7.68	US$	6.69
Third Quarter	HK$	1.18	HK$	0.81	US$	7.50	US$	5.30
Fourth Quarter	HK$	1.11	HK$	0.71*	US$	6.72	US$	4.57*
2008								
First Quarter	HK$	0.82*	HK$	0.41	US$	4.98*	US$	2.76
Second Quarter	HK$	0.78	HK$	0.44	US$	4.32	US$	2.88
Third Quarter	HK$	0.48	HK$	0.20	US$	2.99	US$	1.32
Fourth Quarter	HK$	0.35	HK$	0.11*	US$	2.41	US$	0.89*
December	HK$	0.35	HK$	0.15	US$	2.22	US$	0.96
2009								
January	HK$	0.39	HK$	0.24	US$	2.29	US$	1.54
February	HK$	0.32	HK$	0.23	US$	1.86	US$	1.53
March	HK$	0.32	HK$	0.25	US$	2.02	US$	1.57
April	HK$	0.35	HK$	0.27	US$	2.18	US$	1.82
May	HK$	0.42	HK$	0.29	US$	2.70	US$	2.01
June (through June 15)	HK$	0.47	HK$	0.41	US$	2.96	US$	2.61

(1) Each ADS represents 50 ordinary shares.

* Indicates high and low prices for the fiscal year.

At our request, trading in our shares on the Stock Exchange of Hong Kong was suspended with effect from November 6, 2008, 10:03 a.m., Hong Kong time, pending the release of our announcement regarding our entering into the Share Purchase Agreement with Datang Telecom Technology & Industry Holdings Co., Ltd. Pursuant to our application to the Hong Kong Stock Exchange, trading in our shares resumed on the Stock Exchange of Hong Kong with effect from 9:30 a.m., November 11, 2008, Hong Kong time Also at our request, trading in our ADSs on the NYSE was suspended for a like period.

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Item 10. Additional Information

Memorandum and Articles of Association

The section entitled Description of Share Capital in our IPO registration statement is incorporated by reference into this annual report.

The sections entitled Item 10-Additional Information-Memorandum and Articles of Association in our annual report on Form 20-F for the fiscal year ended December 31, 2004, filed with the SEC on June 26, 2005 and in our annual report on Form 20-F for the fiscal year ended December 31, 2005, filed with the SEC on June 26, 2006 are incorporated by reference into this annual report. In addition, at the annual general meeting of our shareholders held on June 2, 2008, our shareholders approved an amendment to our Articles of Association to provide that a member of our board of directors may be removed by Ordinary Resolution.

Material Contracts

Share Purchase Agreement with Datang Telecom Technology & Industry Holdings Co., Ltd.

We entered into a Share Purchase Agreement dated November 6, 2008 with Datang Telecom Technology & Industry Holdings Co., Ltd, or Datang, pursuant to which Datang subscribed through a Hong Kong incorporated subsidiary, also referred to below as the HKCo, and we allotted and issued, 3,699,094,300 ordinary shares for a purchase price of HK$0.36 per ordinary shares for a total purchase price of US$171.8 million on December 24, 2008, also referred to below as the closing date.

The principal terms of the Share Purchase Agreement are as follows:

Right to Nominate Investor Nominees. Datang has the right to nominate two nominees to our board, provided that the decision of our board to appoint, or propose to our shareholders for appointment, any individual nominated by Datang as a director will be made in the best interests our company and our shareholders as a whole, and we are not obliged to simply appoint any individual nominated by Datang as a director without taking into account such considerations, provided further that.(a) subject to clause (b) below, the number of Datang nominees shall decrease to one if Datang, the HKCo and the permitted transferee, collectively, hold less than 1,849,547,150 shares (as appropriately adjusted for stock splits, stock consolidation, stock dividends, recapitalizations and the like) of the our total issued nominal share capital, or Datang, together with the HKCo, holds less than 924,773,575 shares (as appropriately adjusted for stock splits, stock consolidation, stock dividends, recapitalizations and the like) of our total issued nominal share capital; and (b) the right to nominate any Datang nominee shall cease if Datang, the HKCO and the permitted transferee, collectively, hold less than 924,773,575 shares (as appropriately adjusted for stock splits, stock consolidation, stock dividends, recapitalizations and the like) of our total issued nominal share capital, or if Datang, together with HKCo, holds less than 462,386,788 shares (as appropriately adjusted for stock splits, stock consolidation, stock dividends, recapitalizations and the like) of our total nominal share capital.;

Right to Nominate Vice-President in Charge of TD-SCDMA. Datang has the right to nominate a Vice-President in charge of TD-SCDMA, provided that Datang, HKCo and the permitted transferee, collectively, hold at least 924,773,575 shares (as appropriately adjusted for stock splits, stock consolidation, stock dividends, recapitalizations and the like) of our total nominal share capital from time to time, provide that Datang, together with the HKCO, holds at least 462,386,788 shares (as appropriately adjusted for stock splits, stock consolidation, stock dividends, recapitalizations and the like) of our total issued share capital from time to time, subject to the approval of our board (excluding the Datang nominees).

Pre-emptive Right. Datang has the following right to purchase any new ordinary shares, any securities convertible into or exchangeable into ordinary shares or any warrants or other rights to subscribe for ordinary shares, referred to as the Relevant Securities (subject to the approval of our independent shareholders in order to comply with the Rules Governing the Listing of Securities on the Hong Kong Stock Exchange prior to each such purchase), in the event that we propose to issue the Relevant

Securities, to enable Datang to hold after such issue (i) in the case of an offer to investors that would result in a prospective largest shareholder (other than an underwriter that is placing on our behalf the Relevant Securities in a *bona* fide capital markets transaction), one ordinary share more than the number of ordinary shares proposed to be beneficially owned by the prospective largest shareholder, unless (a) Datang and the HKCo hold less than 2,774,320,725 shares (as appropriately adjusted for stock splits, stock consolidation, stock dividends, recapitalizations and the like) of our total nominal share capital, or (b) at least two-thirds of our board (excluding Datang nominees) in good faith resolves in writing that such exercise is not in the best interests of our company and our shareholders as a whole, and (ii) in the case of the issue of Relevant Securities other than (i) above, a pro rata portion of the Relevant Securities equal to the percentage of our issued share capital then beneficially owned by Datang (together with HKCo) prior to the issuance of the Relevant Securities, provided that Datang (together with HKCo) maintains an ownership interest equal to at least 1,849,547,150 shares (as appropriately adjusted for stock splits, stock consolidation, stock consolidation, stock dividends, recapitalizations and the like) of our total nominal share capital.

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Lock-Up. Datang shall not transfer any of the shares purchased under the Share Purchase Agreement without our prior written consent for a period of two years from the closing date, provided that such lock-up shall not apply to transfer of less than 1,849,547,150 of such shares (as appropriately adjusted for stock splits, stock consolidation, stock dividends, recapitalizations and the like) to a permitted transferee as defined in the Share Purchase Agreement, provided that any such permitted transferee shall be a non-PRC incorporated entity, unless Datang shall have provided to us in writing justifying the need to transfer to a PRC incorporated entity, and our board (excluding the Datang nominees) shall have determined that such transfer to a PRC incorporated entity is not expected to be prejudicial to the interests of, or have an adverse effect, on our group.

Standstill. Datang shall not, except with our prior written consent, directly or indirectly, acquire any of our ordinary shares, any other security carrying voting rights and any outstanding convertible securities, options, warrants or other rights which are convertible into or exchangeable or exercisable or carrying rights of subscription for securities carrying voting rights in us (together our **voting securities** exceeding the lesser of thirty percent of our issued voting securities, or such other threshold that may trigger a mandatory offer obligation as set out in the Hong Kong Code on Takeovers and Mergers, at any time following the date of the Share Purchase Agreement and until the second anniversary of the closing date.

Strategic Cooperation Agreement with Datang Telecom Technology & Industry Holdings Co., Ltd.

We entered into a Strategic Cooperation Agreement, dated December 24, 2008, with Datang Telecom Technology & Industry Holdings Co., Ltd. The principal terms of the Strategic Cooperation Agreement are as follows:

Effective Period: Two years effective from the closing date, being December 24, 2008, subject to all the cooperation pursuant to the Strategic Cooperation Agreement, complying with, among other things, the Rules Governing the Listing of Securities on the Hong Kong Stock Exchange.

Material Terms: Cooperation in the areas of technology, industry, global markets and cooperative undertaking.

Cooperation of technological research and development, or Technological Cooperation. As part of our core business of providing IP design services, we intend to provide our existing research and development facilities and manpower in developing advanced logic processing technology and intellectual property bank for Datang, while Datang will provide pilot authentication products in relation to such development. The funding required for such research and development will be in accordance with the market practice and to be agreed by us and Datang. We expect this to be provided by reference to the extent of each party s responsibilities and rights in the cooperation. We also intend to recommend the technology of Datang to third party customers.

Provision of fabrication services, or Production Cooperation. As part of our core business of semiconductors fabrication, we intend to give priority to the production requiements of Datang while Datang intends to give priority to engage or employ our fabrication services provided that our price, technology and service standards are comparable to competitors and at the prevailing market value. The price for the provision of fabrication services under the Production Cooperation will be determined by reference to market price.

Global markets, or Market Development Cooperation. We also intend to cooperate with Datang in the development of international markets and globalization of its business.

Cooperative Undertaking in relation to PRC National Scientific Research Projects, or Cooperative Undertaking. We and Datang intend to make joint efforts to apply for PRC

national and local projects in connection with scientific research and industrialization relating to the integrated circuit sector.

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Long-Term Loan Facilities

SMIC Shanghai and SMIC Tianjin entered into long-term loan facilities in 2006 See Item 5 Liquidity and Capital Resources on page 65 for a description of these long-term loan facilities.

Please also see the section entitled Litigation above regarding the settlement agreement into which we entered with TSMC.

Other Contracts

Management Service Contracts with Cension Semiconductor Manufacturing Corporation and Wuhan Xinxin Semiconductor Manufacturing Corporation

We provide management services to Cension Semiconductor Manufacturing Corporation (Cension) and Wuhan Xinxin Semiconductor Manufacturing Corporation (Xinxin) which are government-owned foundries pursuant to the Operating and Management Agreement dated October 15, 2005 between us and Cension and the Operating and Management Agreement dated March 30, 2006 between us and Xinxin. Management service revenues under these agreements for 2008, 2007 and 2006 were $33,000,000, $42,000,000 and $4,151,238, respectively.

In 2008, 2007 and 2006, we sold equipment with carrying value of $7,688, $19,530,909 and $19,411,553 to Cension for $175,300, $42,300,258 and $61,182,653, which resulted in gains on sale of $167,612, $22,769,349 and $41,771,099, respectively.

In 2008, the Company sold equipment with carrying value of $3,629,605 to Xinxin for $3,944,204, which resulted in a gain on sale of $314,599.

Transactions with Cension Semiconductor Manufacturing Corporation (Cension) and Elpida Memory, Inc.

On April 10, 2007, Cension entered into an Asset Purchase Agreement with Elpida Memory, Inc., or Elpida, a Japan based memory chip manufacturer, for the purchase of Elpida s 200mm wafer processing equipment currently located in Hiroshima, Japan for the total price of approximately $320 million.

As part of this Asset Purchase Agreement, we provided a corporate guarantee for a maximum guarantee liability of $163.2 million on behalf of Cension in favour of Elpida. Our guarantee liability will terminate upon full payment of the purchase price by Cension to Elpida. In return for providing the above corporate guarantee, we received a guarantee fee from Cension based on 1.5% of the guarantee amount, or $2.4 million. Approximately $160 million in 200mm wafer processing equipment purchased under this Asset Purchase Agreement was held as collateral under the guarantee.

We are entitled to the net profit (loss) associated with the ongoing operations of this equipment, net of a guaranteed fixed share of revenue for Elpida, during the transitional period prior to when the equipment was relocated from Hiroshima to Chengdu. Such relocation was completed in 2008.

On August 30, 2007, Cension negotiated with Elpida and subsequently reduced the purchase price to US$309.5 million.

In April 2008, SMIC entered into an agreement with Cension to purchase approximately half of the equipment from Cension for approximately $152 million. The equipment acquired by the Company will be used for the Company s future expansion. The corporate guarantee was released after this purchase.

Exchange Controls

We receive a portion of our sales in Renminbi, which is currently not a freely convertible currency. Approximately 2.3% of our sales for the year ended December 31, 2006, approximately 0.9% of our sales for the year ended December 31, 2007, and approximately 5.4% of our sales for the year ended December, 31, 2008 were denominated in Renminbi. While we have used these proceeds for the payment of our Renminbi expenses, we may in the future need to convert these sales into foreign currencies to allow us to purchase imported materials and equipment, particularly as we expect the proportion of our sales to China-based companies to increase in the future. Under China s existing foreign exchange regulations, payments of current account items, including profit distributions, interest payments and expenditures from trade may be made in foreign currencies without government approval, except for certain procedural requirements. The Chinese government may, however, at its discretion, restrict access in the future to foreign currencies for current account transactions and prohibit us from converting our Renminbi sales into foreign currencies.

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Taxation

The following discussion of the material U.S. federal income and Cayman Islands tax consequences of an investment in our ADSs or ordinary shares is based upon laws and relevant interpretations thereof in effect as of the date of this prospectus, all of which are subject to change, possibly with retroactive effect. This discussion does not deal with all possible tax consequences relating to an investment in our ADSs or ordinary shares, such as the tax consequences under U.S. state, local and non-U.S. tax laws.

United States Federal Income Taxation

Except where noted, this summary deals only with the ownership and disposition of the ADSs and ordinary shares that are held as capital assets by U.S. Holders. This summary does not represent a detailed description of the U.S. federal income tax consequences applicable to U.S. Holders that are subject to special treatment under the U.S. federal income tax laws, including:

banks;

dealers in securities or currencies;

financial institutions;

real estate investment trusts;

insurance companies;

tax-exempt organizations;

persons holding ADSs or ordinary shares as part of a hedging, integrated or conversion transaction, constructive sale or straddle;

traders in securities that have elected the mark-to-market method of accounting;

persons liable for the alternative minimum tax;

persons who have ceased to be U.S. citizens or to be taxed as resident aliens;

persons who own or are deemed to own more than 10% of our voting shares; or

U.S. persons whose functional currency is not the U.S. dollar.

This summary is based in part on representations by the depositary and assumes that each obligation under the deposit agreement and any related agreement will be performed in accordance with its terms. Furthermore, the discussion below is based upon the provisions of the Internal Revenue Code of 1986, as amended, or the Code, and U.S. Treasury regulations, rulings and judicial decisions thereunder as of the date hereof, and such authorities may be replaced, revoked or modified, possibly on a retroactive basis, so as to result in U.S. federal income tax consequences different from those discussed below.

A U.S. Holder that holds ADSs or ordinary shares is urged to consult its own tax advisor concerning the U.S. federal income tax consequences as well as any consequences arising under the laws of any other taxing jurisdiction (including any U.S. state or locality) or any aspect of U.S. federal gift or estate law in light of the particular circumstances of the U.S. Holder.

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A U.S. Holder is a beneficial owner of ADSs or ordinary shares that is a U.S. person. A U.S. person is:

- a citizen or resident of the United States;
- a corporation or other entity taxable as a corporation created or organized in or under the laws of the United States, any state thereof, or the District of Columbia;
- an estate the income of which is subject to U.S. federal income taxation, regardless of its source; or
- a trust if it is subject to the primary supervision of a court within the United States and one or more U.S. persons have the authority to control all substantial decisions of the trust or has a valid election in effect under applicable U.S. Treasury regulations to be treated as a U.S. person.

If a partnership holds ADSs or ordinary shares, the tax treatment of a partner will generally depend on the status of the partner and the activities of the partnership. A U.S. Holder that is a partner of a partnership holding ADSs or ordinary shares is urged to consult its own tax advisors.

ADSs or Ordinary Shares. In general, for U.S. federal income tax purposes, a U.S. Holder of ADSs will be treated as the owner of the underlying ordinary shares that are represented by such ADSs. Deposits and withdrawals of ordinary shares in exchange for ADSs will not be subject to U.S. federal income taxation.

Distributions on ADSs or Ordinary Shares. Subject to the discussion under Passive Foreign Investment Company Rules below, the gross amount of the cash distributions on the ADSs or ordinary shares will be taxable to a U.S. Holder as dividends to the extent of our current and accumulated earnings and profits, as determined under U.S. federal income tax principles. Subject to certain limitations, dividends paid to noncorporate U.S. Holders, including individuals, may be eligible for a reduced rate of taxation if we are deemed to be a qualified foreign corporation for U.S. federal income tax purposes. A qualified foreign corporation includes:

- a foreign corporation that is eligible for the benefits of a comprehensive income tax treaty with the United States that includes an exchange of information program; and
- a foreign corporation if its stock with respect to which a dividend is paid or its ADSs backed by such stock are readily tradable on an established securities market within the United States,

but does not include an otherwise qualified corporation that is a passive foreign investment company. We believe that we will be a qualified foreign corporation for so long as we are not a passive foreign investment company and the ordinary shares or ADSs are considered to be readily tradable on an established securities market within the United States. A U.S. Holder that exchanges its ADSs for ordinary shares may not be eligible for the reduced rate of taxation on dividends if the ordinary shares are not readily tradable on an established securities market within the United States. Our status as a qualified foreign corporation, however, may change.

Dividends will be includable in a U.S. Holder s gross income on the date actually or constructively received by such U.S. Holder, in the case of ordinary shares, or by the depositary, in the case of ADSs. These dividends will not be eligible for the dividends-received deduction generally allowed to U.S. corporations in respect of dividends received from other U.S. corporations.

To the extent that the amount of any cash distribution exceeds our current and accumulated earnings and profits, the distribution will first be treated as a tax-free return of capital, causing a reduction in the adjusted basis of the ADSs or ordinary shares (thereby increasing the amount of gain, or decreasing the amount of loss, a U.S. Holder would recognize on a subsequent disposition of the ADSs or ordinary shares), and the balance in excess of adjusted basis will be subject to tax as capital gain.

To the extent we pay dividends on the ADSs or the ordinary shares in Hong Kong dollars, the U.S. dollar value of such dividends should be calculated by reference to the exchange rate prevailing on the date of actual or constructive receipt of the dividend, regardless of whether the Hong Kong dollars are converted into U.S. dollars at that time. If Hong Kong dollars are converted into U.S. dollars on the date of actual or constructive receipt of such dividends, the tax basis of the U.S. holder in such Hong Kong dollars will be equal to their U.S. dollar value on that date and, as a result, the U.S. Holder generally should not be required to recognize any foreign currency exchange gain or loss. Any

gain or loss recognized on a subsequent conversion or other disposition of the Hong Kong dollars generally will be treated as U.S. source ordinary income or loss.

It is possible that distributions of ADSs or ordinary shares that are received as part of a pro rata distribution to all of our ordinary shareholders may not be subject to U.S. federal income tax. The basis of the new ADSs or ordinary shares so received will be determined by allocating a U.S. Holder s basis in the old ADSs or ordinary shares between the old ADSs or ordinary shares and the new ADSs or ordinary shares received, based on their relative fair market values on the date of distribution.

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Dividends paid on the ADSs or ordinary shares will be income from sources outside of the United States and for tax years beginning before January 1, 2007, generally will constitute passive income or, in the case of certain U.S. Holders, financial services income and for tax years beginning after December 31, 2006, generally will constitute passive category income or, in the case of certain U.S. Holders, general category income for U.S. foreign tax credit limitation purposes.

Sale, Exchange or Other Disposition of ADSs or Ordinary Shares. Subject to the discussion under Passive Foreign Investment Company Rules below, upon the sale, exchange or other disposition of ADSs or ordinary shares, a U.S. Holder generally will recognize capital gain or loss equal to the difference between the amount realized upon the sale, exchange or other disposition and the adjusted tax basis of the U.S. Holder in the ADSs or ordinary shares. A U.S. Holder s tax basis in an ADS or an ordinary share will be, in general, the price it paid for that ADS or ordinary share. The capital gain or loss generally will be long-term capital gain or loss if, at the time of sale, exchange or other disposition, the U.S. Holder has held the ADS or ordinary share for more than one year. Net long-term capital gains of noncorporate U.S. Holders, including individuals, are eligible for reduced rates of taxation. The deductibility of capital loss is subject to limitations. Any gain or loss that a U.S. Holder recognizes generally will be treated as gain or loss from sources within the United States for U.S. foreign tax credit limitation purposes.

Passive Foreign Investment Company Rules. We believe that we were not a passive foreign investment company for 2007. Based on the projected composition of our income, the timing of our anticipated capital expenditures and valuation of our assets, we do not expect to be a passive foreign investment company for 2008 and do not expect to become one in the future, although this may change.

In general, we will be deemed to be a passive foreign investment company for any taxable year in which either (i) at least 75% of our gross income is passive income or (ii) at least 50% of the value (determined on the basis of a quarterly average) of our assets is attributable to assets that produce or are held for the production of passive income. For this purpose, passive income generally includes dividends, interest, royalties, rents (other than rents and royalties derived in the active conduct of a trade or business and not derived from a related person), annuities and gains from assets that produce passive income.

If we are a PFIC in any taxable year, unless a mark-to-market election described below is made, U.S. Holders will generally be subject to additional taxes and interest charges on certain excess distribution we make and on any gain realized on the disposition or deemed disposition of ADSs or ordinary shares regardless of whether we continue to be a PFIC in the year of the excess distribution or disposition. Distributions in respect of a U.S. Holder s ADSs or ordinary shares during the taxable year will generally constitute excess distributions if, in the aggregate, they exceed 125% of the average amount of distributions in respect of the U.S. Holder s ADSs or ordinary shares over the three preceding taxable years or, if shorter, the portion of the U.S. Holder s holding period before such taxable year.

To compute the tax on excess distributions or any gain, (i) the excess distribution or the gain will be allocated ratably to each day in the holding period; (ii) the amount allocated to the current year and any tax year before we became a PFIC will be taxed as ordinary income in the current year; (iii) the amount allocated to other taxable years will be taxable at the highest applicable marginal rate in effect for that year; and (iv) an interest charge at the rate for underpayment of taxes will be imposed with respect to any portion of the excess distribution or gain described under (iii) above that is allocated to such other taxable years. In addition, if we are PFIC, no distribution will qualify for taxation at the preferential rate for non-corporate holders discussed in Distributions on ADSs or Ordinary Shares above.

If we are a PFIC in any year in which our ADSs or ordinary shares are marketable , a U.S. Holder will be able to avoid the excess distribution rules described above if such U.S. Holder makes a timely mark-to-market election with respect to its ADSs or ordinary shares. The ADSs or ordinary shares will be marketable as long as they remain regularly traded on a national securities exchange, such as the New York Stock Exchange or the Hong Kong Stock Exchange. If this election is made in a timely fashion, the U.S. Holder will generally recognize as ordinary income or ordinary loss the difference between the fair market value of the ADSs or ordinary shares on the last day of any taxable year and the U.S. Holder s adjusted tax basis in the ADSs or ordinary shares. Any ordinary income resulting from this election will generally be taxed at ordinary income rates. Any ordinary losses will be deductible only to the extent of the net amount of previously included income as a result of the mark-to-market election, if any. The U.S. Holder s adjusted

tax basis in the ADSs or ordinary shares will be adjusted to reflect any such income or loss.

Alternatively, the excess distribution rules described above may generally be avoided by electing to treat us as a Qualified Electing Fund, or QEF, under Section 1295 of the Internal Revenue Code of 1986, as amended. A QEF election is available only if the U.S. Holder receives an annual information statement from the PFIC setting forth its ordinary earnings and net capital gains, as calculated for U.S. federal income tax purposes. We will not provide our U.S. Holders with the information statement necessary to make a QEF election. Accordingly, U.S. Holders will not be able to make or maintain such an election.

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A U.S. Holder is urged to consult its own tax advisors concerning the availability of making a mark-to-market election or a qualified electing fund election and the U.S. federal income tax consequences of holding the ADSs or ordinary shares if we are deemed to be a passive foreign investment company in any taxable year.

Information Reporting and Backup Withholding. In general, unless a U.S. Holder belongs to a category of certain exempt recipients (such as corporations), information reporting requirements will apply to distributions on ADSs or ordinary shares made within the United States and to the proceeds of sales of ADSs or ordinary shares that are effected through the U.S. office of a broker or the non-U.S. office of a broker that has certain connections with the United States. Backup withholding currently imposed at a rate of 28% may apply to these payments if a U.S. Holder fails to provide a correct taxpayer identification number or certification of exempt status, fails to report in full dividend and interest income or, in certain circumstances, fails to comply with applicable certification requirements. Any amounts withheld under the backup withholding rules may generally be allowed as a refund or a credit against a U.S. Holder s U.S. federal income tax, provided the U.S. Holder furnishes the required information to the Internal Revenue Service in a timely manner.

Cayman Islands Taxation

The following summary constitutes the opinion of Conyers Dill & Pearman to the material Cayman Islands tax consequences of acquiring, owning, and transferring our ADSs and ordinary shares.

The Cayman Islands currently levy no taxes on individuals or corporations based upon profits, income, gains or appreciation and there is no taxation in the nature of inheritance tax or estate duty. You will not be subject to Cayman Islands taxation on payments of dividends or upon the repurchase by us of your ADSs or ordinary shares. In addition, you will not be subject to withholding tax on payments of dividends or distributions, including upon a return of capital, nor will gains derived from the disposal of ADSs or ordinary shares be subject to Cayman Islands income or corporation tax.

No Cayman Islands stamp duty will be payable by you in respect of the issue or transfer of ADSs or ordinary shares. However, an instrument transferring title to an ADS, if brought to or executed in the Cayman Islands, would be subject to Cayman Islands stamp duty. The Cayman Islands are not party to any double taxation treaties. There are no exchange control regulations or currency restrictions in the Cayman Islands.

We were incorporated under the laws of the Cayman Islands as an exempted company and, as such, obtained an undertaking in April 2000 from the Governor in Council of the Cayman Islands substantially that, for a period of twenty years from the date of such undertaking, no law which is enacted in the Cayman Islands imposing any tax to be levied on profit or income or gains or appreciation shall apply to us and no such tax and no tax in the nature of estate duty or inheritance tax will be payable, either directly or by way of withholding, on our ADSs or ordinary shares.

Documents on Display

We are subject to the information requirements of the Securities Exchange Act of 1934, as amended. In accordance with these requirements, we file reports and other information with the Securities and Exchange Commission. These materials, including this annual report and the exhibits thereto, may be inspected and copied at the Commission s Public Reference Room at 450 Fifth Street, N.W., Washington, D.C. 20549. The public may obtain information on the operation of the Commission s Public Reference Room by calling the Commission in the United States at 1-800-SEC-0330. The Commission also maintains a website at http://www.sec.gov that contains reports, proxy statements and other information regarding registrants that file electronically with the Commission. In addition, material filed by us can be inspected at the offices of the New York Stock Exchange at 20 Broad Street, New York, New York 10005.

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Item 11. Quantitative and Qualitative Disclosures About Market Risk

Market risk is the risk of loss related to adverse changes in market prices, including foreign currency exchange rates and interest rates of financial instruments. We are exposed to these risks in the ordinary course of our business. Our exposure to these risks derives primarily from changes in interest rates and foreign currency exchange rates. To mitigate some of these risks, we utilize spot, forward, and derivative financial instruments.

Foreign Exchange Rate Fluctuation Risk

Our revenue, expense, and capital purchasing activities are primarily transacted in U.S. dollars. However, since we have operations consisting of manufacturing, sales activities and capital purchasing outside of the U.S., we enter into transactions in other currencies. We are primarily exposed to changes in exchange rate for the Euro, Japanese Yen, and Rmb.

To minimize these risks, we purchase foreign-currency forward exchange contracts with contract terms normally lasting less than six months to protect against the adverse effect that exchange rate fluctuations may have on foreign-currency denominated activities. These forward exchange contracts are principally denominated in Rmb, Japanese Yen or Euros, and do not qualify for hedge accounting in accordance with SFAS No. 133. As of December 31, 2008, we had outstanding foreign currency forward exchange contracts with notional amounts of US$220.7 million. As of December 31, 2008, the fair value of foreign currency forward exchange contracts was approximately a loss of US$3.5 million, which is recorded in other expense and other currentliabilities. We had US$220.7 million of foreign currency exchange contracts outstanding as of December 31, 2008.

We do not enter into foreign currency exchange contracts for speculative purposes. See Risk Factors Risks Related to Our Financial Condition and Business Exchange rate fluctuations could increase our costs, which could adversely affect our operating results and the value of our ADSs and Risks Related to Conducting Operations in China Devaluation or appreciation in the value of the Renminbi or restrictions on convertibility of the Renminbi could adversely affect our business and operating results.

	As of December 31, 2008 Expected maturity date (in US$ thousands)	
	2008	Unrealized Fair Value
Forward Exchange Agreement		
(Receive RMB/Pay US$)		
Contract Amount	189,543	(3,069)
(Receive EUR/Pay US$)		
Contract Amount	31,144	(441)
Total Contract Amount	220,687	(3,510)

Cross Currency Swap Fluctuation Risk

On December 15, 2005, the Company entered into a long-term loan facility agreement in the aggregate principal amount of EUR 85 million. The company is primarily exposed to changes in the exchange rate for the Euro.

To minimize the risk, the company entered into cross currency swap contracts with a contract term fully matching the repayment schedule of the long-term loan to protect against the adverse effect of exchange rate fluctuations arising from foreign-currency denominated loans. The cross currency swap contract does not qualify for hedge accounting in accordance with SFAS No. 133.

For the portion of the Euro long-term loan that is not covered by cross currency swap contracts, we have separately entered into foreign exchange forward contracts to minimize the currency risk. These foreign exchange forward contracts do not qualify for hedge accounting in accordance with SFAS No.133.

As of December 31, 2008, the Company had outstanding cross currency swap contracts with notional amounts of US$36.7 million. Notional amounts are stated in the U.S. dollar equivalents at spot exchange rates as of the respective

dates. As of December 31, 2008, the fair value of cross currency swap contracts was approximately a loss of US$0.36 million, which is recorded in other income and other current assets. We had US$36.7 million of cross currency swap contracts outstanding as of December 31, 2008, all of which will mature in 2012.

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Interest Rate Risk

Our exposure to interest rate risks relates primarily to our long-term debt obligations, which we generally assume to fund capital expenditures and working capital requirements. The table below presents annual principal amounts due and related weighted average implied forward interest rates by year of maturity for our debt obligations outstanding as of December 31, 2008. Our long-term debt obligations are all subject to variable interest rates. The interest rates on our U.S. dollar-denominated loans are linked to the LIBOR rate, while our EUR-denominated loans have interest rates linked to the EURIBOR rates. As a result, the interest rates on our loans are subject to fluctuations in the underlying interest rates to which they are linked.

	As of December 31,				
	2009	**2010**	**2011**	**2012**	**2013**
			(Forecast)		
			(in US$ thousands, except percentages)		
US$ denominated					
Average balance	754,059	361,029	133,435	37,225	
Average interest rate	1.83%	1.81%	2.03%	2.22%	
EUR denominated					
Average balance	46,551	29,789	16,201	3,245	
Average interest rate	1.99%	2.01%	2.10%	2.48%	
Weighted average forward interest rate	1.89%	1.89%	2.13%	2.32%	

Item 12. Description of Securities Other Than Equity Securities

Not applicable.

PART II

Item 13. Defaults, Dividend Arrearages, and Delinquencies

None.

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Item 14. Material Modifications to the Rights of Security Holders and Use of Proceeds

Not applicable.

Item 15. Controls and Procedures

Disclosure Controls and Procedures

Our Chief Executive Officer and our Acting Chief Financial and Accounting Officer have evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934). They have concluded that as of December 31, 2008, our disclosure controls and procedures were adequate and effective to ensure that material information relating to us and our consolidated subsidiaries was made known to them by others within our company and our consolidated subsidiaries.

Report By Management On Internal Control Over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Rule 13a-15(f) under the Securities Exchange Act of 1934, as amended, for our company. Internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of consolidated financial statements in accordance with generally accepted accounting principles and 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 a company s assets, (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of consolidated financial statements in accordance with generally accepted accounting principles, and that a company s receipts and expenditures are being made only in accordance with authorizations of a company s management and directors, and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of a company s assets that could have a material effect on the consolidated financial statements.

Because of its inherent limitations, a system of internal control over financial reporting can provide only reasonable assurance with respect to consolidated financial statement preparation and presentation and 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.

As required by Section 404 of the Sarbanes-Oxley Act of 2002 and related rules as promulgated by the Securities and Exchange Commission, management assessed the effectiveness of the internal control over financial reporting as of December 31, 2008 using criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission.

Based on this assessment, management concluded that the our internal control over financial reporting was effective as of December 31, 2008 based on the criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission.

Attestation Report of the Registered Public Accounting Firm

The effectiveness of internal control over financial reporting as of December 31, 2008 has been audited by our independent registered public accounting firm, Deloitte Touche Tohmatsu as stated in its report (See F-2).

Changes In Internal Control Over Financial Reporting

In 2008 there were no changes in our internal control over financial reporting that materially affected, or are reasonably likely to materially affect our internal control over financial reporting.

Item 16A. Audit Committee Financial Expert

Our board has determined that Mr. Lip-Bu Tan is an audit committee financial expert as defined under the applicable rules of the SEC issued pursuant to Section 407 of the Sarbanes-Oxley Act of 2002. Mr. Tan is independent as such term is defined under Section 303A.02 of the New York Stock Exchange Listed Company Manual.

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Item 16B. Code of Ethics

We have adopted a Code of Business Conduct and Ethics which is applicable to all of our employees, including our Chief Executive Officer, Acting Chief Financial and Accounting Officer, and any other persons performing similar functions.

Our Code of Business Conduct and Ethics is available, free of charge, to any person who sends a request for a paper copy to us at Semiconductor Manufacturing International Corporation, 18 Zhangjiang Road, Pudong New Area, Shanghai, China 201203, Attention: Investor Relations.

Item 16C. Principal Accountant Fees and Services

The following table sets forth the aggregate audit fees, audit-related fees, tax fees and all other fees we paid or incurred for audit services, audit-related services, tax services and other services rendered by our principal accountants during the fiscal years ended December 31, 2007 and December 31, 2008.

	2007	2008
Audit Fees	US$ 1,533,000	US$ 1,584,925
Audit-Related Fees	US$ 152,358	US$
Tax Fees	US$ 12,935	US$
Total	US$ 1,698,293	US$ 1,584,925

Audit fees consist of the standard work associated with U.S. GAAP and statutory audits of our annual financial statements including the review of our quarterly financial results and filings with the Securities and Exchange Commission, Hong Kong Stock Exchange and other regulators.

Audit-related fees include services relating to our compliance with the requirements of the Sarbanes-Oxley Act and services relating to our resolution of SEC related comments.

Tax services include tax compliance, tax advice, tax planning and transfer pricing with respect to the various regulations to which we are subject.

The audit committee has approved all audit-related services performed by Deloitte Touche Tohmatsu, 35/F, One Pacific Place, 88, Queensway, Hong Kong. The audit committee has also approved and will continue to consider, on a case-by-case basis, all non-audit services. According to the charter of our audit committee, before our principal accountants are engaged by us to render audit or non-audit services, the engagement, including the nature and scope of the work to be performed and the associated fees, must be approved by our audit committee. Our audit committee has not established any pre-approval policies and procedures.

Item 16D. Exemptions from the Listing Standards of Audit Committees

Not applicable.

Item 16E. Purchases of Equity Securities by the Issuer and Affiliated Purchasers

Pursuant to the terms of our 2001 Stock Plan, 2001 Preference Shares Stock Plan, 2001 Regulation S Stock Plan and 2001 Regulation S Preference Shares Stock Plan recipients of stock options to purchase our ordinary shares are entitled to early exercise their options, subject to our right of repurchase. When employees, directors, or service providers who have early exercised their options terminate their employment with us, we may repurchase the unvested shares subject to the option, at a price which is the lower of the exercise price of the option and the fair market value of our ordinary shares as of the date of repurchase. Other than repurchases of unvested shares upon termination of employment pursuant to these employee stock option plans, we have not repurchased any of our outstanding capital stock during 2008.

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Item 16G. Corporate Governance

We are incorporated under the laws of the Cayman Islands. The principal trading market for our shares is the Hong Kong Stock Exchange. We have adopted a set of corporate governance guidelines in accordance with the applicable laws, rule and regulations, including our Corporate Governance Policy and our Code of Business Conduct and Ethics, each of which are posted on our website.

Because our American Depositary Shares are registered with the United States Securities and Exchange Commission and are listed on the New York Stock Exchange, or the NYSE, we are also subject to certain U.S. corporate governance requirements, including many of the provisions of the Sarbanes-Oxley Act of 2002. However, because we are a foreign private issuer, many of the corporate governance rules in the NYSE Listed Company Manual, or the NYSE Standards, do not apply to us. We are permitted to follow corporate governance practices in accordance with Cayman Islands law and the Hong Kong Stock Exchange Listing Rules in lieu of most of the corporate governance standards contained in the NYSE Standards.

Set forth below is a brief summary of the significant differences between our corporate governance practices and the corporate governance standards applicable to U.S. domestic companies listed on the NYSE, or U.S. domestic issuers:

- The NYSE Standards require U.S. domestic issuers to have a nominating/corporate governance committee composed entirely of independent directors. We are not subject to this requirement, and we have not established a nominating/corporate governance committee.

- The NYSE Standards provide detailed tests that U.S. domestic issuers must use for determining independence of directors. While we may not specifically apply the NYSE tests, our board assesses independence in accordance with Hong Kong Stock Exchange Listing Rules, and in the case of audit committee members in accordance with Rule 10A-3 under the U.S. Securities and Exchange Act of 1934, as amended, and considers whether there are any relationships or circumstances which are likely to affect such director s independence from management.

- We believe that the composition of our board and its committees and their respective duties and responsibilities are otherwise generally responsive to the relevant NYSE Standards applicable to U.S. domestic issuers. However, the charters for our audit and compensation committees may not address all aspects of the NYSE Standards. For example, NYSE Standards require compensation committees of U.S. domestic issuers to produce a compensation committee report annually and include such report in their annual proxy statements or annual reports on Form 10-K. We are not subject to this requirement, and we have not addressed this in our compensation committee charter. We disclose the amounts of compensation of our directors on a named basis and the five highest individuals on an aggregate basis in our annual report in accordance with the requirements of the Hong Kong Stock Exchange Listing Rules.

- The NYSE Standards require that shareholders must be given the opportunity to vote on all equity compensation plans and material revisions to those plans. We comply with the requirements of Cayman Islands law and the Hong Kong Stock Exchange Listing Rules in determining whether shareholder approval is required, and we do not take into consideration the NYSE s detailed definition of what are considered material revisions.

The above summary is not a detailed, item-by-item analysis of the differences between our corporate governance practices and the corporate governance standards applicable to U.S. domestic issuers, but rather is intended to provide our U.S. shareholders with a brief, general summary of the significant ways that our corporate governance practices differ from those of a U.S. domestic issuer.

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PART III

Item 17. Financial Statements

We have elected to provide the financial statements and related information specified in Item 18 in lieu of Item 17.

Item 18. Financial Statements

See pages F-1 to F-80.

Item 19. Exhibits

Exhibit 1.1	Eleventh Amended and Restated Articles of Association, as adopted at the Registrant s annual general meeting of shareholders on June 2, 2008 (1)
Exhibit 4.1	Settlement Agreement dated January 31, 2005 by and between Semiconductor Manufacturing International Corporation and Taiwan Semiconductor Manufacturing Corporation, Ltd., including Patent License Agreement (2)
Exhibit 4.2	English language summary of Chinese language Syndicate Loan Agreement dated May 26, 2005, between Semiconductor Manufacturing International (Beijing) Corporation, Semiconductor Manufacturing International Corporation, as guarantor, and China Development Bank, China Construction Bank, Bank of China, Agricultural Bank of China, China Merchants Bank, HuaXia Bank, China Mingsheng Bank, Bank of Communications, Bank of Beijing, Industrial and Commercial Bank of China (Asia) and CITIC Ka Wah Bank (2)
Exhibit 4.3	Form of Indemnification Agreement, as adopted at the Registrant s annual general meeting of shareholders on May 6, 2005(2)
Exhibit 4.4	Form of Service Contract between the Company and each of its executive officers
Exhibit 4.5	Form of Service Contract between the Company and each of its directors
Exhibit 4.6	English language summary of Chinese language Syndicate Loan Agreement dated May 31, 2006, between Semiconductor Manufacturing International (Tianjin) Corporation, Semiconductor Manufacturing International Corporation, as guarantor, and China Construction Bank, China Minsheng Bank, China Development Bank, Industrial and Commercial Bank of China, Agricultural Bank of China, Bank of China, China Merchants Bank, China Bo Hai Bank, Bank of Communications and Bangkok Bank (3)
Exhibit 4.7	English language summary of Chinese language Syndicate Loan Agreement dated June 8, 2006, between Semiconductor Manufacturing International (Shanghai) Corporation, Semiconductor Manufacturing International Corporation, as guarantor, and ABN AMRO Bank N.V., Bank of China (Hong Kong) Limited, Bank of Communications, The Bank of Tokyo-Mitsubishi UFJ, Ltd., China Construction Bank, DBS Bank Ltd., Fubon Bank (Hong Kong) Limited, Industrial and Commercial Bank of China and Shanghai Pudong Development Bank (3)
Exhibit 4.8	Share Purchase Agreement, dated November 6, 2008, by and between the Company and Datang Telecom Technology & Industry Holdings Limited Co., Ltd.(4)
Exhibit 4.9	English language translation of Strategic Cooperation Agreement, dated December 24, 2008 by and between the Company and Datang Telecom Technology & Industry Holdings Co., Ltd. (5)
Exhibit 8.1	List of Subsidiaries

Exhibit 12.1	Certification of CEO under Section 302 of the U.S. Sarbanes-Oxley Act of 2002
Exhibit 12.2	Certification of Acting CFO under Section 302 of the U.S. Sarbanes-Oxley Act of 2002
Exhibit 13.1	Certification of CEO and Acting CFO under Section 906 of the U.S. Sarbanes-Oxley Act of 2002
Exhibit 99.1	Consent of Deloitte Touche Tohmatsu

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(1) Previously filed as an exhibit to the Registrant s Annual Report on Form 20F for the fiscal year ended December 31, 2007, filed June 27, 2008 and amended November 28, 2008.

(2) Previously filed as an exhibit to the Registrant s Annual Report on Form 20F for the fiscal year ended December 31, 2004, filed June 28, 2005. With respect to Exhibit 4.1, please refer to Item 8 Litigation in the Registrant s Annual Report on Form 20F for the fiscal year ended December 31, 2008.

(3) Previously filed as an exhibit to the Registrant s Annual Report on Form 20F for the fiscal year ended December 31, 2005, filed June 28, 2006.

(4) Previously filed as an exhibit to the Registrant s Form 6-K dated November 17, 2008. Portions of this exhibit were omitted and filed separately with the Commission pursuant to Rule 24b-2 of the Securities Exchange Act of 1934, as amended, concerning confidential treatment.

(5) Previously filed as an exhibit to the Registrant s Form 6-K dated January 5, 2009. Portions of this exhibit were omitted and filed separately with the Commission pursuant to Rule 24b-2 of the Securities Exchange Act of 1934, as amended, concerning confidential treatment.

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SIGNATURES

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.

SEMICONDUCTOR MANUFACTURING INTERNATIONAL CORPORATION

Date: June 22, 2009

By: /s/ Richard Ru Gin Chang
Name: Richard Ru Gin Chang
Title: President and Chief Executive Officer

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders of Semiconductor Manufacturing International Corporation:

We have audited the accompanying consolidated balance sheets of Semiconductor Manufacturing International Corporation and subsidiaries (the Company) as of December 31, 2008, 2007 and 2006, and the related consolidated statements of operations, stockholders equity and comprehensive income (loss), and cash flows for each of the three years in the period ended December 31, 2008. Our audit also included the financial statement schedule included in Schedule I. We also have audited the Company 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 Company s management is responsible for these financial statements, 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 Report by Management on Internal Control over Financial Reporting. Our responsibility is to express an opinion on these financial statements and an opinion on the Company s internal control over financial reporting 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 and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting 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 audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company s internal control over financial reporting is a process designed by, or under the supervision of, the company s principal executive and principal financial officers, or persons performing similar functions, and effected by the company s board of directors, management, and other personnel 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 the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the 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 consolidated financial statements referred to above present fairly, in all material respects, the financial position of Semiconductor Manufacturing International Corporation and subsidiaries as of December 31, 2008, 2007 and 2006 and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2008, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, such financial statement schedule, when considered in relation to the basic consolidated financial statements taken as whole, present fairly, in all material respects, the information set forth therein. Also, in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2008, based on the criteria established in Internal Control Integrated

Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission.
As discussed in Note 2(s), effective January 1, 2007, the Company adopted FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes an Interpretation of FASB Statement No. 109 .
Deloitte Touche Tohmatsu
Certified Public Accountants
Hong Kong
April 17, 2009, except for Note 28 and Schedule I, as to which the date is June 22, 2009

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SEMICONDUCTOR MANUFACTURING INTERNATIONAL CORPORATION
CONSOLIDATED BALANCE SHEETS
(In US dollars, except share data)

	NOTES	2008	December 31, 2007	2006
ASSETS				
Current assets:				
Cash and cash equivalents		**$ 450,229,569**	$ 469,284,013	$ 363,619,731
Restricted Cash		**6,254,813**		
Short-term investments	5	**19,928,289**	7,637,870	57,950,603
Accounts receivable, net of allowances of $5,680,658, $4,492,090 and $4,048,845 at December 31, 2008, 2007 and 2006, respectively	7	**199,371,694**	298,387,652	252,184,975
Inventories	8	**171,636,868**	248,309,765	275,178,952
Prepaid expense and other current assets		**56,299,086**	31,237,755	20,766,945
Receivable for sale of manufacturing equipment		**23,137,764**	17,321,000	70,544,560
Assets held for sale	9		3,123,567	9,420,729
Total current assets		**926,858,083**	1,075,301,622	1,049,666,495
Land use rights, net	10	**74,293,284**	57,551,991	38,323,333
Plant and equipment, net	11	**2,963,385,840**	3,202,957,665	3,244,400,822
Acquired intangible assets, net	13	**200,059,106**	232,195,132	71,692,498
Deferred cost, net	28	**47,091,516**	70,637,275	94,183,034
Equity investment	14	**11,352,186**	9,896,398	13,619,643
Other long-term prepayments		**1,895,337**	2,988,404	4,119,433
Deferred tax assets	19	**45,686,470**	56,915,172	25,286,900
TOTAL ASSETS		**$ 4,270,621,822**	$ 4,708,443,659	$ 4,541,292,158
LIABILITIES AND STOCKHOLDERS EQUITY				
Current liabilities:				
Accounts payable	15	**$ 185,918,539**	$ 301,992,739	$ 309,129,199
Accrued expenses and other current liabilities		**122,173,803**	150,109,963	97,121,231
Short-term borrowings	17	**201,257,773**	107,000,000	71,000,000
Current portion of promissory note	16	**29,242,001**	29,242,000	29,242,001
Current portion of long-term debt	17	**360,628,789**	340,692,788	170,796,968
Income tax payable		**552,006**	1,152,630	72,417
Total current liabilities		**899,772,911**	930,190,120	677,361,816
Long-term liabilities:				

Promissory notes	16	**23,589,958**	51,057,163	77,601,657
Long-term debt	17	**536,518,281**	616,294,743	719,570,905
Long-term payables relating to license agreements	18	**18,169,006**	62,833,433	16,992,950
Other long term liabilities				3,333,333
Deferred tax liabilities	19	**411,877**	604,770	210,913
Total long-term liabilities		**578,689,122**	730,790,109	817,709,758
Total liabilities		**1,478,462,033**	1,660,980,229	1,495,071,574
Commitments	25			
Minority interest	20	**42,795,288**	34,944,408	38,800,666
Stockholders equity:				
Ordinary shares, $0.0004 par value, 50,000,000,000 shares authorized, 22,327,784,827, 18,558,919,712 and 18,432,756,463 shares issued and outstanding at December 31, 2008, 2007 and 2006, respectively	21	**8,931,114**	7,423,568	7,373,103
Additional paid-in capital		**3,489,382,267**	3,313,375,972	3,288,765,465
Accumulated other comprehensive (loss) income		**(439,123)**	(1,881)	91,840
Accumulated deficit		**(748,509,757)**	(308,278,637)	(288,810,490)
Total stockholders equity		**2,749,364,501**	3,012,519,022	3,007,419,918
TOTAL LIABILITIES AND STOCKHOLDERS EQUITY		**$ 4,270,621,822**	$ 4,708,443,659	$ 4,541,292,158

The accompanying notes are an integral part of these consolidated financial statements.

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SEMICONDUCTOR MANUFACTURING INTERNATIONAL CORPORATION
CONSOLIDATED STATEMENTS OF OPERATIONS
(In US dollars, except share data)

	NOTES	Year ended December 31, 2008	2007	2006
Sales	26	**$ 1,353,711,299**	$ 1,549,765,288	$ 1,465,322,867
Cost of sales		**1,412,851,079**	1,397,037,881	1,338,155,004
Gross (loss) profit		**(59,139,780)**	152,727,407	127,167,863
Operating expenses (income):				
Research and development		**102,239,779**	97,034,208	94,170,750
General and administrative		**58,841,103**	74,489,877	47,364,533
Selling and marketing		**20,661,254**	18,715,961	18,231,048
Amortization of acquired intangible assets		**32,191,440**	27,070,617	24,393,561
Impairment loss of long-lived assets	12,13	**106,740,667**		
Income from sale of equipment and other fixed assets	9,11	**(2,877,175)**	(28,651,446)	(43,121,929)
Total operating expenses, net		**317,797,068**	188,659,217	141,037,963
Loss from operations	31	**(376,936,848)**	(35,931,810)	(13,870,100)
Other income (expense):				
Interest income		**11,542,339**	12,348,630	14,916,323
Interest expense		**(50,766,958)**	(37,936,126)	(50,926,084)
Foreign currency exchange gain (loss)		**3,229,710**	11,249,889	(21,912,234)
Others, net		**7,428,721**	2,237,902	1,821,337
Total other expense, net		**(28,566,188)**	(12,099,705)	(56,100,658)
Loss before income tax		**(405,503,036)**	(48,031,515)	(69,970,758)
Income tax benefit (expense)	19	**(26,432,993)**	29,719,775	24,927,744
Minority interest		**(7,850,880)**	2,856,258	(18,803)
Loss from equity investment	14	**(444,211)**	(4,012,665)	(4,201,247)
Net loss before cumulative effect of a change in accounting principle		**(440,231,120)**	(19,468,147)	(49,263,064)
Cumulative effect of a change in accounting principle				5,153,986
Net loss		**$ (440,231,120)**	$ (19,468,147)	$ (44,109,078)
On the basis of net loss before accounting change per share, basic and diluted	23	**$ (0.02)**	$ (0.00)	$ (0.00)

Cumulative effect of an accounting change per share, basic and diluted	23	**$**		$		$ 0.00
Loss per share, basic and diluted	23	**$**	**(0.02)**	$	(0.00)	$ (0.00)
Shares used in calculating basic and diluted loss per share	23		**18,682,544,866**		18,501,940,489	18,334,498,923

The accompanying notes are an integral part of these consolidated financial statements.

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SEMICONDUCTOR MANUFACTURING INTERNATIONAL CORPORATION
CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY AND COMPREHENSIVE INCOME (LOSS)
(In US dollars, except share data)

	Ordinary		Additional paid-in	Accumulated other comprehensive income	Deferred stock compensation,	Accumulated	Total stockholders	Comprehen
	Share	Amount	capital	(loss)	net	deficit	equity	loss
nce at ary 1,	18,301,680,867	$ 7,320,673	$ 3,291,439,835	$ 138,978	$ (24,881,919)	$ (244,701,412)	$ 3,029,316,155	
cise of k options	132,744,596	53,098	3,912,210				3,965,308	
urchase of cted nary es	(1,669,000)	(668)	(57,522)				(58,190)	
rred stock pensation stment			(24,881,919)		24,881,919			
e-based pensation			23,506,847				23,506,847	
ulative t of a ge in unting iple			(5,153,986)				(5,153,986)	
oss gn ncy lation stments						(44,109,078)	(44,109,078)	$ (44,109,
zed gain stments				(16,885)			(16,885)	(16,
				(30,253)			(30,253)	(30,
nce at mber 31,	18,432,756,463	$ 7,373,103	$ 3,288,765,465	$ 91,840	$	$ (288,810,490)	$ 3,007,419,918	$ (44,156,
cise of k options	126,455,749	50,582	3,988,549				4,039,131	
urchase of cted nary	(292,500)	(117)	(21,383)				(21,500)	

es e-based pensation			20,643,341				20,643,341		
oss gn ncy lation stments				(93,721)		(19,468,147)	(19,468,147)	$	(19,468, (93,
nce at mber 31,	18,558,919,712	$ 7,423,568	$ 3,313,375,972	$ (1,881)	$	$ (308,278,637)	$ 3,012,519,022	$	(19,561,
cise of k options	69,770,815	27,908	768,361				796,269		
nce of nary es to a tholder	3,699,094,300	1,479,638	163,620,362				165,100,000		
e-based pensation			11,617,572				11,617,572		
oss gn ncy lation stments				(437,242)		(440,231,120)	(440,231,120) (437,242)	$	(440,231, (437,
nce at mber 31,	22,327,784,827	$ 8,931,114	$ 3,489,382,267	$ (439,123)	$	$ (748,509,757)	$ 2,749,364,501	$	(440,668,

The accompanying notes are an integral part of these consolidated financial statements.

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SEMICONDUCTOR MANUFACTURING INTERNATIONAL CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS
(In US dollars)

	Year ended December 31,		
	2008	2007	2006
Operating activities:			
Net Loss	**$ (440,231,120)**	$ (19,468,147)	$ (44,109,078)
Less: Cumulative effect of a change in accounting principle			(5,153,986)
Net loss before cumulative effect of a change in accounting principle	**(440,231,120)**	(19,468,147)	(49,263,064)
Adjustments to reconcile net loss to net cash provided by operating activities:			
Minority interest	**7,850,880**	(2,856,258)	18,803
Deferred taxes	**11,035,809**	(31,234,415)	(25,075,987)
Income from sale of equipment and other fixed assets	**(2,877,175)**	(28,651,446)	(43,121,929)
Depreciation and amortization	**761,808,822**	706,277,464	919,616,493
Non-cash interest expense on promissory note and long-term payable relating to license agreements	**6,915,567**	4,762,343	5,702,607
Amortization of acquired intangible assets	**32,191,440**	27,070,616	24,393,561
Share-based compensation	**11,617,572**	20,643,341	23,506,847
Loss from equity investment	**444,211**	4,012,665	4,201,247
Impairment loss of long-lived assets	**106,740,667**		
Changes in operating assets and liabilities:			
Accounts receivable, net	**99,015,958**	(46,202,677)	(10,851,061)
Inventories	**76,672,897**	26,869,187	(83,941,316)
Prepaid expense and other current assets	**(23,968,264)**	(9,339,779)	(8,926,442)
Accounts payable	**(76,827,049)**	19,852,824	24,705,615
Accrued expenses and other current liabilities	**(7,487)**	2,982,369	(14,722,249)
Income tax payable	**(600,624)**	1,080,213	72,417
Other long term liabilities		(3,333,333)	3,333,333
Net cash provided by operating activities	**569,782,104**	672,464,967	769,648,875
Investing activities:			
Purchase of plant and equipment	**(669,054,599)**	(717,170,957)	(882,580,833)
Proceeds from government grant to purchase plant and equipment	**4,181,922**		2,208,758
Proceeds from sale of equipment	**2,319,597**	98,128,041	4,044,702
Proceeds received from sale of assets held for sale	**563,008**	16,476,045	12,716,742
Purchase of acquired intangible assets	**(79,277,586)**	(90,090,114)	(9,573,524)
Acquisition of minority interest		(1,000,000)	
Purchase of short-term investments	**(291,007,766)**	(135,241,799)	(135,058,817)
Sale of short-term investments	**278,717,347**	185,554,532	90,873,820
Change in restricted cash	**(6,254,813)**		
Purchase of equity investment	**(1,900,000)**		
Net cash used in investing activities	**(761,712,890)**	(643,344,252)	(917,369,152)

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SEMICONDUCTOR MANUFACTURING INTERNATIONAL CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS
(In US dollars)

	Year ended December 31,		
	2008	2007	2006
Financing activities:			
Proceeds from short-term borrowings	**422,575,386**	201,658,000	255,003,999
Repayment of short-term borrowings	**(328,317,613)**	(165,658,000)	(449,485,081)
Proceeds from long-term debt	**285,929,954**	262,247,672	785,344,546
Repayment of long-term debt	**(345,770,415)**	(195,628,015)	(635,613,638)
Repayment of promissory note	**(30,000,000)**	(30,000,000)	(30,000,000)
Payment of loan initiation fee			(3,596,938)
Proceeds from exercise of employee stock options	**796,269**	4,039,131	3,965,308
Proceeds from issuance of ordinary shares	**168,100,000**		
Repurchase of restricted ordinary shares		(21,500)	(58,190)
Net cash provided by (used in) financing activities	**173,313,581**	76,637,288	(74,439,994)
Effect of exchange rate changes	**(437,239)**	(93,721)	(16,885)
NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	**(19,054,444)**	105,664,282	(222,177,156)
CASH AND CASH EQUIVALENTS, beginning of year	**469,284,013**	363,619,731	585,796,887
CASH AND CASH EQUIVALENTS, end of year	**$ 450,229,569**	$ 469,284,013	$ 363,619,731
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:			
Income taxes paid	**$ 15,997,808**	$ 435,109	$ 164,409
Interest paid	**$ 54,423,059**	$ 45,322,891	$ 46,808,533
SUPPLEMENTAL DISCLOSURES OF INVESTING AND FINANCING ACTIVITIES			
Accounts payable for plant and equipment	**$ (99,592,362)**	**$ (138,839,513)**	$ (165,828,795)
Long-term payable for acquired intangible assets	**$ (18,169,006)**	$ (62,833,433)	$ (16,992,950)
Receivables for sales of manufacturing equipment	**$ 23,137,764**	$ 17,321,000	$ 70,544,560

The accompanying notes are an integral part of these consolidated financial statements.

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SEMICONDUCTOR MANUFACTURING INTERNATIONAL CORPORATION
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
For the years ended December 31, 2008, 2007 and 2006
(In US dollars, except where otherwise stated)

1. ORGANIZATION AND PRINCIPAL ACTIVITIES

Semiconductor Manufacturing International Corporation was incorporated under the laws of the Cayman Islands on April 3, 2000. As of December 31, 2008, the Company operates primarily through the following subsidiaries:

Name of company	Place and date of incorporation/ establishment	Attributable equity interest held	Principal activity
Better Way Enterprises Limited (Better Way)	Samoa April 5, 2000	100%	Trading of semiconductor products
Semiconductor Manufacturing International (Shanghai) Corporation (SMIS)*#	PRC December 21, 2000	100%	Manufacturing and trading of semiconductor products
SMIC, Americas	United States of America June 22, 2001	100%	Marketing related activities
Semiconductor Manufacturing International (Beijing) Corporation (SMIB)*#	PRC July 25, 2002	100%	Manufacturing and trading of semiconductor products
SMIC Japan Corporation*	Japan October 8, 2002	100%	Marketing related activities
SMIC Europe S.R.L	Italy July 3, 2003	100%	Marketing related activities
SMIC Commercial (Shanghai) Limited Company (formerly SMIC Consulting Corporation)*#	PRC September 30, 2003	100%	Operation of a convenience store
Semiconductor Manufacturing International (Tianjin) Corporation (SMIT)*#	PRC November 3, 2003	100%	Manufacturing and trading of semiconductor products
Semiconductor Manufacturing International (AT) Corporation (AT)*	Cayman Islands July 26, 2004	57.3%	Investment holding
Semiconductor Manufacturing International (Chengdu) Corporation (SMICD)*#	PRC December 28, 2004	57.3%	Manufacturing and trading of semiconductor products
SMIC Energy Technology	PRC	100%	

(Shanghai) Corporation (Energy Science)*#	September 9, 2005	Manufacturing and trading of solar cells and modules

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SEMICONDUCTOR MANUFACTURING INTERNATIONAL CORPORATION
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
For the years ended December 31, 2008, 2007 and 2006
(In US dollars, except where otherwise stated)

Name of company	Place and date of incorporation/ establishment	Attributable equity interest held	Principal activity
SMIC Development (Chengdu) Corporation*#	PRC December 29, 2005	100%	Construction, operation, and management of SMICD s living quarter, schools, and supermarket
Magnificent Tower Limited	British Virgin Islands January 5, 2006	100%	Investment holding
Semiconductor Manufacturing International (BVI) Corporation	British Virgin Islands April 26, 2007	100%	Trading of semiconductor products
Admiral Investment Holdings Limited	British Virgin Islands October 10, 2007	100%	Investment holding
SMIC Shenzhen (HK) Company Limited	Hong Kong January 29, 2008	100%	Investment holding
Semiconductor Manufacturing International (Shenzhen) Corporation*#	PRC March 20, 2008	100%	Manufacturing and trading of semiconductor products

 # Companies registered as wholly foreign-owned enterprises in the People s Republic of China (PRC), excluding for the purpose of this annual report, Hong Kong, Macau and Taiwan.

** For identification*

purposes only

In addition to the above, the Company has a number of wholly-owned subsidiaries in the PRC, Hong Kong, Samoa, the British Virgin Islands and Cayman Islands.

Semiconductor Manufacturing International Corporation and its subsidiaries (hereinafter collectively referred to as the Company or SMIC) are mainly engaged in the computer-aided design, manufacturing, packaging, testing and trading of integrated circuits and other semiconductor services, as well as manufacturing and designing semiconductor masks.

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SEMICONDUCTOR MANUFACTURING INTERNATIONAL CORPORATION
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
For the years ended December 31, 2008, 2007 and 2006
(In US dollars, except where otherwise stated)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(a) Basis of presentation

The consolidated financial statements of the Company are prepared in accordance with accounting principles generally accepted in the United States of America (US GAAP).

(b) Principles of consolidation

The consolidated financial statements include the accounts of the Company and its majority owned subsidiaries. All inter-company transactions and balances have been eliminated upon consolidation.

(c) Use of estimates

The preparation of financial statements in conformity with US GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and revenue and expenses in the financial statements and accompanying notes. Significant accounting estimates reflected in the Company s financial statements include valuation allowance for deferred tax assets, allowance for doubtful accounts, inventory valuation, non- marketable equity investment valuation, useful lives and commencement of productive use for plant and equipment and acquired intangible assets, impairment of long-lived assets, accruals for sales adjustments, accrued expenses, contingencies and assumptions related to the valuation of share-based compensation and related forfeiture rates.

(d) Cash and cash equivalents

Cash and cash equivalents consist of cash on hand and highly liquid investments which are unrestricted as to withdrawal or use, and which have maturities of three months or less when purchased.

(e) Restricted Cash

Restricted cash consists of bank deposits pledged against short-term credit facilities and unused government grants for fab construction.

(f) Investments

Short-term investments consist primarily of debt instruments and mutual funds are classified either as held-tomaturity, available-for-sale or trading securities.

Held-to-maturity securities are recorded at amortized cost.

Available-for-sale securities are recorded at fair market value. Unrealized gains and losses are recorded as part of accumulated other comprehensive income (loss). The unrealized gains and losses are reclassified to earnings once the available-for-sale investments are settled. Unrealized losses, which are deemed other than temporary, are recorded in the statement of operations as other expenses.

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SEMICONDUCTOR MANUFACTURING INTERNATIONAL CORPORATION
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
For the years ended December 31, 2008, 2007 and 2006
(In US dollars, except where otherwise stated)

Trading securities are recorded at fair value with unrealized gains and losses classified in earnings.

Equity investments are recorded in long-term assets and accounted for under the equity method when the Company has the ability to exercise significant influence, but not control, over the investee or under the cost method when the investment does not qualify for the equity method. Equity method investments only include non-marketable investments.

Available-for-sale and non-marketable equity investments are evaluated for impairment when the Company identifies indicator of impairment. Investments are considered to be impaired when a decline in fair value is judged to be other than temporary, when events or circumstances are identified that would significantly harm the fair value of the investment and the fair value is significantly below cost basis and /or the significant decline has lasted for an extended period of time. If the investment is other than temporarily impaired, the investment would be written down to its fair value.

(g) Concentration of credit risk

Financial instruments that potentially expose the Company to concentrations of credit risk consist primarily of cash and cash equivalents, short-term investments, accounts receivable, other current assets and receivable for sale of manufacturing equipment. The Company places its cash and cash equivalents with reputable financial institutions.

The Company conducts credit evaluations of customers and generally does not require collateral or other security from its customers. The Company establishes an allowance for doubtful accounts based upon estimates, factors surrounding the credit risk of specific customers and other information.

(h) Inventories

Inventories are stated at the lower of cost (weighted average) or market. Cost comprises direct materials, direct labor costs and those overheads costs that were incurred in bringing the inventories to their present location and condition.

Adjustments are recorded to write down the cost of obsolete and excess inventory to the estimated market value based on historical and forecasted demand. In 2008, 2007 and 2006, inventory was written down by $40,818,979, $22,676,608 and $16,106,471, respectively, and recorded in cost of sales to reflect the lower of cost or market adjustments.

(i) Land use rights, net

Land use rights are recorded at cost less accumulated amortization. Amortization is provided over the term of the land use right agreement on a straight-line basis over the terms of the agreements, which range from 50 to 70 years.

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(j) Plant and equipment, net

Plant and equipment are carried at cost less accumulated depreciation and are depreciated on a straight-line basis over the following estimated useful lives:

Buildings	25 years
Facility, machinery and equipment	10 years
Manufacturing machinery and equipment	5-7 years
Furniture and office equipment	3-5 years
Transportation equipment	5 years

The Company constructs certain of its plant and equipment. In addition to costs under the construction contracts, external costs directly related to the construction of such facilities, including duties and tariffs, equipment installation and shipping costs, are capitalized. Interest incurred on funds used to construct plant and equipment during the active construction period is capitalized, net of government subsidies received. See Note 2(n). Depreciation is recorded at the time assets are ready for their intended use.

(k) Acquired intangible assets

Acquired intangible assets, which consist primarily of technology, licenses and patents, are carried at cost less accumulated amortization. Amortization is computed using the straight-line method over the expected useful lives of the assets of 3 to 10 years.

(l) Impairment of long-lived assets

The Company assesses the impairment of long-lived assets when events or changes in circumstances indicate that the carrying value of the assets or the asset group may not be recoverable. Factors that we consider in deciding when to perform an impairment review include, but are not limited to significant under-performance of a business or product line in relation to expectations, significant negative industry or economic trends, and significant changes or planned changes in our use of the assets. An impairment analysis is performed at the lowest level of identifiable independent cash flows for an asset or asset group. We make subjective judgments in determining the independent cash flows that can be related to specific asset group based on our asset usage model and manufacturing capabilities. We measure the recoverability of assets that will continue to be used in our operations by comparing the carrying value of the asset group to our estimate of the related total future undiscounted cash flows. If an asset group s carrying value is not recoverable through the related undiscounted cash flows, the impairment loss is measured by comparing the difference between the asset group s carrying value and its fair value, based on the best information available, including market prices or discounted cash flow analysis.

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(m) Revenue recognition

The Company manufactures semiconductor wafers for its customers based on the customers designs and specifications pursuant to manufacturing agreements and/or purchase orders. The Company also sells certain semiconductor standard products to customers. Revenue is recognized when persuasive evidence of an arrangement exists, service has been performed, the fee is fixed or determinable and collectability is reasonably assured. Sales to customers are recognized upon shipment and title transfer, if all other criteria have been met. The Company also provides certain services, such as mask making, testing and probing. Revenue is recognized when the services are completed or upon shipment of semiconductor products, if all other criteria have been met.

Customers have the right of return within one year pursuant to warranty and sales return provisions. The Company typically performs tests of its products prior to shipment to identify yield rate per wafer. Occasionally, product tests performed after shipment identify yields below the level agreed with the customer. In those circumstances, the customer arrangement may provide for a reduction to the price paid by the customer or for the costs to return products and to ship replacement products to the customer. The Company estimates the amount of sales returns and the cost of replacement products based on the historical trend of returns and warranty replacements relative to sales as well as a consideration of any current information regarding specific known product defects that may exceed historical trends.

The Company provides management services to certain government-owned foundries. Service revenue is recognized when persuasive evidence of an arrangement exists, service has been performed, the fee is fixed or determinable, and collectability is reasonably assured.

(n) Capitalization of interest

Interest incurred on funds used to construct plant and equipment during the active construction period is capitalized, net of government subsidies received. The interest capitalized is determined by applying the borrowing interest rate to the average amount of accumulated capital expenditures for the assets under construction during the period. Capitalized interest is added to the cost of the underlying assets and is amortized over the useful life of the assets. Government subsidies, capitalized interest and net interest expense are as follows:

	For the year ended December 31,		
	2008	2007	2006
Total actual interest expense	**$ 70,735,520**	$ 72,686,950	$ 78,120,699
Less: Government subsidy	**9,308,764**	27,083,604	22,396,613
Less: Capitalized interest	**10,659,798**	7,667,220	4,798,002
Net interest expense	**$ 50,766,958**	$ 37,936,126	$ 50,926,084

(o) Government subsidies

The Company received the following types of government subsidies:

(1) Reimbursement of certain interest costs incurred on borrowings

The Company received government subsidies in cash of $9,308,764, $27,083,604 and $22,396,613 in 2008, 2007 and 2006, respectively, which were based on the interest expense on the Company s budgeted borrowings. The Company records government subsidies as a reduction of interest expense on an accrual basis.

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(2) Government awards

The Company received government awards of $56,967,187, $5,058,722 and $11,886,551 in the form of reimbursement of certain expenses in 2008, 2007 and 2006, respectively. These awards were recorded as reductions of related expenses, primarily research and development.

(3) Government subsidy for fab construction

Certain local governments provided subsidies to encourage the Company to participate and manage new plants relating to the integrated circuit industry.

As of December 31, 2008, the Company received $7,324,792, of which $4,181,922 has been used to offset the cost of construction in progress. The unused balance of $3,142,870 is recorded in restricted cash.

In 2006, the Company received a government subsidy of $2,208,758 as a reimbursement of land use right payment, which has been used to offset the cost of the land use rights.

(p) Research and development costs

Research and development costs are expensed as incurred and reported net of related government subsidies.

(q) Start-up costs

In accordance with Statement of Position No. 98-5, Reporting on the costs of start-up activities, the Company expenses all costs incurred in connection with start-up activities, including preproduction costs associated with new manufacturing facilities and costs incurred with the formation of these facilities such as organization costs. Preproduction costs including the design, formulation and testing of new products or process alternatives are included in research and development expenses. Preproduction costs including facility and employee costs incurred in connection with constructing new manufacturing plants are included in general and administrative expenses.

(r) Foreign currency translation

The United States dollar (US dollar), the currency in which a substantial portion of the Company s transactions are denominated, is used as the functional and reporting currency of the Company. Monetary assets and liabilities denominated in currencies other than the US dollar are translated into US dollar at the rates of exchange ruling at the balance sheet date. Transactions in currencies other than the US dollar during the year are converted into the US dollar at the applicable rates of exchange prevailing on the transaction dates. Transaction gains and losses are recognized in the statements of operations.

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The financial records of certain of the Company s subsidiaries are maintained in local currencies other than the US dollar, such as Japanese Yen, which are their functional currencies. Assets and liabilities are translated at the exchange rates at the balance sheet date. Equity accounts are translated at historical exchange rates, and revenues, expenses, gains and losses are translated using the monthly weighted average exchange rates. Translation adjustments are reported as cumulative translation adjustments and are shown as a separate component of other comprehensive income (loss) in the statements of stockholders equity and comprehensive income (loss).

(s) Income taxes

Current income taxes are provided for in accordance with the laws of the relevant taxing authorities.

As part of the process of preparing financial statements, the Company is required to estimate its income taxes in each of the jurisdictions in which it operates. The Company accounts for income taxes using the liability method. Under this method, deferred income taxes are recognized for tax consequences in future years of differences between the tax bases of assets and liabilities and their financial reporting amounts at each year-end, based on enacted laws and statutory tax rates applicable for the difference that are expected to affect taxable income. Valuation allowances are provided if, based on available evidence, it is more likely than not that some or all of the deferred tax assets will not be realized.

On January 1, 2007, the Company adopted FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes an Interpretation of FASB Statement No. 109 (FIN 48), which prescribes a more-likely-than-not threshold for financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. This interpretation also provides guidance on de-recognition of income tax assets and liabilities, classification of current and deferred income tax assets and liabilities, accounting for interest and penalties associated with tax positions, accounting for income taxes in interim periods and income tax disclosures.

(t) Comprehensive income (loss)

Comprehensive income (loss) includes such items as net loss, foreign currency translation adjustments and unrealized income (loss) on available-for-sales securities. Comprehensive income (loss) is reported in the statements of stockholders equity and comprehensive income (loss).

(u) Fair value of financial instruments

On January 1, 2008, the Company adopted the provisions of Financial Accounting Standards Board (FASB) Statement of Financial Accounting Standards (SFAS) No. 157 Fair Value Measurements (SFAS 157) for all financial assets and financial liabilities recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually). The Company has deferred its implementation of the provisions of SFAS No. 157 for all non-financial assets and liabilities in accordance with FASB Staff Position (FSP) FAS 157-2, Effective Date of FASB Statement No. 157 (FSP 157-2), SFAS No. 157 defines fair value, establishes a framework for measuring fair value, and enhances fair value measurement disclosure. The adoption of SFAS No. 157 did not have a significant impact on our consolidated financial statements, and the resulting fair values calculated under SFAS No. 157 after adoption were not significantly different than the fair values that would have been calculated under previous guidance.

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In October 2008, the FASB issued FSP FAS 157-3, Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active (FSP 157-3). FSP 157-3 clarifies the application of SFAS No. 157 in a market that is not active, and addresses application issues such as the use of internal assumptions when relevant observable data does not exist, the use of observable market information when the market is not active, and the use of market quotes when assessing the relevance of observable and unobservable data. FSP 157-3 is effective for all periods presented in accordance with SFAS No. 157. The adoption of FSP 157-3 did not have a significant impact on our consolidated financial statements or the fair values of our financial assets and liabilities.

When available, the Company measures the fair value of financial instruments based on quoted market prices in active markets, valuation techniques that use observable market-based inputs or unobservable inputs that are corroborated by market data. Pricing information the Company obtains from third parties is internally validated for reasonableness prior to use in the consolidated financial statements. When observable market prices are not readily available, the Company generally estimates the fair value using valuation techniques that rely on alternate market data or inputs that are generally less readily observable from objective sources and are estimated based on pertinent information available at the time of the applicable reporting periods. In certain cases, fair values are not subject to precise quantification or verification and may fluctuate as economic and market factors vary and the Company s evaluation of those factors changes. Although the Company uses its best judgment in estimating the fair value of these financial instruments, there are inherent limitations in any estimation technique. In these cases, a minor change in an assumption could result in a significant change in its estimate of fair value, thereby increasing or decreasing the amounts of the Company s consolidated assets, liabilities, stockholders equity (deficit) and net income or loss. See Note 4, Fair Value , for further details.

On January 1, 2008, the Company adopted SFAS No. 159, Fair Value of Option for Financial Assets and Financial Liabilities including an amendment of FASB Statement No.115 (SFAS 159). SFAS 159 permits companies to choose to measure certain financial instruments and other items at fair value using an instrument-by-instrument election. The Company does not elect to use the fair value option and therefore, the adoption of SFAS 159 did not have a material impact on the Company s consolidated financial position or result of operations.

(v) Share-based compensation

The Company grants stock options to its employees and certain non-employees. Under the provisions of SFAS 123(R), share-based compensation cost is measured at the grant date, based on the fair value of the award, and is recognized as an expense over the employee s requisite service period (generally the vesting period of the equity grant).

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The Company s total actual share-based compensation expense for the years ended December 31, 2008, 2007 and 2006 was $11,617,572, $20,643,341 and $23,506,847, respectively.

(w) Derivative financial instruments

The Company s primary objective for holding derivative financial instruments is to manage currency and interest rate risks. The Company records derivative instruments as assets or liabilities, measured at fair value. The Company does not offset the carrying amounts of derivatives with the same counterparty in accordance with FASB Interpretation (FIN) No. 39, Offsetting of Amounts Related to Certain Contracts an interpretation of APB Opinion No. 10 and FASB Statement No. 105 (FIN 39) as amended. The recognition of gains or losses resulting from changes in the values of those derivative instruments is based on the use of each derivative instrument. The Company does not have any derivative instruments that qualify for hedge accounting.

(x) Recently issued accounting standards

In December 2007, the FASB issued SFAS No. 141, Business Combinations: (Revised 2007) (SFAS 141R). SFAS 141R is relevant to all transactions or events in which one entity obtains control over one or more other businesses. SFAS 141R requires an acquirer to recognize any assets and noncontrolling interest acquired and liabilities assumed to be measured at fair value as of the acquisition date. Liabilities related to contingent consideration are recognized and measured at fair value on the date of acquisition rather than at a later date when the amount of the consideration may be resolved beyond a reasonable doubt. This revised approach replaces SFAS 141 s cost allocation process in which the cost of an acquisition was allocated to the individual assets acquired and liabilities assumed based on their respective fair value. SFAS 141R requires any acquisition-related costs and restructuring costs to be expensed as incurred as opposed to allocating such costs to the assets acquired and liabilities assumed as previously required by SFAS 141. Under SFAS 141R, an acquirer recognizes liabilities for a restructuring plan in purchase accounting only if the requirements of SFAS 146, Accounting for Costs Associated with Exit or Disposal Activities , are met. SFAS 141R allows for the recognition of pre-acquisition contingencies at fair value only if these contingencies are likely to materialize. If this criterion is not met at the acquisition date, then the acquirer accounts for the non-contractual contingency in accordance with recognition criteria set forth under SFAS 5, Accounting for Contingencies , in which case no amount should be recognized in purchase accounting. SFAS 141R is effective as of the beginning of an entity s first fiscal year that begins after December 15, 2008. The adoption of SFAS 141R will change the Company s accounting treatment for business combination on a prospective basis beginning on January 1, 2009.

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In December 2007, the FASB issued SFAS No. 160, Noncontrolling Interests in Consolidated Financial Statements an Amendment of ARB No. 51 (SFAS 160). This Statement amends ARB 51, Consolidated Financial Statements, to establish accounting and reporting standards for the noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. It clarifies that a noncontrolling interest in a subsidiary is an ownership interest in the consolidated entity and should be reported as equity on the financial statements. SFAS 160 requires consolidated net income to be reported at amounts that include the amounts attributable to both the parent and the noncontrolling interest. Furthermore, disclosure of the amounts of consolidated net income attributable to the parent and to the noncontrolling interest is required on the face of the financial statements. SFAS 160 is effective as of the beginning of an entity s first fiscal year that begins after December 15, 2008. The Company will incorporate the presentation requirements outlined by SFAS No. 160 on January 1, 2009.

In March 2008, the FASB issued SFAS No. 161, Disclosures about Derivative Instruments and Hedging Activities an amendment of FASB Statement No. 133 (SFAS 161). SFAS 161 enhances the required disclosures under SFAS 133, Accounting for Derivative Instruments and Hedging Activities , in order to provide the investing community additional transparency in an entity s financial statements and to more adequately disclose the impact investments in derivative instruments and use of hedging have on financial position, operating results and cash flows. SFAS 161 is effective for fiscal years and interim periods beginning after November 15, 2008, with early application allowed. SFAS 161 does not change the accounting treatment for derivative instruments and will change the Company s disclosure for derivative instruments and hedging activities on January 1, 2009.

In April, 2008, the FASB issued FSP. FAS 142-3, Determination of the Useful Life of Intangible Assets (FSP 142- 3). In determining the useful life of acquired intangible assets, FSP 142-3 removes the requirement to consider whether an intangible asset can be renewed without substantial cost of material modifications to the existing terms and conditions and, instead, requires an entity to consider its own historical experience in renewing similar arrangements. FSP 142-3 also requires expanded disclosure related to the determination of intangible asset useful lives. FSP 142-3 is effective for fiscal years beginning after December 15, 2008. The guidance for determining the useful life of a recognized intangible asset must be applied prospectively to intangible assets acquired after the effective date. Early adoption is prohibited. The adoption of FSP 142-3 will not have a material impact on the Company s consolidated financial position or result of operations.

In November 2008, the Emerging Issues Task Force issued EITF No. 08-6, Equity Method Investment Accounting Considerations (EITF 08-6) that addresses how the initial carrying value of an equity method investment should be determined, how an impairment assessment of an underlying indefinite-lived intangible asset of an equity method investment should be performed, how an equity method investee s issuance of shares should be accounted for, and how to account for a change in an investment from the equity method to the cost method. EITF 08-6 shall be effective in fiscal years beginning on or after December 15, 2008, and interim periods within those fiscal years. EITF 08-6 shall be applied prospectively with early application prohibited. The impact of adopting EITF 08-6 will not have a material impact on our consolidated financial condition or results of operations.

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(y) Loss per share

Basic loss per share is computed by dividing loss attributable to holders of ordinary shares by the weighted average number of ordinary shares outstanding (excluding shares subject to repurchase) for the year. Diluted loss per ordinary share reflects the potential dilution that could occur if securities or other contracts to issue ordinary shares were exercised or converted into ordinary shares. Ordinary share equivalents are excluded from the computation in loss periods as their effects would be anti-dilutive.

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3. CHANGE IN ACCOUNTING ESTIMATE IN 2007

Prior to January 2007, all manufacturing machinery and equipment were depreciated over estimated useful lives of 5 years. From January 1, 2007 onward, the Company re-evaluated the periods over which the equipment is available to use and extended the estimated useful lives of the manufacturing machinery and equipment based on historical usage experience and industry practices. The useful lives of the manufacturing machinery and equipment used in the wafer manufacturing processing were changed from 5 years to a 5 to 7 year range. The change in accounting estimate resulted in lower depreciation expense of $248,218,139 for the year ended December 31, 2007.

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4. FAIR VALUE

SFAS No. 157 defines fair value as the price that would be received from selling an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. When determining the fair value measurements for assets and liabilities required or permitted to be recorded at fair value, we consider the principal or most advantageous market in which we would transact and we consider assumptions that market participants would use when pricing the asset or liability, such as inherent risk, transfer restrictions, and risk of non-performance.

Fair Value Hierarchy

SFAS No. 157 establishes a fair value hierarchy that requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. Observable inputs are obtained from independent sources and can be validated by a third party, whereas unobservable inputs reflect assumptions regarding what a third party would use in pricing an asset or liability. A financial instrument s categorization within the fair value hierarchy is based upon the lowest level of input that is significant to the fair value measurement. SFAS No. 157 establishes three levels of inputs that may be used to measure fair value that gives the highest priority to observable inputs and the lowest priority to unobservable inputs as follows:

Level 1 Quoted prices in active markets for identical assets or liabilities.

Level 2 Inputs other than quoted market prices in active markets that are observable, either directly or indirectly.

Level 3 Unobservable inputs to the valuation methodology that are significant to the measurement of fair value of assets or liabilities.

The Company uses valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs. The Company performs a thorough analysis of the assets and liabilities within the scope of SFAS 157 to determine the appropriate level based on the observability of the inputs used in the valuation techniques. Assets and liabilities carried at fair value as of December 31, 2008 are classified in the categories described above based on the lowest level input that is significant to the fair value measurement in its entirety.

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Financial Instruments Measured at Fair Value on a Recurring Basis

Financial instruments measured on the Company s balance sheet at fair value on a recurring basis subsequent to initial recognition consisted of the following:

	Fair Value Measurements at Reporting Date Using			
	Quoted Prices in Active Markets for Identical Instruments (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Balance
Liabilities:				
Forward foreign exchange contracts	$	$ 3,510,305	$	$ 3,510,305
Cross-currency interest swap contracts		360,089		360,089
Derivative liabilities measured at fair value	$	$ 3,870,394	$	$ 3,870,394

The derivatives were priced by models that use readily observable market inputs, such as time value, forward interest rates, volatility factors, and current and forward market prices for foreign currency.

Financial Instruments not Recorded at Fair Value

The Company discloses the fair value of financial instruments that are not carried at fair value in accordance with SFAS 107, Disclosure of Fair Value of Financial Instruments . Financial instruments include cash and cash equivalents, restricted cash, held-to-maturity investments, equity and cost method investments, short-term borrowings, promissory note, longterm payables relating to license agreements, long-term debt, accounts payables, accounts receivables, other current assets and receivables for sale of manufacturing equipment. The fair values of cash and cash equivalents, restricted cash and short-term borrowings approximate their carrying values due to their short-term maturities. The fair value of long-term promissory notes and payables relating to license agreements was approximately $42,253,031 which was calculated based on current interest rates over the remaining payment terms. The fair value of long-term debt approximates its carrying value due to variable interest rates that approximate market rates. The fair value of cost method investment could not be practically estimated due to its non-marketability.

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5. SHORT-TERM INVESTMENTS

As of December 31, 2008 and 2007, the Company has the following held-to-maturity security, respectively:

	Debt instruments maturing in one year			
	Amortized Cost	**Gross unrealized gains**	**Gross unrealized losses**	**Fair value**
December 31, 2008	**$ 19,928,289**	**$**	**$**	**$ 19,928,289**
December 31, 2007	$ 7,637,870	$	$	$ 7,637,870

As of December 31, 2006, the Company has available-for-sale security as follows:

	December 31, 2006			
	Cost	**Gross unrealized gains**	**Gross unrealized losses**	**Fair value**
Mutual fund	$ 52,866,825	$	$	$ 52,866,825

As of December 31, 2006, the Company held certain trading securities with cost of $5,000,000 and fair value of $5,083,778.

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6. DERIVATIVE FINANCIAL INSTRUMENTS

The Company has the following notional amount of derivative instruments:

		December 31	
	2008	2007	2006
Forward foreign exchange contracts	**$ 220,687,295**	$ 404,103	$ 35,660,177
Interest rate swap contracts			250,000,000
Cross-currency interest rate swap contracts	**36,731,630**	51,057,531	15,947,874
	$ 257,418,925	$ 51,461,634	$ 301,608,051

The Company purchases foreign-currency forward exchange contracts with contract terms expiring within one year to protect against the adverse effect that exchange rate fluctuations may have on foreign-currency denominated purchase activities, principally the Renminbi, the Japanese Yen and the European Euro. The foreign-currency forward exchange contracts do not qualify for hedge accounting. Notional amounts are stated in the US dollar equivalents at spot exchange rates at the respective dates.

Settlement currency	**Notional amount**	**US dollar equivalents**
As of December 31, 2008		
European Euro	21,979,034	$ 31,144,291
Renminbi	1,294,294,400	189,543,004
		$ 220,687,295
As of December 31, 2007		
Renminbi	2,950,400	$ 404,103
As of December 31, 2006		
Japanese Yen	4,235,537,500	$ 35,660,177

In 2007 and 2006, the Company entered into various cross-currency interest rate swap agreements to protect against volatility of future cash flows caused by the changes in both interest rates and exchange rates associated with outstanding long-term debt that are denominated in a currency other than the US dollar. The cross-currency interest rate swap agreements did not qualify for hedge accounting. Notional amounts are stated in the US dollar equivalents at spot exchange rates at the respective dates.

Settlement currency	**Notional amount**	**US dollar equivalents**
As of December 31, 2008		
Euro	25,922,110	$ 36,731,630
As of December 31, 2007		
Euro	34,624,665	$ 51,057,531

As of December 31, 2006		
Euro	12,098,220	$ 15,947,874

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In 2006, the Company entered into various interest rates swap contracts to protect against volatility of future cash flows caused by the changes in interest rates associated with outstanding debt. The interest rate swap contracts did not qualify for hedge accounting. In 2006, gains or losses on the interest rate swap contracts of $(5,641,467) were recognized in interest expense, respectively. As of December 31, 2006, the Company had outstanding interest rate swap contracts with notional amounts of $250,000,000.

The fair values of each derivative instrument are as follows:

	December 31		
	2008	2007	2006
Forward foreign exchange contracts	**$ (3,510,305)**	$ 530,354	$ (2,694,415)
Interest rate swap contracts			(5,641,467)
Cross-currency interest rate swap contracts	**(360,089)**	1,003,275	323,630
	$ (3,870,394)	$ 1,533,629	$ (8,012,252)

As of December 31, 2008, 2007 and 2006, the fair value of the derivative instruments was recorded in accrued expenses and other current liabilities, prepaid expense and other current assets, and accrued expenses and other current liabilities, respectively, with the change in fair value of forward foreign exchange contracts recorded in other income (expense) and the change in fair value of interest rate swap contract and cross currency interest rate swap contracts recorded in interest expense.

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7. ACCOUNTS RECEIVABLE, NET OF ALLOWANCES

The Company determines credit terms for each customer on a case-by-case basis, based on its assessment of such customer s financial standing and business potential with the Company.

An aging analysis of accounts receivable, net of allowance for doubtful accounts, is as follows:

	2008	2007	2006
Current	**$ 108,109,977**	$ 249,489,644	$ 213,539,198
Overdue:			
Within 30 days	**18,211,498**	39,131,577	31,611,729
Between 31 to 60 days	**6,073,500**	6,107,866	5,879,705
Over 60 days	**66,976,719**	3,658,565	1,154,343
	$ 199,371,694	$ 298,387,652	$ 252,184,975
Allowance for doubtful accounts	**$ (5,680,658)**	$ (4,492,090)	$ (4,048,845)

The change in the allowance for doubtful accounts is as follows:

	2008	2007	2006
Balance, beginning of year	**$ 4,492,090**	$ 4,048,845	$ 1,091,340
Provision recorded during the year	**1,301,556**	486,920	2,957,505
Write-offs in the year	**(112,988)**	(43,675)	
Balance, end of year	**$ 5,680,658**	$ 4,492,090	$ 4,048,845

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8. INVENTORIES

	2008	2007	2006
Raw materials	**$ 76,299,347**	$ 83,645,656	$ 89,431,781
Work in progress	**53,674,794**	139,959,481	150,506,509
Finished goods	**41,662,727**	24,704,628	35,240,662
	$ 171,636,868	$ 248,309,765	$ 275,178,952

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9. ASSETS HELD FOR SALE

Assets held for sale represent residential real estate that the Company has constructed for its employees.

In 2008, the Company sold residential real estate units with a carrying value of $1,594,508 for $2,283,375, which resulted in a gain on sale of $688,867. The Company reclassified the remaining unsold real estate units of $1,529,057 to land use rights and plant and equipment.

In 2007, the Company sold residential real estate units with a carrying value of $8,402,962 for $12,599,790, which resulted in a gain on sale of $4,196,828. Meanwhile, the Company reclassified the remaining unsold real estate units of $1,017,767 of 2007 to land use rights and plant and equipment. In addition, the Company decided to offer employees another 42 residential real estate units, and classified the $3,123,567 carrying value as assets held for sale, among which, none have been sold out up to December 31, 2007.

In 2006, the Company offered to sell employees 381 residential real estate units, and classified the $17,097,675 carrying value as assets held for sale. The Company sold residential real estate units with a carrying value of $7,676,946 for $8,934,560, which resulted in a gain on sale of $1,257,614. The remaining balances of assets held for sale as of December 31, 2006 was $9,420,729, representing 213 residential real estate units.

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10. LAND USE RIGHTS, NET

	2008	2007	2006
Land use rights (50-70 years)	**$ 80,079,885**	$ 62,410,846	$ 42,485,856
Less: accumulated amortization	**(5,786,601)**	(4,858,855)	(4,162,523)
	$ 74,293,284	$ 57,551,991	$ 38,323,333

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11. PLANT AND EQUIPMENT, NET

	2008	2007	2006
Buildings	**$ 292,572,075**	$ 283,153,927	$ 269,721,109
Facility, machinery and equipment	**540,021,636**	470,434,074	435,112,058
Manufacturing machinery and equipment	**5,467,846,683**	5,035,366,468	4,539,566,491
Furniture and office equipment	**76,210,542**	67,835,774	61,979,029
Transportation equipment	**1,768,949**	1,750,734	1,666,185
	6,378,419,885	5,858,540,977	5,308,044,872
Less: accumulated depreciation and impairment	**(3,763,083,884)**	(2,930,088,762)	(2,314,667,455)
Construction in progress	**348,049,839**	274,505,450	251,023,405
	$ 2,963,385,840	$ 3,202,957,665	$ 3,244,400,822

The Company recorded depreciation expense of $760,881,076, $705,391,171 and $919,038,915 for the years ended December 31, 2008, 2007 and 2006, respectively. In 2008, the Company sold equipment with a carrying value of $5,948,053 for $8,136,361, which resulted in a gain on sale of $2,188,308. In 2007, the Company sold equipment with a carrying value of $26,920,427 for $51,375,045, which resulted in a gain on sale of $24,454,618. In 2006, the Company sold equipment with a carrying value of $26,554,170 for $68,418,485, which resulted in a gain on sale of $41,864,315.

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12. IMPAIRMENT OF PLANT AND EQUIPMENT

In 2008, the Company reached an agreement with certain customers to discontinue production of DRAM products and subsequently the Company decided to exit the commodity DRAM business as a whole. The Company considered these actions to be an indicator of impairment in regard to certain plant and equipment of the Company s Beijing facilities. The Company recorded an impairment loss of $105,774,000, equal to the excess of the carrying value over the fair value of the associated assets. The Company computed the fair value of the plant and equipment utilizing a discounted cash flow approach. For the purpose of the analysis, the Company applied a discount rate of 9% to the expected cash flows to be generated over the remaining useful lives of primary manufacturing machinery and equipment of approximately 5 years.

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13. ACQUIRED INTANGIBLE ASSETS, NET

	2008	2007	2006
Technology, Licenses and Patents			
Cost:	**$ 323,457,444**	$ 322,435,363	$ 134,862,112
Accumulated Amortization and Impairment	**(123,398,338)**	(90,240,231)	(63,169,614)
Acquired intangible assets, net	**$ 200,059,106**	$ 232,195,132	$ 71,692,498

The Company entered into several technology, patent and license agreements with third parties whereby the Company purchased intangible assets for $1,022,081, $187,573,251 and $15,418,322 in 2008, 2007 and 2006, respectively.
In 2008, the Company recorded an impairment loss of $966,667 for licenses related to DRAM products that are no longer in use.
The Company recorded amortization expense of $32,191,440, $27,070,617 and $24,393,561 in 2008, 2007 and 2006 respectively. The Company will record amortization expenses related to the acquired intangible assets of $37,634,121, $28,557,689, $24,479,980, $18,858,581 and $17,130,688 for 2009, 2010, 2011, 2012 and 2013, respectively.

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14. EQUITY INVESTMENT

	December 31, 2008	
	Carrying Amount	% of Ownership
Equity Method Investment		
Toppan SMIC Electronics (Shanghai) Co., Ltd.	$ 9,162,766	30.0
Cost method investments	$ 2,189,420	Less than 20.0
Acquired intangible assets, net	$ 11,352,186	

On July 6, 2004, the Company and Toppan Printing Co., Ltd (Toppan) entered into an agreement to form Toppan SMIC Electronics (Shanghai) Co., Ltd. (Toppan SMIC) in Shanghai, to manufacture on-chip color filters and micro lenses for CMOS image sensors.
In 2005, the Company injected cash of $19,200,000 into Toppan SM IC, representing 30% equity ownership. In 2008, 2007 and 2006, the Company recorded $444,211, $4,012,665 and $4,201,247, respectively, as its share of the net loss of the equity investment.

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15. ACCOUNTS PAYABLE

An aging analysis of the accounts payable is as follows:

	2008	2007	2006
Current	**$ 126,149,360**	$ 223,527,856	$ 238,864,239
Overdue:			
Within 30 days	**26,524,678**	46,571,502	43,364,820
Between 31 to 60 days	**9,510,883**	10,226,533	9,594,873
Over 60 days	**23,733,618**	21,666,848	17,305,267
	$ 185,918,539	$ 301,992,739	$ 309,129,199

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16. PROMISSORY NOTE

As set out in Note 28, the Company has been performing obligations under a settlement and license agreement with TSMC. Under this agreement, the Company issued thirteen non-interest bearing promissory notes with an aggregate amount of $175,000,000 as the settlement consideration. The Company has recorded a discount of $17,030,709 for the imputed interest on the notes, which was calculated using an effective interest rate of 3.45% and was recorded as a reduction of the face amounts of the promissory notes. The Company repaid $30,000,000, $30,000,000 and $30,000,000 in 2008, 2007 and 2006, respectively. The outstanding promissory notes are as follows:

	December 31, 2008	
Maturity	**Face value**	**Discounted value**
2009	**$ 30,000,000**	**$ 29,242,001**
2010	**25,000,000**	**23,589,958**
Less: Current portion of promissory notes	**30,000,000**	**29,242,001**
Long-term portion of promissory notes	**$ 25,000,000**	**$ 23,589,958**

In 2008, 2007 and 2006, the Company recorded interest expense of $2,532,795, $3,455,506 and $4,347,221, respectively, relating to the amortization of the discount.

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17. INDEBTEDNESS

Short-term and long-term debts are as follows:

	2008	2007	2006
Short-term borrowings from commercial banks (a)	**$ 201,257,773**	$ 107,000,000	$ 71,000,000
Long-term debt by contracts (b):			
Shanghai USD syndicate loan	**$ 266,050,000**	$ 393,910,000	$ 274,420,000
Beijing USD syndicate loan	**300,060,000**	500,020,000	600,000,000
EUR loan	**72,037,070**	51,057,531	15,947,873
Tianjin USD syndicate loan	**259,000,000**	12,000,000	
	$ 897,147,070	$ 956,987,531	$ 890,367,873
Long-term debt by repayment schedule:			
2009	**$ 360,628,789**		
2010	**305,568,789**		
2011	**135,482,995**		
2012	**95,466,497**		
	897,147,070		
Less: current maturities of long-term debt	**360,628,789**		
Non-current maturities of long-term debt	**$ 536,518,281**		

(a) Short-term borrowings from commercial banks

As of December 31, 2008, the Company had ten short-term credit agreements that provided total credit facilities of up to $268 million on a revolving credit basis. As of December 31, 2008, the Company had drawn down $201 million under these credit agreements and $67 million is available for future borrowings. The outstanding borrowings under the credit agreements are unsecured. The interest expense incurred in 2008 was $9,411,024, of which $1,103,335 was capitalized as additions to assets under construction. The interest rate on the loan ranged from 1.88% to 8.75% in 2008.

As of December 31, 2007, the Company had fifteen short-term credit agreements that provided total credit facilities of up to $484 million on a revolving credit basis. As of December 31, 2007, the Company had drawn down $107 million under these credit agreements and $377 million was available for future borrowings. The outstanding borrowings under the credit agreements were unsecured. The interest expense incurred in 2007 was $4,537,200, of which $1,909,602 was capitalized as additions to assets under construction. The interest rate on the loan ranged from 5.37% to 6.44% in 2007.

As of December 31, 2006, the Company had fifteen short-term credit agreements that provided total credit facilities of up to $474 million on a revolving credit basis. As of December 31, 2006, the Company had drawn down $71 million under these credit agreements and $403 million was available for future borrowings. The outstanding borrowings under the credit agreements were unsecured. The interest expense incurred in 2006 was $8,471,823, of which $1,019,903 was capitalized as additions to assets under construction. The interest rate on the loans ranged from 3.62% to 6.52% in 2006.

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(b) Long-term debt

Shanghai USD syndicate loan

In June, 2006, SMIS entered into the Shanghai USD syndicate loan with the aggregate principal amount of $600,000,000, with a consortium of international and PRC banks. Of this principal amount, $393,000,000 was used to repay the principal amount outstanding under SMIS s previous USD syndicate loans. The remaining principal amount was available to be used to finance future expansion and general corporate requirements of SMIS. As of December 31, 2007 and 2006, SMIS had drawn down $600,000,000 and $393,000,000 from this facility. The principal amount is repayable starting from December 2006 in ten semi-annual installments. In 2008, 2007 and 2006, SMIS had repaid $127,860,000, $87,510,000 and $118,580,000, respectively, according to the repayment schedule. As of December 31, 2008 and 2007 and 2006, the outstanding balance of this borrowing was $266,050,000, $393,910,000 and $274,420,000, respectively. In 2008, the interest rate on the loan ranged from 2.47% to 5.76%. The interest expense incurred in 2008, 2007 and 2006 was $16,979,883, $17,260,814 and $13,522,886, respectively, of which $5,358,081, $3,308,444 and $1,624,224 was capitalized as additions to assets under construction in 2008, 2007 and 2006, respectively.

The total outstanding balance of the Shanghai USD syndicate loan is collateralized by certain plant and equipment with an original cost of $1,871 million as of December 31, 2008.

The Shanghai USD syndicate loan contains covenants relating to the minimum consolidated tangible net worth, limits total borrowings compared to tangible net worth and EBITDA for the prior four quarters, and requires minimum debt service coverage ratios. SMIS has complied with these covenants (unless otherwise waived by the lenders to such agreement) as of December 31, 2008.

Beijing USD syndicate loan

In May 2005, SMIB entered into the Beijing USD syndicate loan, a five-year loan facility in the aggregate principal amount of $600,000,000, with a syndicate of financial institutions based in the PRC. This five-year bank loan was used to expand the capacity of SMIB s fabs. The withdrawal period of the facility was twelve months from date of signing the agreement. As of December 31, 2008, 2007 and 2006, the outstanding balance was $300,060,000, $500,020,000 and $600,000,000, respectively, on this loan facility. The principal amount is repayable starting from December 2007 in six equal semi-annual installments. In 2008 and 2007, SMIB had repaid $199,960,000 and $99,980,000, respectively, according to the repayment schedule. In 2008, the interest rate on the loan ranged from 3.46% to 6.38%. The interest expense incurred in 2008, 2007 and 2006 was $25,599,360, $42,183,106 and $28,525,628, of which $1,599,175, $2,342,794 and $450,516 was capitalized as additions to assets under construction in 2008, 2007 and 2006, respectively.

The total outstanding balance of the Beijing USD syndicate loan is collateralized by certain plant and equipment with an original cost of $1,047 million as of December 31, 2008.

The Beijing USD syndicate loan contains covenants to maintain minimum cash flows as a percentage of non-cash expenses and to limit total liabilities, excluding shareholder loans, as a percentage of total assets. SMIB has complied with these covenants (unless otherwise waived by the lenders to such agreement) as of December 31, 2008.

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EUR loan

On December 15, 2005, the Company entered into the EUR loan, a long-term loan facility agreement in the aggregate principal amount of EUR 85 million with ABN Amro Bank N.V. Commerz Bank N.V., Shanghai Branch. The proceeds from the facility were used to purchase lithography equipment to support the expansion of the Company s manufacturing facilities. The drawdown period of the facility ends on the earlier of (i) the date on which the loans have been fully drawn down; or (ii) 36 months after the date of the agreement. Each drawdown made under the facility shall be repaid in full by the Company in ten equal semi-annual installments starting from May 6, 2006.

In 2008, 2007 and 2006, SMIS and SMIT had drawn down EUR 28,475,000 ($38,929,954), EUR 28,390,000 ($41,863,894) and EUR 15,122,775 ($19,934,841), respectively. SMIS and SMIT repaid an aggregated amount of EUR12,261,930 ($17,950,415), EUR 5,863,555 ($8,173,357) and EUR 3,024,555 ($3,986,968) in 2008, 2007 and 2006, respectively. As of December 31, 2008, 2007 and 2006, the outstanding balance is EUR 50,837,735 ($72,037,070), EUR 34,624,665 ($51,057,531) and EUR 12,098,220 ($15,947,873). In 2008, the interest rate on the loan ranged from 3.01% to 6.12%. The interest expense incurred in 2008, 2007 and 2006 was $2,682,195, $996,706 and $279,908, respectively, of which $810,495, $82,036 and $65,072 was capitalized as additions to assets under construction in 2008, 2007 and 2006, respectively.

The total outstanding balance of the facility is collateralized by certain plant and equipment with an original cost of $21.8 million for SMIT and $114.5 million for SMIS as of December 31, 2008.

Tianjin USD syndicate loan

On May 31, 2006, SMIT entered into the Tianjin USD syndicate loan, a five-year loan facility in the aggregate principal amount of $300,000,000, with a syndicate of financial institutions based in the PRC. This five-year bank loan was used to expand the capacity of SMIT s fab. In 2008 and 2007, SMIT drew down $247,000,000 and $12,000,000 of the facility amount, respectively. The principal amount is repayable starting from 2010 in six semi-annual installments. In 2008, the interest rate on the loan ranged from 3.11% to 6.03%. The interest expense incurred in 2008 and 2007 was $9,147,490 and $285,253, respectively, of which $1,788,712 and $24,344 was capitalized as additions to assets under construction in 2008 and 2007, respectively.

The total outstanding balance of the Tianjin USD syndicate loan is collateralized by certain plant and equipment with an original cost of $627.4 million as of December 31, 2008.

The Tianjin USD syndicate loan contains covenants to maintain minimum cash flows as a percentage of non-cash expenses and to limit total liabilities as a percentage of total assets. SMIT has complied with these covenants (unless otherwise waived by the lenders to such agreement) as of December 31, 2008.

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18. LONG-TERM PAYABLES RELATING TO LICENSE AGREEMENTS

The Company entered into several license agreements for acquired intangible assets to be settled by installment payments. Installments payable under the agreements as of December 31, 2008 are as follows:

	December 31, 2008	
Maturity	**Face value**	**Discounted value**
2009	**$ 50,133,334**	**$ 49,203,521**
2010	**14,766,666**	**13,614,440**
2011	**5,200,000**	**4,554,566**
	70,100,000	**67,372,527**
Less: Current portion of long-term payables	**50,133,334**	**49,203,521**
Long-term portion of long-term payables	**$ 19,966,666**	**$ 18,169,006**

These long-term payables were interest free, and the present value was discounted using the Company s weighted-average borrowing rates ranging from 3.45% to 4.94%.

The current portion of other long-term payables is recorded in accrued expenses and other current liabilities.

In 2008, 2007 and 2006, the Company recorded interest expense of $4,382,772, $1,511,880 and $1,355,386 relating to the amortization of the discount.

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19. INCOME TAXES

The Company is a taxexempted company incorporated in the Cayman Islands.

In 2008, the Company recorded withholding income tax expense of $15,400,000 for license income generated from its PRC subsidiaries.

Subsidiaries in PRC

Prior to January 1, 2008, the subsidiaries incorporated in the PRC were governed by the Income Tax Law of the PRC Concerning Foreign Investment and Foreign Enterprises and various relevant income tax laws, regulations and policies (the FEIT Laws).

On March 16, 2007, the National People s Congress of China enacted a new Enterprise Income Tax Law (New EIT Law) which became effective January 1, 2008. Under the New EIT Law, domestically-owned enterprises and foreign invested enterprises (FIEs) are subject to a uniform tax rate of 25%. The New EIT Law also provides a transition period starting from its effective date for those enterprises which were established before the promulgation date of the New EIT Law and which are entitled to a preferential lower tax rate and/or tax holiday under the FEIT Law or other related regulations. Based on the New EIT Law, the tax rate of such enterprises will transition to the uniform tax rate throughout a five-year period. Tax holidays that were enjoyed under the FEIT Laws may continue to be enjoyed until the end of the holiday. Tax holidays that have not started because the enterprise is not profitable will take effect regardless whether the FIEs are profitable in 2008.

According to Guofa (2007) No. 39 the Notice of the State Council Concerning Implementation of Transitional Rules for Enterprise Income Tax Incentives (Circular 39) issued on December 26, 2007, enterprises that enjoyed preferential tax rates shall gradually transit to the statutory tax rate over 5 years after the new EIT Law is effective. Enterprises that enjoyed a tax rate of 15% under the FEIT Law shall be levied of rates of 18% in 2008, 20% in 2009, 22% in 2010, 24% in 2011 and 25% in 2012.

On February 22, 2008, the PRC government promulgated Caishui (2008) No.1, the Notice of the Ministry of Finance and State Administration of Tax concerning Certain Enterprise Income Tax Preferential Policies (Caishui No.1). Pursuant to Caishui No.1, integrated circuit production enterprises whose total investment exceeds RMB8,000 million (approximately $1,095 million) or whose integrated circuits have a line width of less than 0.25 micron are entitled to preferential tax rate of 15%. If the operation period is more than 15 years, those enterprises are entitled to a full exemption from income tax for five years starting from the first profitable year after utilizing all prior years tax losses and 50% reduction for the following five years. SMIS, SMIB and SMIT have met such accreditation requirements.

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The detailed tax status of SMIC s PRC entities is elaborated as follows:

1) SMIS

Pursuant to the preferential tax policy available under the FEIT law as well as other related tax regulation, SMIS was subject to a preferential income tax rate of 15% . According to Circular Guofa (2000) No. 18 New Policy Implemented for Software and Semiconductor Industries (Circular 18) issued by the State Council of China, SMIS is entitled to a 10-year tax holiday (5-year full exemption followed by 5-year half reduction) for FEIT rate starting from the first profit- making year after utilizing all prior years tax losses. The tax holiday enjoyed by SMIS took effect in 2004 when the SMIS completed its first profit-making year.

In accordance with the New EIT Law and Caishui No.1, SMIS is eligible to continue enjoying 15% income tax rate and its tax holiday through its expiry in 2013.

2) SMIB and SMIT

In accordance with the Circular 18 and Caishui No.1, SMIB and SMIT are currently entitled to the preferential tax rate of 15% and will be entitled to a 10-year tax holiday (5-year full exemption followed by 5-year half reduction) subsequent to their first profit-making years after utilizing all prior tax losses. Both entities were in loss positions as of December 31, 2008 and as a result the tax holiday has not yet taken effect.

3) SMICD

Under the FEIT Laws, SMICD was qualified for a 5-year tax holiday (2-year full exemption followed by 3-year half reduction) subsequent to its first profit-making year after utilizing all prior tax losses. As of December 31, 2008, SMICD was still in a loss position. Pursuant to the New EIT Law, the tax holiday began in 2008 at the statutory tax rate of 25% despite the fact that SMICD had yet to be profitable. The applicable income tax rates for the years ended December 31, 2008, 2009, 2010, 2011, 2012 and thereafter are 0%, 0%, 12.5% 12.5%, 12.5% and 25%, respectively.

4) Energy Science

Energy Science is a manufacturing enterprise located in the Shanghai Pudong New Area. Pursuant to the preferential tax policy granted to the Pudong New Area under the FEIT Law, Energy Science was subject to a preferential tax rate of 15% and qualified for a 5-year tax holiday (2-year full exemption followed by 3-year half reduction in FEIT rate) subsequent to its first profit-making year after utilizing all prior years tax losses or 2008 in accordance with the New EIT Law. The tax holiday commenced in 2007 and would continue until 2011. The statutory tax rate is gradually transiting to 25% within a 5-year transition period starting from 2008. The applicable income tax rates for the year ended December 31, 2008, 2009, 2010, 2011 and thereafter are 0%, 10%, 11%, 12% and 25%, respectively.

Subsidiaries in other jurisdictions

The Company s other subsidiaries are subject to the respective local country s income tax laws, including those of Japan, the United States of America, Taiwan, Europe and Hong Kong. In 2008, 2007 and 2006, the Company s US subsidiary had recorded current income tax expense of $223,812, $163,604 and $31,030, respectively. In 2008, 2007 and 2006, the Company s European subsidiary had recorded current income tax expense of $128,010, $181,451 and $112,671, respectively. In 2008, 2007 and 2006, the Company recorded income tax expense of $405,000, $1,149,983

and $nil and income tax refund of $774,744, $nil, $nil for the service income generated in Japan. In 2008, 2007 and 2006, the Company had minimal taxable income in Hong Kong.

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The Company estimates its income taxes in each of the jurisdictions in which it operates. The Company accounts for income taxes by the liability method. Under this method, deferred income taxes are recognized for tax consequences in future years of differences between the tax basis of assets and liabilities and their financial reporting amounts at each yearend, based on enacted laws and statutory tax rates applicable for temporary differences that are expected to affect taxable income. Valuation allowances are provided if based on available evidence, it is more likely than not that some or all of the deferred tax assets will not be realized.

The provision for income taxes by tax jurisdiction is as follows:

		December 31	
	2008	2007	2006
PRC			
Current	**$ 15,106**	$ 19,602	$ 4,542
Adjustments on deferred tax assets and liabilities for enacted changes in tax rate	**20,542,716**	(20,542,716)	
Deferred	**(9,506,907)**	(10,691,699)	(25,075,987)
Other jurisdictions			
Current	**15,382,078**	1,495,038	143,701
Deferred			
	$ 26,432,993	$ (29,719,775)	$ (24,927,744)

The income (loss) before income taxes by tax jurisdiction is as follows:

		December 31	
	2008	2007	2006
PRC	**$ (291,664,135)**	$ 51,906,337	$ 46,806,662
Other jurisdictions	**(113,838,901)**	(99,937,852)	(116,777,420)
	$ (405,503,036)	$ (48,031,515)	$ (69,970,758)

Details of deferred tax assets and liabilities are as follows:

	2008	2007	2006
Deferred tax assets:			
Allowances and reserves	**$ 4,732,017**	$	$ 1,962,410
Start-up costs	**929,991**	53,698	958,105
Net operating loss carry forwards	**55,476,943**		5,201,545
Unrealized exchange loss	**33,228**		47,860
Depreciation of fixed assets	**59,224,163**	75,886,896	33,715,867
Subsidy on long lived assets	**479,817**	479,817	295,654
Accrued sales return	**603,274**		137,719
Total deferred tax assets	**121,479,433**	76,420,411	42,319,160
Valuation allowance	**(75,792,963)**	(19,505,239)	(17,032,260)

Net deferred tax assets	non-current	**$ 45,686,470**	$ 56,915,172	$ 25,286,900
Deferred tax liability:				
Capitalized interest		**$ (411,877)**	$ (604,770)	$ (210,913)

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As a result of strategic tax planning that became effective in 2006, a temporary difference between the tax and book basis of certain assets was created. Under SFAS 109 Accounting for Income Taxes , the Company recognized a valuation allowance of $20.3 million, $19.5 million and $8.4 million to reduce the deferred tax asset of $59.2 million, $75.9 million and $33.7 million to an amount that is more-likely-than-not to be realized as of December 31, 2008, 2007 and 2006, respectively. Accordingly, income tax expense of $17.5 million and income tax benefits of $31.1 million and $25.3 million were recorded in 2008, 2007 and 2006, respectively. The deferred tax asset recognized relates specially to one of the Company s subsidiaries on the basis that this subsidiary has achieved profitability in prior years and is expected to continue to be profitable based on the current forecast.

As of December 31, 2008, the Company s Beijing, Tianjin and Chengdu subsidiaries had net operating loss carry forward of $917.1 million, of which $117.8 million, $174.9 million, $271.8 million and $352.6 million will expire in 2011, 2012, 2013 and 2014, respectively.

Under the New EIT Law, profits earned subsequent to January 1, 2008 from a foreign invested enterprise that are distributed to a non-resident enterprise outside of China, will be subject to a withholding tax rate of 10%. A lower withholding tax rate may be applied if there is a favorable tax treaty between mainland China and the jurisdiction of the non-resident enterprise. For example, holding companies in Hong Kong that are also tax residents in Hong Kong are eligible for a 5% withholding tax (for the Hong Kong holding company which directly holds at least 25% of the capital of the foreign invested enterprise) on dividends under the Tax Memorandum between China and the Hong Kong Special Administrative Region. However, under Guoshuihan (2009) No. 81, a transaction or arrangement entered into for the primary purpose of being qualified for a preferential tax rate on dividends under a tax agreement would not be a valid reason for qualifying for such preferential treatment. Where a taxpayer inappropriately enjoyed the tax agreement treatment due to such a transaction or arrangement, the competent tax authorities are empowered to make appropriate adjustments that they deem appropriate.

Since the Company intends to reinvest its earnings to expand its businesses in mainland China, its PRC subsidiaries do not intend to distribute profits to their immediate foreign holding companies in the foreseeable future. Accordingly, as of December 31, 2008, the Company has not recorded any withholding tax on the retained earnings of its PRC subsidiaries.

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Uncertainties exist with respect to how China s current income tax law applies to our overall operations, and more specifically, with regard to tax residency status. New EIT Law includes a provision specifying that legal entities organized outside of China will be considered residents for Chinese income tax purposes if their place of effective management or control is within China. The Implementation Rules to the EIT Law provide that non-resident legal entities will be considered China residents if substantial and overall management and control over the manufacturing and business operations, personnel, accounting, properties, etc. occurs within China. Additional guidance is expected to be released by the Chinese government in the near future that may clarify how to apply the rules to taxpayers. Despite the present uncertainties resulting from the limited PRC tax guidance on the issue, we do not believe that our legal entities organized outside of China should be treated as residents for EIT Law purposes. If one or more of our legal entities organized outside of China were characterized as China tax residents for the year ended December 31, 2008, the impact would adversely affect our results of operation.

Income tax expense computed by applying the applicable EIT tax rate of 15% is reconciled to income before income taxes and minority interest as follows:

	2008	2007	2006
Applicable enterprise income tax rate	**15.0%**	15.0%	15.0%
Expenses (credit) not deductible for tax purpose	**(1.8%)**	(0.9%)	3.1%
Effect of tax holiday and tax concession	**0.0%**	48.7%	25.0%
Expense (credit) to be recognized in future periods	**8.2%**	(19.2%)	29.3%
Changes in valuation allowances	**(15.6%)**	9.3%	(11.9%)
Effect of different tax rate of subsidiaries operating in other jurisdictions	**(7.2%)**	(33.8%)	(24.9%)
Changes of tax rate	**(5.1%)**	42.8%	
Effective tax rate	**(6.5%)**	61.9%	35.6%

The aggregate amount and per share effect of the tax holiday are as follows:

	2008	2007	2006
The aggregate dollar effect	**$ 10,572**	$ 23,415,370	$ 17,472,283
Per share effect- basic and diluted	**$ 0.00**	$ 0.00	$ 0.00

The Company adopted FIN 48 on January 1, 2007. The Company made its assessment of the level of tax authority for each tax position (including the potential application of interest and penalties) based on its technical merits. FIN 48 did not have any impact on the Company total liabilities or stockholders equity as of January 1, 2007. The Company has no material uncertain tax positions as of December 31, 2008 or unrecognized tax benefit which would favorably affect the effective income tax rate in future periods. The Company classifies interest and/or penalties related to income tax matters in income tax expense. As of December 31, 2008, the amount of interest and penalties related to uncertain tax positions is immaterial. The Company does not anticipate any significant increases or decreases to its liability for unrecognized tax benefits within the next 12 months.

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20. MINORITY INTEREST

In 2004, the Company incorporated AT and SMICD, a wholly-owned subsidiary of AT.

In 2005, AT issued Series A redeemable convertible preference shares (Series A shares) to certain third parties for cash consideration of $39 million, representing 43.3% equity interest of AT. In 2007, AT repurchased 1 million preference shares with $1 million from a minority stockholder, and equity interest of the minority stockholders in AT decreased to 42.7% as of December 31, 2007. No share transaction occurred in 2008.

At any time after January 1, 2009, if AT has not filed its initial registration statement relating its initial public offering as of such date, the holders of Series A shares (other than SM IC) shall have the right to require AT to redeem such holders shares upon redemption request by paying cash in an amount per share equal to the initial purchase price at $1.00 for such Series A shares plus the product of (i) purchase price relating to the Series A shares and (ii) 3.5% per annum calculated on a daily basis from May 23, 2005. As of December 31, 2008, 38 million preferred shares are outstanding to minority interest holders and will be redeemable beginning January 1, 2009. The Series A shares are not considered participating securities and have been recorded at their redemption amount as a non-controlling interest in the consolidated balance sheets. Adjustments to the carrying value of the Series A shares have been recorded as a minority interest expense in the consolidated statements of operations.

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21. CAPITAL STOCK

In November 2008, the Company issued 3,699,094,300 ordinary shares to a stockholder at HK$0.36 per share and received consideration of $165,100,000, net of issuance costs of approximately $3,000,000.

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22. SHARE-BASED COMPENSATION

Stock options

The Company s employee stock option plans (the Plans) allow the Company to offer a variety of incentive awards to employees, consultants or external service advisors of the Company. In 2004, the Company adopted the 2004 Stock Option Plan (2004 Option Plan) whereby the Company grants stock options to attract, retain and motivate employees, directors and service providers. Following the Company s IPO in March 2004, the Company issued stock options solely through the 2004 Option Plan. Options to purchase 1,317,000,000 ordinary shares are authorized under the 2004 Option Plan. Under the terms of the 2004, Option Plan options are granted at the fair market value of the Company s ordinary shares, and expire 10 years from the date of grant and vest over a requisite service period of four years. Any compensation expense is recognized on a straight-line basis over the employee service period. As of December 31, 2008, options to purchase 786,071,676 ordinary shares were outstanding, and options to purchase 530,428,324 ordinary shares were available for future grants.

In 2001, the Company adopted the 2001 Stock Option Plan (2001 Option Plan). Options to purchase 998,675,840 ordinary shares and 536,566,500 of Series A convertible preference shares are authorized under the 2001 Option Plan. Options to purchase Series A convertible preference shares were converted into options to purchase ordinary shares immediately prior to the completion of the IPO. Under the terms of the 2001 Option Plan, options are generally granted at prices equal to the fair market value, expire 10 years from the date of grant and vest over a requisite service period of four years. Following the IPO, the Company no longer issues stock options under the 2001 Option Plan. As of December 31, 2008, options to purchase 338,084,318 ordinary shares were outstanding.

A summary of the stock option activity is as follows:

	Ordinary shares		Weighted Average	
	Number of options	Weighted average exercise price	Remaining Contractual Term	Aggregated Intrinsic Value
Options outstanding at January 1, 2008	1,042,398,482	$ 0.14		
Granted	248,840,090	$ 0.05		
Exercised	(22,730,522)	$ 0.03		
Forfeited or cancelled	(144,352,056)	$ 0.13		
Options outstanding at December 31, 2008	1,124,155,994	$ 0.12	6.79 years	$ 34,499,475
Vested or expected to vest at December 31, 2008	1,080,819,321	$ 0.12	6.87 years	$ 30,288,832
Exercisable at December 31, 2008	491,098,679	$ 0.13	4.89 years	$ 28,604,914

The total intrinsic value of options exercised in the year ended December 31, 2008, 2007 and 2006 was $1,434,758, $5,679,680 and $5,240,221, respectively.

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Certain options were granted to non-employees that resulted in a share-based compensation expense of $374,967, $665,787 and $584,283 in 2008, 2007 and 2006, respectively.

The weighted-average grant-date fair value of options granted during the year 2008, 2007 and 2006 was $0.05, $0.04 and $0.05, respectively.

The fair value of each option and share grant is estimated on the date of grant using the Black-Scholes option pricing model with the assumptions noted below. The Company uses historical data to estimate option exercise and employee termination within the pricing formula. The risk-free rate for periods within the contractual life of the option is based on the yield of the US Treasury Bond. The expected term of options granted represents the period of time that options granted are expected to be outstanding. Expected volatilities are based on the average volatility of the Company with the time period commensurate with the expected time of the options. The dividend yield is based on the Company s intended future dividend plan.

	2008	2007	2006
Average risk-free rate of return	**2.13%**	3.98%	4.72%
Expected term	**1-4 years**	1-4 years	2-4 years
Volatility rate	**46.82%**	35.28%	32.69%
Expected dividend yield			

Restricted share units (RSU)

In January 2004, the Company adopted the 2004 Equity Incentive Plan (2004 EIP) whereby the Company provided additional incentives to the Company s employees, directors and external consultants through the issuance of restricted shares, restricted share units (RSU) and stock appreciation rights to the participants at the discretion of the Board of Directors. Under the 2004 EIP, the Company was authorized to issue up to 2.5% of the issued and outstanding ordinary shares immediately following the closing of its IPO, which were 455,409,330 ordinary shares. As of December 31, 2008, 95,620,762 RSU were outstanding and 200,948,509 ordinary shares were available for future grant. The RSU vest over a requisite service period of 4 years and expire 10 years from the date of grant. No stock appreciation rights have been issued. Any compensation expense is recognized on a straight-line basis over the vesting period.

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A summary of RSU activity is as follows:

	Restricted share units		Weighted Average	
	Number of Share Units	Weighted Average Fair Value	Remaining Contractual Term	Aggregated Fair Value
Outstanding at January 1, 2008	119,442,808	$ 0.14		
Granted	41,907,100	$ 0.08		
Exercised	(49,953,525)	$ 0.13		
Forfeited or cancelled	(15,775,621)	$ 0.13		
Outstanding at December 31, 2008	95,620,762	$ 0.12	8.19 years	$ 11,970,507
Vested or expected to vest at December 31, 2008	29,485,303	$ 0.12	8.29 years	$ 4,047,455

Pursuant to the 2004 EIP, the Company granted 41,907,100, 40,519,720 and 16,058,864 RSU in 2008, 2007, and 2006, respectively. The fair value of the RSU at the date of grant was $3,313,114, $5,631,263 and $2,055,597 in 2008, 2007, and 2006, respectively. The Company recorded compensation expense of $5,644,789, $7,216,799 and $5,452,148 in 2008, 2007, and 2006, respectively.

Unrecognized compensation cost related to non-vested share-based compensation

As of December 31, 2008, there was $13,996,655 of total unrecognized compensation cost related to non-vested share- based compensation arrangements granted under the 2001 Stock Option Plan, 2004 Stock Option Plan and 2004 EIP. The cost is expected to be recognized over a weighted-average period of 1.15 years.

As of December 31, 2008, 2007, and 2006 the Company had the following shares subject to repurchase:

	2008	2007	2006
Ordinary Shares		90,000	16,498,871

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23. RECONCILIATION OF BASIC AND DILUTED LOSS PER SHARE

The following table sets forth the computation of basic and diluted loss per share for the years indicated:

	2008	2007	2006
Net Loss	**$ (440,231,120)**	$ (19,468,147)	$ (44, 109,078)
Less: Cumulative effect of a change in accounting principle			(5,153,986)
Net loss before cumulative effect of a change in accounting principle	**(440,231,120)**	(19,468,147)	(49,263,064)
Basic and diluted:			
Weighted average ordinary shares outstanding	**18,682,585,932**	18,505,650,171	18,361,910,033
Less: Weighted average ordinary shares outstanding subject to repurchase	**(41,066)**	(3,709,682)	(27,411,110)
Weighted average shares used in computing basic and diluted income per share	**18,682,544,866**	18,501,940,489	18,334,498,923
On the basis of loss per share before cumulative effect of a change in accounting principle, basic and diluted	**$ (0.02)**	$ (0.00)	$ (0.00)
Cumulative effect of a change in accounting principle per share, basic and diluted	**$**	$	$ 0.00
Basic and diluted loss per share	**$ (0.02)**	$ (0.00)	$ (0.00)

Ordinary share equivalents of share options and restricted share units are calculated using the treasury stock method. Under the treasury stock method, the proceeds from the assumed conversion of share options and restricted share units are used to repurchase outstanding ordinary shares using the average fair value for the periods.

As of December 31, 2008, 2007 and 2006, the Company had 189,478,507, 147,988,221 and 223,818,877, respectively, ordinary share equivalents outstanding which were excluded in the computation of diluted loss per share, as their effect would have been anti-dilutive due to the net loss reported in such periods. They include:

		December 31	
	2008	2007	2006
Outstanding options to purchase ordinary shares	**128,361,312**	72,685,282	62,339,207
Outstanding unvested restricted share units to purchase ordinary shares	**61,117,195**	75,302,939	161,479,670
	189,478,507	147,988,221	223,818,877

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24. TRANSACTIONS WITH MANAGED GOVERNMENT-OWNED FOUNDRIES

The Company provides management services to Cension Semiconductor Manufacturing Corporation (Cension) and Wuhan Xinxin Semiconductor Manufacturing Corporation (Xinxin), which are government-owned foundries. Management service revenues under these arrangements for 2008, 2007 and 2006 were $33,000,000, $42,000,000 and $4,151,238, respectively.

In 2008, 2007 and 2006, the Company sold equipment with carrying value of $7,688, $19,530,909 and $19,411,553 to Cension for $175,300, $42,300,258 and $61,182,653, which resulted in gains on sale of $167,612, $22,769,349 and $41,771,099, respectively.

In 2008, the Company sold equipment with carrying value of $3,629,605 to Xinxin for $3,944,204, which resulted in a gain on sale of $314,599.

On April 10, 2007, Cension entered into an Asset Purchase Agreement (the Agreement) with Elpida Memory, Inc. (Elpida), a Japan based memory chip manufacturer, for the purchase of Elpida s 200mm wafer processing equipment currently located in Hiroshima, Japan for the total price of approximately $320 million.

As part of the Agreement, the Company provided a corporate guarantee for a maximum guarantee liability of $163.2 million on behalf of Cension in favour of Elpida. The Company s guarantee liability will terminate upon full payment of the purchase price by Cension to Elpida. In return for providing the above corporate guarantee, the Company received a guarantee fee from Cension based on 1.5% of the guarantee amount, or $2.4 million. Approximately $160 million in 200mm wafer processing equipment purchased under the Agreement was held as collateral under the guarantee.

The Company is entitled to the net profit (loss) associated with the ongoing operations of this equipment, net of a guaranteed fixed share of revenue for Elpida, during the transitional period prior to when the equipment was relocated from Hiroshima to Chengdu. Such relocation was completed in 2008.

On August 30, 2007, Cension negotiated with Elpida and subsequently reduced the purchase price to US$309.5 million.

In April 2008, SMIC entered into an agreement with Cension to purchase approximately half of the Equipment from Cension for approximately $152 million. The equipment acquired by the Company will be used for the Company s future expansion. The corporate guarantee was released after this purchase.

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25. COMMITMENTS

(a) Purchase commitments

As of December 31, 2008 the Company had the following commitments to purchase machinery, equipment and construction obligations. The machinery and equipment is scheduled to be delivered at the Company s facility by December 31, 2009.

Facility construction	$ 7,359,374
Machinery and equipment	$ 52,235,105
	$ 59,594,479

(b) Royalties

The Company has entered into several license and technology agreements with third parties. The terms of the contracts range from 3 to 10 years. The Company is subject to royalty payments based on a certain percentage of product sales, using the third parties technology or license. In 2008, 2007 and 2006, the Company incurred royalty expense of $18,867,409, $13,118,570 and $7,724,704, respectively, which was included in cost of sales.

The Company has entered into several license agreements with third parties where the Company provides access to certain licensed technology. The Company will receive royalty payments based on a certain percentage of product sales using the Company s licensed technology. In 2008, 2007 and 2006, the Company earned royalty income of $1,192,537, $1,428,603 and $1,384,137, respectively, which was included in sales. Royalty income is recognized one quarter in arrears when reports are received.

(c) Operating lease as lessor

The Company owns apartment facilities that are leased to the Company s employees at negotiated prices. The apartment rental agreement is renewed on an annual basis. The Company also leases office space to non-related third parties. Office lease agreements are renewed on an annual basis as well. The total amount of rental income recorded in 2008, 2007 and 2006 was $5,818,655, $6,937,107 and $6,142,692, respectively, and is recorded in other income in the statement of operations.

(d) Operating lease as lessee

The Company has various operating leases including land use rights, under non-cancellable leases expiring at various times through 2053. Future minimum lease payments under these leases as of December 31, 2008 are as follows:

Year ending	
2009	$ 6,055,605
2010	269,868
2011	202,580
2012	168,153
Thereafter	3,024,384

	$ 9,720,590

The total operating lease expense recorded in 2008, 2007 and 2006 was $1,084,894, $643,621 and $410,193, respectively.

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26. SEGMENT AND GEOGRAPHIC INFORMATION

The Company is engaged principally in the computer-aided design, manufacturing and trading of integrated circuits. In accordance with SFAS No. 131, Disclosures about Segments of an Enterprise and Related Information, the Company s chief operating decision maker has been identified as the Chief Executive Officer, who reviews consolidated results of manufacturing operations when making decisions about allocating resources and assessing performance of the Company. The Company believes it operates in one segment, and all financial segment information required by SFAS No. 131 can be found in the consolidated financial statements. The following table summarizes the Company s net revenues generated from different geographic locations:

	2008	2007	2006
Total sales:			
United States	**$ 767,966,660**	$ 657,603,189	$ 602,506,213
Europe	**92,572,683**	328,710,235	440,327,872
Asia Pacific (Excluding Japan and Taiwan)	**269,616,334**	227,973,648	168,607,598
Taiwan	**185,848,747**	183,113,880	153,057,616
Japan	**37,706,875**	152,364,336	100,823,568
	$ 1,353,711,299	$ 1,549,765,288	$ 1,465,322,867

Revenue is attributed to countries based on headquarter of customer operations and is not related to the shipment destination.

Substantially all of the Company s long-lived assets are located in the PRC.

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27. SIGNIFICANT CUSTOMERS

The following table summarizes net revenue and receivable from customers which accounted for 10% or more of our net revenue, accounts receivable, other current assets or receivable for sale of manufacturing equipment:

	Net revenue Year ended December 31,			Accounts receivable December 31,		
	2008	2007	2006	**2008**	2007	2006
A	**22%**	16%	17%	**23%**	14%	14%
B	**14%**	*	*	*	*	*
C	**13%**	*	*	*	*	*
D	*	18%	28%	*	15%	29%
E	*	*	*	*	13%	*
F	*	*	*	**16%**	*	*
G	*	*	*	**18%**	*	*

	Other current assets December 31,			Receivable for sale of manufacturing equipment December 31,		
	2008	2007	2006	**2008**	2007	2006
F	**50%**	29%	*	**83%**	100%	100%
G	*	*	*	**17%**	*	*

* Less than 10%

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28. LITIGATION

Overview of TSMC Litigation:

Beginning in December 2003 through August 2004, the Company became subject to several lawsuits brought by Taiwan Semiconductor Manufacturing Company, Limited (TSMC) relating to alleged infringement of certain patents and misappropriation of alleged trade secrets relating to methods for conducting semiconductor fab operations and manufacturing integrated circuits.

On January 30, 2005, the Company and TSMC exchanged signature pages later attached to a settlement agreement. Terms were added to the document subsequent to the exchange of signatures. The identification of the exact terms of the agreement were determined at a preliminary trial in 2009, as described below under Recent TSMC Legal Developments. As found by the California Superior Court, SMIC and TSMC agreed, without admission of liability, to dismiss all pending legal actions without prejudice between the two companies (the Settlement Agreement). The terms of the Settlement Agreement also were determined to include the following:

1) The Company and TSMC agreed to cross-license each other s patent portfolio for all semiconductor device products, effective from January 2005 through December 2010.

2) TSMC covenanted not to sue the Company for trade secret misappropriation as alleged in TSMC s legal actions as it related to .15ìm and larger processes subject to certain conditions (TSMC Covenant). The TSMC Covenant did not cover .13ìm and smaller technologies after 6 months following execution of the Settlement Agreement (July 31, 2005). Excluding the .13ìm and smaller technologies, the TSMC Covenant remains in effect indefinitely, terminable upon a breach by the Company.

3) The Company is required to deposit certain Company materials relating to .13ìm and smaller technologies into an escrow account until December 31, 2006 or under certain circumstances for a longer period of time.

4) The Company agreed to pay TSMC an aggregate of $175 million in installments of $30 million for each of the first five years and $25 million in the sixth year.

The Company believes the Court s ruling is erroneous. The ruling may be appealed by SMIC following the filing of a final judgment by the Court in this matter.

Accounting under the Settlement Agreement:

In accounting for the Settlement Agreement, the Company determined that there were several components of the Settlement Agreement settlement of litigation, covenant not to sue, patents licensed by us to TSMC and the use of TSMC s patent license portfolio both prior and subsequent to the settlement date.

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The Company does not believe that the settlement of litigation, covenant not to sue or patents licensed by us to TSMC qualify as accounting elements. In regard to the settlement of litigation, the Company cites the following:

1) The Settlement Agreement reached between TSMC and SMIC clearly stated that there was no admission of liability by either party;

2) The Settlement Agreement required all parties to bear their own legal costs;

3) There were no other damages associated with the Settlement Agreement;

4) There was a provision in the Settlement Agreement for a grace period to resolve any misappropriation issues had they existed;

5) Albeit a complaint had been filed by TSMC on trade secret infringement, TSMC has never identified to the Company which trade secrets it claimed were being infringed upon by the Company;

6) The Settlement Agreement was concluded when the litigation process was still at a relatively early stage and the outcome of the litigation was therefore highly uncertain.

The TSMC covenant not to sue for alleged trade secrets misappropriation does not qualify as a separable asset in accordance with either SFAS 141 or SFAS 142 as TSMC had never specified the exact trade secrets that it claimed were misappropriated, the Company s belief that TSMC s trade secrets may be obtained within the marketplace by other legal means and the Company never obtained the legal right to use TSMC s trade secrets.

In addition, the Company did not attribute any value to the patents licensed to TSMC under the Settlement Agreement due to the limited number of patents held by the Company at the time of the Settlement Agreement.

As a result, the Company determined that only the use of TSMC s patent license portfolio prior and subsequent to the settlement date were considered elements of an arrangement for accounting purposes. In attributing value to these two elements, the Company first discounted the payment terms of the $175 million settlement amount using an annual 3.4464% interest rate to arrive at a net present value of $158 million. This amount was then allocated to the pre- and post- settlement periods based on relative fair value, as further described below.

Based on this approach, $16.7 million was allocated to the pre-settlement period, reflecting the amount that the Company would have paid for use of the patent license portfolio prior to the date of the Settlement Agreement. The remaining $141.3 million, representing the relative fair value of the licensed patent license portfolio, was recorded on the Company s consolidated balance sheets as a deferred cost and is being amortized over a six-year period, which represents the life of the licensed patent license portfolio. The amortization of the deferred cost is included as a component of cost of sales in the consolidated statements of operations.

Valuation of Deferred Cost:

The fair value of the patent license portfolio was calculated by applying the estimated royalty rate to the specific revenue generated and expected to be generated from the specific products associated with the patent license portfolio.

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The selected royalty rate was based on the review of median and mean royalty rates for the following categories of licensing arrangements:

a) existing third-party license agreements with SMIC;

b) the analysis of comparable industry royalty rates related to semiconductor chip/integrated circuit (IC) related technology; and

c) the analysis of comparable industry royalty rates related to semiconductor fabrication.

On an annualized basis, the amounts allocated to past periods was lower than that allocated to future periods as the Company assumed increases in revenues relating to the specific products associated with the patent license portfolio. As the total estimated fair value of the patent license portfolio exceeded the present value of the settlement amount, the Company allocated the present value of the settlement amount based on the relative fair value of the amounts calculated prior and subsequent to the settlement date.

Recent TSMC Legal Developments:

On August 25, 2006, TSMC filed a lawsuit against the Company and certain subsidiaries, namely SMIC (Shanghai), SMIC (Beijing) and SM IC (Americas) in the Superior Court of the State of California, County of Alameda for alleged breach of a settlement agreement, alleged breach of promissory notes and alleged trade secret misappropriation by the Company. TSMC seeks, among other things, damages, injunctive relief, attorneys fees, and the acceleration of the remaining payments outstanding under that settlement agreement.

In the present litigation, TSMC alleges that the Company has incorporated TSMC trade secrets in the manufacture of the Company s 0.13 micron or smaller process products. TSMC further alleges that as a result of this claimed breach, TSMC s patent license is terminated and the covenant not to sue is no longer in effect with respect to the Company s larger process products. The Company has vigorously denied all allegations of misappropriation. The Court has made no finding that TSMC s claims are valid. The Court has set a trial date of September 8, 2009.

On September 13, 2006, the Company announced that in addition to filing a response strongly denying the allegations of TSMC in the United States lawsuit, it filed on September 12, 2006, a cross-complaint against TSMC seeking, among other things, damages for TSMC s breach of contract and breach of implied covenant of good faith and fair dealing.

On November 16, 2006, the High Court in Beijing, the People s Republic of China, accepted the filing of a complaint by the Company and its wholly-owned subsidiaries, namely, SMIC (Shanghai) and SMIC (Beijing), regarding the unfair competition arising from the breach of bona fide (i.e. integrity, good faith) principle and commercial defamation by TSMC (PRC Complaint). In the PRC Complaint, the Company is seeking, among other things, an injunction to stop TSMC s infringing acts, public apology from TSMC to the Company and compensation from TSMC to the Company, including profits gained by TSMC from their infringing acts.

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On August 14, 2007, the Company filed an amended cross-complaint against TSMC seeking, among other things, damages for TSMC s breach of contract and breach of patent license agreement. TSMC thereafter denied the allegations of the Company s amended cross-complaint and subsequently filed additional claims that the Company breached a settlement agreement by filing an action in the Beijing High Court. The Company has denied these additional claims by TSMC.

On August 15-17, 2007, the California Court held a preliminary injunction hearing on TSMC s motion to enjoin use of certain process recipes in certain of the Company s 0.13 micron logic process flows.

On September 7, 2007, the Court denied TSMC s preliminary injunction motion, thereby leaving unaffected the Company s development and sales. However, the court required the Company to provide 10 days advance notice to TSMC if the Company plans to disclose logic technology to non-SMIC entities under certain circumstances, to allow TSMC to object to the planned disclosure.

In May 2008, TSMC filed a motion in the California Court for summary adjudication against the Company on several of the Company s cross claims. The Company opposed the motion and on August 6, 2008, the Court granted in part and denied in part TSMC s motion.

On June 23, 2008, the Company filed in the California court a cross-complaint against TSMC seeking, among other things, damages for TSMC s unlawful misappropriation of trade secrets from SMIC to improve its competitive position against SM IC.

On July 10, 2008, the California Court held a preliminary injunction hearing on TSMC s motion to enjoin disclosure of information on certain process recipes in the Company s 0.30 micron logic process flows to 3rd parties. On August 8, 2008, the Court granted-in-part TSMC s motion and preliminarily enjoined SMIC from disclosing fourteen 0.30 ìm process steps. On October 3, 2008, SMIC filed a notice of appeal of the Court s August 8, 2008 Order with the California Court of Appeal. This appeal is currently pending.

During the pre-trial proceedings in the matter, questions arose regarding the actual terms of the 2005 Settlement Agreement between SMIC and TSMC. Accordingly, the California Court held a preliminary trial on January 13 to 16, 2009, limited to a determination of the terms of the Settlement Agreement and an interpretation of any requirements to meet and confer prior to institution of litigation. On March 10, 2009, the Court issued a Statement of Decision finding, in part, that an agreement between the parties was executed on January 30, 2005, and thereafter amended on February 2, 2005, as urged by TSMC. The Company believes the Court s ruling is erroneous. The ruling may be appealed by SMIC following the filing of a final judgment by the Court in this matter.

On May 1, 2009, the Company filed motions for summary adjudication against TSMC s claims for breach of promissory notes and violation of the California Uniform Trade Secrets Act. The motions will be heard by the Court on July 17, 2009.

The California Court has further scheduled a trial upon all liability issues related to a selected list of TSMC trade secret claims and SMIC trade secret claims to commence on September 8, 2009.

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In the Company s action in the Beijing High People s Court, following an unsuccessful challenge to that Court s jurisdiction by TSMC, the Court has held evidentiary hearings on October 15, October 29, and November 25, 2008. The Court rendered its first-instance judgment on June 10, 2009. Claims of SMIC against TSMC were not supported by the Court in the first-instance judgment. The first-instance judgment is not final and either TSMC or SMIC may further appeal to the PRC Supreme People s Court according to the law.

Under the provisions of SFAS 144, the Company is required to make a determination as to whether or not this pending litigation represents an event that requires a further analysis of whether the patent license portfolio has been impaired. We believe that the lawsuit is at a discovery stage and we are still evaluating whether or not the litigation represents such an event. The Company expects further information to become available to us, which will aid us in making a determination. The outcome of any impairment analysis performed under SFAS 144 might result in a material impact to our financial position and results of operations. Because the case is in its discovery stage, the Company is unable to evaluate the likelihood of an unfavorable outcome or to estimate the amount or range of potential loss.

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29. RETIREMENT BENEFIT

The Company s local Chinese employees are entitled to a retirement benefit based on their basic salary upon retirement and their length of service in accordance with a state-managed pension plan. The PRC government is responsible for the pension liability to these retired staff. The Company is required to make contributions to the state-managed retirement plan equivalent to 20% 22.5% of the monthly basic salary of current employees. Employees are required to make contributions equivalent to 6% 8% of their basic salary. The contribution of such an arrangement was approximately $11,039,680, $7,223,644 and $5,452,660 for the years ended December 31, 2008, 2007 and 2006, respectively. The retirement benefits do not apply to non-PRC citizens. The Company s retirement benefit obligations outside the PRC are not significant.

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30. DISTRIBUTION OF PROFITS

As stipulated by the relevant laws and regulations applicable to China s foreign investment enterprise, the Company s PRC subsidiaries are required to make appropriations from net income as determined under accounting principles generally accepted in the PRC (PRC GAAP) to non-distributable reserves which include a general reserve, an enterprise expansion reserve and a staff welfare and bonus reserve. Wholly-owned PRC subsidiaries are not required to make appropriations to the enterprise expansion reserve but appropriations to the general reserve are required to be made at not less than 10% of the profit after tax as determined under PRC GAAP. The staff welfare and bonus reserve is determined by the Board of Directors.

The general reserve is used to offset future extraordinary losses. The subsidiaries may, upon a resolution passed by the stockholders, convert the general reserve into capital. The staff welfare and bonus reserve is used for the collective welfare of the employee of the subsidiaries. The enterprise expansion reserve is for the expansion of the subsidiaries operations and can be converted to capital subject to approval by the relevant authorities. These reserves represent appropriations of the retained earnings determined in accordance with Chinese law. Appropriations to general reserve by the Company s PRC subsidiaries were nil, $15,640,153 and $11,956,185 in 2008, 2007 and 2006, respectively.

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31. COMPONENTS OF LOSS (INCOME) FROM OPERATIONS

	2008	2007	2006
Loss (income) from operations is arrived at after charging (crediting):			
Auditors remuneration	**$ 1,584,925**	$ 1,698,293	$ 1,577,928
Amortization of land use rights	**927,746**	886,293	577,578
Foreign currency exchange loss (gain)	**(8,195,569)**	3,117,962	3,939,745
Bad debt expense	**1,301,556**	486,920	2,957,505
Inventory write-down	**17,766,628**	6,570,137	2,297,773
Staff costs inclusive of directors remuneration	**$ 190,942,366**	$ 151,447,470	$ 108,742,094

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32. DIRECTORS REMUNERATION AND FIVE HIGHEST PAID INDIVIDUALS

Directors

Details of emoluments paid by the Company to the directors of the Company in 2008, 2007 and 2006 are as follows:

	Richard Chang	Kawanishi Tsuyoshi	Wang Yang Yuan	Hsu Ta-Lin	Lip-Bu Tan	Henry Shaw	Zheng Gang Wang	Albert Y.C.	Jiang Shang Zhou	Total
2008										
Salaries and other benefits	**$ 218,398**	**$**	**$**	**$**	**$**	**$**	**$**	**$**	**$**	**$ 218,398**
Stock option benefits	**144,300**	**4,285**	**4,285**	**4,285**	**4,285**	**4,285**		**12,489**		**178,214**
Total emoluments	**$ 362,698**	**$ 4,285**	**$ 4,285**	**$ 4,285**	**$ 4,285**	**$ 4,285**	**$**	**$ 12,489**	**$**	**$ 396,612**
2007										
Salaries and other benefits	$ 195,395	$	$	$	$	$	$	$	$	$ 195,395
Stock option benefits	172,203	17,189	17,189	17,189	17,189	17,189		50,094		308,242
Total emoluments	$ 367,598	$ 17,189	$ 17,189	$ 17,189	$ 17,189	$ 17,189	$	$ 50,094	$	$ 503,637
2006										
Salaries and other benefits	$ 192,727	$	$	$	$	$	$	$	$	$ 192,727
Stock option benefits	156,241	12,951	12,951	12,951	12,951	12,951		37,742		258,738
Total emoluments	$ 348,968	$ 12,951	$ 12,951	$ 12,951	$ 12,951	$ 12,951	$	$ 37,742	$	$ 451,465

The emoluments of the directors were within the following bands:

	2008 Number of directors	2007 Number of directors	2006 Number of directors
HK$nil to HK$1,000,000 ($128,620)	**8**	9	10
HK$1,000,001 ($128,620) to HK$1,500,000 ($192,930)			
HK$1,500,001 ($192,930) to HK$2,000,000 ($257,240)			
HK$2,000,001 ($257,240) to HK$2,500,000 ($321,550)			
HK$2,500,001 ($321,550) to HK$3,000,000 ($385,860)	**1**	1	1

The Company granted nil, nil and 3,500,000 options to purchase ordinary shares of the Company to the directors in 2008, 2007 and 2006, respectively. During the year ended December 31, 2008, no stock options were exercised and 500,000 stock options were cancelled by the directors. The cancellation was due to the resignation of a director.
The Company granted nil, nil and 500,000 restricted share units to purchase ordinary shares of the Company to the directors in 2008, 2007 and 2006, respectively. During the year ended December 31, 2008, 500,000 restricted share units automatically vested and no restricted share units were cancelled.

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In 2008, 2007 and 2006, no emoluments were paid by the Company to any of the directors as an inducement to join or upon joining the Company or as compensation for loss of office. In September 2006, two directors were each offered options to purchase 500,000 ordinary shares. Both directors declined the options.

Five highest paid employees emoluments

Of the five individuals with the highest emoluments in the Group, one is a director of the Company whose emoluments are included in the disclosure above. The emoluments of the remaining four in 2008, 2007 and 2006 are as follows:

	2008	2007	2006
Salaries and other benefits	**$ 941,001**	$ 586,065	$ 518,198
Bonus		237,969	233,662
Stock option benefits	**232,296**	283,125	268,528
Total emoluments	**$ 1,173,297**	$ 1,107,159	$ 1,020,388

The bonus is determined on the basis of the basic salary and the performance of the Company and the individual. Their emoluments were within the following bands:

	2008 Number of individuals	2007 Number of individuals	2006 Number of individuals
HK$nil to HK$1,000,000 ($128,620)			
HK$1,000,001 ($128,620) to HK$1,500,000 ($192,930)	**1**		
HK$1,500,001 ($192,930) to HK$2,000,000 ($257,240)	**3**		3
HK$2,000,001 ($257,240) to HK$2,500,000 ($321,550)	**1**	4	1
HK$2,500,001 ($321,550) to HK$4,500,000($578,790)		1	1
HK$4,500,001 ($578,790) to HK$5,000,000 (643,100)			

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33. DIVIDEND

No dividend has been paid or declared by the Company in 2008, 2007 and 2006.

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34. SUBSEQUENT EVENTS

On January 1, 2009, the minority interest holders of AT redeemed 8,000,000 Series A shares with a total redemption amount of $9,013,444.

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35. DIFFERENCE BETWEEN US GAAP AND INTERNATIONAL FINANCIAL REPORTING STANDARDS

The consolidated financial statements are prepared in accordance with US GAAP, which differ in certain significant respects from International Financial Reporting Standards (IFRS). The significant differences relate principally to share-based payments to employees and non-employees, presentation of minority interest, convertible financial instruments and assets held for sale.

(i) In regard to accounting treatment for share-based payments, IFRS 2, Share Based Payment , was issued to specify recognition, measurement and disclosure for equity compensation. IFRS 2 requires all share-based payment to be recognized in the financial statements using a fair value measurement basis. An expense should be recognized when goods or services received are consumed. IFRS 2 was effective for periods beginning on or after January 1, 2005.

Had the Company prepared the financial statements under IFRS, the Company would have adopted IFRS 2 retrospectively for the fiscal year beginning on January 1, 2005 and compensation expenses on share-based payments to employees would have been calculated using fair value method for the years prior to January 1, 2006.

Under US GAAP, prior to the adoption of the SFAS 123(R) from January 1, 2006, the Company was able to account for stock-based compensation issued to employees using either intrinsic value method or fair value method and the Company adopted the intrinsic value method of accounting for its stock options to employees.

Under the intrinsic value method, compensation expense is the excess, if any, of the fair value of the stock at the grant date or other measurement date over the amount an employee must pay to acquire the stock. Compensation expense, if any, is recognized over the applicable service period, which is the vesting period.

Effective January 1, 2006, the Company adopted the provisions of SFAS 123(R), Share-Based Payment . Under the provisions of SFAS 123(R), share-based compensation is measured at the grant date, based on the fair value of the award similar to IFRS 2. In addition, under SFAS 123(R) the Company was no longer required to record deferred sharebased compensation related to unvested share options in stockholder s equity, consistent with IFRS 2. Upon the adoption of this accounting principle, the Company has recorded a cumulative effect of $5,153,986 in the year 2006 under US GAAP, which is not required under IFRS2.

(ii) Under US GAAP, the Series A shares of AT are accounted as minority interest and presented as temporary equity. The Series A shares are accreted to their redemption value at each reporting date. The accretion of interest is presented as minority interest expense in the consolidated statements of operations.

Under IFRS, the Series A shares of AT contains both liability and conversion option components. A conversion option that will be settled by the exchange of a fixed amount of cash or another financial asset for a fixed number of AT s ordinary shares is classified as an equity instrument.

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On initial recognition, the fair value of the liability component is determined using the prevailing market interest of similar non-convertible debt. The different between the gross proceeds from the issuance of the Series A shares and the fair value assigned to the liability components, presenting the conversion option for the holder to convert the loan notes into equity, is included in equity. In subsequent periods, the liability component is carried at amortized cost using the effective interest method. The equity component, representing the option to convert the liability component into ordinary shares of AT, will remain in equity until the embedded option is exercised. No gain or loss is recognized in profit or loss upon conversion or expiration of the conversion option.

The value assigned to the conversion option of the Series A shares is considered to be insignificant at initial recognition. The accretion of interest to record the Series A shares at redemption value is recognized as interest expense.

(iii) Under US GAAP, a beneficial conversion feature refers to the preferential price of certain convertible equity instruments an investor receives when the effective conversion price of the equity instruments in lower than the fair market value of the common stock to which the convertible equity instrument is convertible into at the date of issuance. US GAAP requires the recognition of the difference between the effective conversion price of the convertible equity instrument and the fair market value of the common stock as a deemed dividend.

Under IFRS, this deemed dividend is not required to be recorded.

(iv) Under IFRS, leases of land and buildings are classified as operating or finance leases in the same way as leases of other assets. However, a characteristic of land is that it normally has an indefinite economic life and, if title is not expected to pass to the lessee by the end of the lease term, the lessee normally does not receive substantially all of the risks and rewards incidental to ownership, in which case the lease of land will be an operating lease. A payment made on entering into or acquiring a leasehold that is accounted for as an operating lease represents lease prepayments that are amortized over the lease term in accordance with the pattern of benefits provided. For balance sheet presentation, the prepayment of land use rights should be disclosed as current and non-current.

Under US GAAP, land use rights are also accounted as operating leases and represent lease pre-payments that are amortized over the lease term in accordance with the pattern of benefits provided. Current and non-current asset classification is not required under US GAAP.

(v) IFRS requires an enterprise to evaluate at each balance sheet date whether there is any indication that a long-lived asset may be impaired. If any such indication exists, an enterprise should estimate the recoverable amount of the long-lived asset. Recoverable amount is the higher of a long-lived asset s net selling price and its value in use. Value in use is measured on a discounted present value basis. An impairment loss is recognized for the excess of the carrying amount of such assets over their recoverable amounts. A reversal of previous provision of impairment is allowed to the extent of the loss previously recognised as expense in the income statement.

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Under US GAAP, long-lived assets and certain identifiable intangibles (excluding goodwill) held and used by an entity are reviewed for impairment whenever events or changes in circumstances indicate that the carrying value of a long-lived asset and certain identifiable intangibles (excluding goodwill) may not be recoverable. An impairment loss is recognized if the expected future cash flows (undiscounted) are less than the carrying amount of the assets. The impairment loss is measured based on the fair value of the long-lived assets and certain identifiable intangibles (excluding goodwill). Subsequent reversal of the loss is prohibited. Long-lived assets and certain identifiable intangibles (excluding goodwill) to be disposed of are reported at the lower of carrying amount or fair value less cost to sell.

The Company considered the operating loss in SMIB to be an impairment indicator for its long-lived assets in SMIB and evaluated whether or not such assets have been impaired at December 31, 2007. The undiscounted expected future cash flows were in excels of the carrying amount of the relevant long-lived assets and no impairment loss was required to be recognized under US GAAP in 2007. However, under IFRS, the estimated recoverable value derived from a discounted expected cash flow was less than the carrying value of those long-lived assts. As such, the Company has recognized an impairment loss of US$105,774,000 for the year ended December 31, 2007 under IFRS.

The Company reached an agreement with certain customers to discontinue production of DRAM products and subsequently the Company s Board of Directors decided to exit the commodity DRAM business as a whole. The Company considered these actions to be an indicator of impairment in regard to the plant and equipment in the Company s Beijing facility. Based on a detailed analysis, the Company recorded an impairment loss of $105,774,000, equal to the excess of the carrying value over the fair value of the associated assets under US GAAP in 2008.

The difference in timing of recognition of impairment loss under US GAAP and IFRS give rise to the difference in depreciation charges on long-lived assets after impairment allocation, which would be gradually reversed in future periods when the long-lived assets are fully depreciating.

(vi) Under US GAAP, income (loss) from equity investment is presented as a separate item before net income (loss) on net of tax basis.

Under IFRS, the income (loss) from equity investment is presented as a component of income (loss) before income tax benefit (expense).

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The adjustments necessary to restate loss attributable to holders of ordinary shares and stockholders equity in accordance with IFRS are shown in the tables set out below.

	2008	2007	2006
Net loss under US GAAP	**$ (440,231,120)**	$ (19,468,147)	$ (44,109,078)
IFRS adjustments:			
i) Reverse of cumulative effect of a change in accounting principle for share-based payment			(5,153,986)
ii) Accretion of interest on Series A Share	**3,055,592**	(2,856,258)	18,803
v) Impairment of long-lived assets	**105,774,000**	(105,774,000)	
v) Depreciation of long-lived assets	**4,633,535**		
Net loss under IFRS	**$ (326,767,993)**	$ (128,098,405)	$ (49,244,261)
Net loss per share under IFRS	**$ (0.02)**	$ (0.01)	$ (0.00)
Stockholders equity as reported under US GAAP	**$ 2,749,364,501**	$ 3,012,519,022	$ 3,007,419,918
ii) Presentation of minority interest		34,944,408	38,800,666
v) Impairment of long-lived assets		(105,774,000)	
v) Depreciation of long-lived assets	**4,633,535**		
Stockholders equity under IFRS	**$ 2,753,998,036**	$ 2,941,689,430	$ 3,046,220,584
Current liabilities as reported under US GAAP	**$ 899,772,911**	$ 930,190,120	$ 677,361,816
ii) Presentation of Series A shares	**42,795,288**		
Under IFRS	**$ 942,568,199**	$ 930,190,120	$ 677,361,816
Land use rights, net current portion as reported under US GAAP	**$**	$	$
IFRS adjustment			
iv) Current portion adjustment for land use right	**1,442,730**	1,054,777	712,521
Under IFRS	**$ 1,442,730**	$ 1,054,777	$ 712,521
Land use rights, net			
As reported under US GAAP	**$ 74,293,284**	$ 57,551,991	$ 38,323,333
IFRS adjustments			
iv) Current portion adjustment for land use right	**(1,442,730)**	(1,054,777)	(712,521)
Under IFRS	**$ 72,850,554**	$ 56,497,214	$ 37,610,812

Plant and equipment			
As reported	**$ 2,963,385,840**	$ 3,202,957,665	$ 3,244,400,822
IFRS adjustments			
v) Impairment of long lived assets		(105,774,000)	
v) Depreciation of long lived assets	**4,633,535**		
Under IFRS	**$ 2,968,019,375**	$ 3,097,183,665	$ 3,244,400,822
Additional paid-in capital as reported under US GAAP	**$ 3,489,382,267**	$ 3,313,375,972	$ 3,288,765,465
IFRS adjustments			
i) Retrospective adjustment on adoption of IFRS 2	**30,388,316**	30,388,316	30,388,316
i) Reverse of cumulative effect of a change in accounting principle	**5,153,986**	5,153,986	5,153,986
iii) Carry forward prior year s adjustment on deemed dividend	**(55,956,051)**	(55,956,051)	(55,956,051)
Under IFRS	**$ 3,468,968,518**	$ 3,292,962,223	$ 3,268,351,716
Accumulated deficit as reported under US GAAP	**$ (748,509,757)**	$ (308,278,637)	$ (288,810,490)
IFRS adjustments			
i) Carried over impact under IFRS 2	**(30,388,316)**	(30,388,316)	(30,388,316)
i) Reverse of cumulative effect of a change in accounting principle	**(5,153,986)**	(5,153,986)	(5,153,986)
iv) Carry forward prior year s adjustment on deemed dividend	**55,956,051**	55,956,051	55,956,051
v) Impairment of long-lived assets		(105,774,000)	
v) Depreciation of long-lived assets	**4,633,535**		
Under IFRS	**$ (723,462,473)**	$ (393,638,888)	$ (268,396,741)

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	2008	2007	2006
Cost of sales as reported under US GAAP	**$ 1,412,851,079**	$ 1,397,037,881	$ 1,338,155,004
IFRS adjustments			
v) Depreciation of long-lived assets	**(4,633,535)**		
Under IFRS	**$ 1,408,217,544**	$ 1,397,037,881	$ 1,338,155,004
Operating expenses as reported under US GAAP	**$ 317,797,068**	$ 188,659,217	$ 141,037,963
IFRS adjustments			
v) Impairment of long-lived assets	**(105,774,000)**	105,774,000	
Under IFRS	**$ 212,023,068**	$ 294,433,217	$ 141,037,963
Interest expense as reported under US GAAP	**$ 50,766,958**	$ 37,936,126	$ 50,926,084
IFRS adjustments			
ii) Accretion of interest on Series A shares	**4,795,288**		
Under IFRS	**$ 55,562,246**	$ 37,936,126	$ 50,926,084
Loss before income tax as reported under US GAAP	**$ (405,503,036)**	$ (48,031,515)	$ (69,970,758)
IFRS adjustments			
v) Impairment of long-lived assets	**105,774,000**	(105,774,000)	
v) Depreciation of long-lived assets	**4,633,535**		
vi) Presentation of income (loss) from equity investment	**(444,211)**	(4,012,665)	(4,201,247)
ii) Accretion of interest on Series A shares	**(4,795,288)**		
Under IFRS	**$ (300,335,000)**	$ (157,818,180)	$ (74,172,005)

In addition to the above, there are also other differences between US GAAP and IFRS relevant to the accounting policies of the Company. These differences have not led to any material differences in 2008, 2007 and 2006, and details of which are set out as below:

(a) Inventory valuation

Inventories are carried at cost under both US GAAP and IFRS. However, if there is evidence that the net realisable value of goods, in their disposal in the ordinary course of business, will be less than cost, whether due to physical obsolescence, changes in price levels, or other causes, the difference should be recognized as a loss of the current period. This is generally accomplished by stating such goods at a lower level commonly known as market .

Under US GAAP, a write-down of inventories to the lower of cost or market at the close of a fiscal period creates a new cost basis that subsequently cannot be reversed based on changes in underlying facts and circumstances.

Market under US GAAP is the lower of the replacement cost and net realizable value minus normal profit margin.

Under IFRS, a write-down of inventories to the lower of cost or market at the close of a fiscal period is a valuation allowance that can be subsequently reversed if the underlying facts and circumstances changes. Market under IFRS is net realizable value.

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SEMICONDUCTOR MANUFACTURING INTERNATIONAL CORPORATION
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(In US dollars, except where otherwise stated)

(b) Deferred income taxes

Deferred tax liabilities and assets are recognized for the estimated future tax effects of all temporary differences between the financial statement carrying amount of assets and liabilities and their respective tax bases under both US GAAP and IFRS.

Under IFRS, a deferred tax asset is recognized to the extent that it is probable that future profits will be available to offset the deductible temporary differences or carry forward of unused tax losses and unused tax credits. Under US GAAP, all deferred tax assets are recognized, subject to a valuation allowance, to the extent that it is more likely than not that some portion or all of the deferred tax assets will be realized. More likely than not is defined as a likelihood of more than 50%.

With regard to the measurement of the deferred tax, IFRS requires recognition of the effects of a change in tax laws or rates when the change is substantively enacted . US GAAP requires measurement using tax laws and rates enacted at the balance sheet date.

Under US GAAP, deferred tax liabilities and assets are classified as current or non-current based on the classification of the related asset or liability for financial reporting. Under IFRS, deferred tax assets and liabilities are always classified as non-current.

(c) Segment reporting

Under IFRS, a listed enterprise is required to determine its primary and secondary segments on the basis of lines of business and geographical areas, and to disclose results, assets and liabilities and certain other prescribed information for each segment. The determination of primary and secondary segment is based on the dominant source of the enterprise s business risks and returns. Accounting policies adopted for preparing and presenting the financial statements of the Company should also be adopted in reporting the segmental results and assets. The business segment is considered as the primary segment for the Company. Meanwhile, the Management believes the risk and return shall be similar among its different geographical segments.

Under US GAAP, a public business enterprise is required to report financial and descriptive information about its reportable operating segments. Operating segments are components of an enterprise about which separate financial information is available that is evaluated regularly by the chief operating decision maker in deciding how to allocate resources and in assessing performance. US GAAP also permits the use of the accounting polices used for internal reporting purposes that are not necessarily consistent with the accounting policies used in consolidated financial statements.

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(d) Borrowing costs

IFRS and US GAAP require capitalization of borrowing costs for those borrowings that are directly attributable to acquisition, construction or production of assets that necessarily take a substantial period of time to get ready for their intended use or sale. The amount to be capitalized is the borrowing cost which could theoretically have been avoided if the expenditure on the qualifying asset was not made. Under IFRS, borrowing costs are defined as interest and any other costs incurred by an enterprise in connection with the borrowing of funds, while under the US GAAP, borrowing costs are defined as interest only.

Under IFRS, to the extent that funds are borrowed specifically for the purpose of obtaining a qualified asset, the amount of borrowing costs eligible for capitalization is determined as the actual borrowing costs incurred on the borrowing during the period less any investment income on the temporary investment of those borrowing. The amount of borrowing costs to be capitalized under US GAAP is based solely on actual interest incurred related to the actual expenditure incurred.

(e) Research and development costs

IFRS requires the classification of the costs associated with the creation of intangible assets by research phase and development phase. Costs in the research phase must always be expensed. Costs in the development phase are expensed unless the entity can demonstrate all of the following:

the technical feasibility of completing the intangible asset so that it will be available for use or sale;

its intention to complete the intangible asset and use or sell it;

its ability to use or sell the intangible asset;

how the intangible asset will generate probable future economic benefits. Among other things, the enterprise should demonstrate the existence of a market for the output of the intangible asset or the intangible asset itself or, if it is to be used internally, the usefulness of the intangible asset;

the availability of adequate technical, financial and other resources to complete the development and to use or sell the intangible asset; and

its ability to measure the expenditure attributable to the intangible asset during the development phase.

Under US GAAP, research and development costs are expensed as incurred except for:

those incurred on behalf of other parties under contractual arrangements;

those that are unique for enterprises in the extractive industries;

certain costs incurred internally in creating a computer software product to be sold, leased or otherwise marketed, whose technological feasibility is established, i.e. upon completion of a detailed program design or, in its absence, upon completion of a working model; and

certain costs related to the computer software developed or obtained for internal use.

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The general requirement to write off expenditure on research and development as incurred is extended to research and development acquired in a business combination.

(f) Statements of cash flows

There are no material differences on statements of cash flows between US GAAP and IFRS. Under US GAAP, interest received and paid must be classified as an operating activity. Under IFRS, interest received and paid may be classified as an operating, investing, or financing activity.

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ADDITIONAL INFORMATION FINANCIAL STATEMENTS SCHEDULE I
SEMICONDUCTOR MANUFACTURING INTERNATIONAL CORPORATION
FINANCIAL INFORMATION OF PARENT COMPANY
BALANCE SHEETS
(In US dollars, except share data)

	December 31,		
	2008	**2007**	**2006**
ASSETS			
Current assets:			
Cash and cash equivalents	$ 164,107,042	$ 6,042,030	$ 33,450,295
Accounts receivable, net	260,331	10,970,690	
Amount due from subsidiaries	203,326,525	21,586,283	138,701,627
Prepaid expense and other current assets	30,767,721	12,278,199	8,490,138
Total current assets	398,461,619	50,877,202	180,642,060
Plant and equipment, net	5,210,772	6,723,900	5,321,319
Acquired intangible assets, net	187,061,939	216,281,235	71,115,222
Deferred cost, net	47,091,516	70,637,275	94,183,034
Investment in subsidiaries	2,553,682,338	2,995,391,546	2,962,930,960
Investment in equity affiliate	9,452,186	9,896,398	13,619,643
TOTAL ASSETS	**$ 3,200,960,370**	**$ 3,349,807,556**	**$ 3,327,812,238**
LIABILITIES AND STOCKHOLDERS EQUITY			
Current liabilities:			
Accounts payable	$ 20,231,796	$ 4,811,093	$
Accrued expenses and other current liabilities	81,367,429	34,021,253	46,191,765
Amount due to subsidiaries	61,512,045	76,762,892	84,080,142
Short-term borrowings	181,257,773	20,000,000	31,000,000
Current portion of promissory note	29,242,001	29,242,000	29,242,001
Current portion of long-term payables relating to license agreements	44,711,003	69,189,413	12,690,472
Income tax payable	474,983	1,149,983	
Total current liabilities	418,797,030	235,176,634	203,204,380

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	December 31,		
	2008	**2007**	**2006**
Long-term liabilities:			
Promissory notes	23,589,958	51,057,163	96,861,657
Long-term payables relating to license agreements	9,208,881	51,054,737	16,992,950
Other long term liabilities			3,333,333
Total long-term liabilities	32,798,839	102,111,900	117,187,940
Total liabilities	$ 451,595,869	$ 337,288,534	$ 320,392,320
Stockholders equity:			
Ordinary shares, $0.0004 par value, 50,000,000,000 shares authorized, shares issued and outstanding 22,327,784,827, 18,558,919,712, and 18,432,756,463, respectively	8,931,114	7,423,568	7,373,103
Additional paid-in capital	3,489,382,267	3,313,375,972	3,288,765,465
Accumulated other comprehensive (loss) income	(439,123)	(1,881)	91,840
Accumulated deficit	(748,509,757)	(308,278,637)	(288,810,490)
Total stockholders equity	2,749,364,501	3,012,519,022	3,007,419,918
TOTAL LIABILITIES AND STOCKHOLDERS EQUITY	**$ 3,200,960,370**	**$ 3,349,807,556**	**$ 3,327,812,238**

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SEMICONDUCTOR MANUFACTURING INTERNATIONAL CORPORATION
FINANCIAL INFORMATION OF PARENT COMPANY
STATEMENTS OF OPERATIONS
(In US dollars)

	Year ended December 31,		
	2008	**2007**	**2006**
Revenue	$ 208,459,285	$ 12,363,023	$ 81,000
Operating expenses:			
General and administrative expenses	48,818,885	61,970,384	42,208,145
Amortization of deferred cost and acquired intangible assets	51,728,389	48,049,863	47,073,403
Impairment loss of long-lived assets	966,667		
Total operating expenses	**101,513,941**	**110,020,247**	**89,281,548**
Loss from operations	**106,945,344**	**(97,657,224)**	**(89,200,548)**
Other income (expense):			
Interest income	571,870	1,267,478	1,290,279
Interest expense	(11,637,266)	(6,029,720)	(12,880,250)
Other expense, net	(3,889,327)	(2,610,379)	(20,125,363)
Total other expense, net	**(14,954,723)**	**(7,372,621)**	**(31,715,334)**
Net income (loss) before income tax	**91,990,621**	**(105,029,845)**	**(120,915,882)**
Income tax expense	(15,030,257)	(1,149,983)	
Loss from equity investment	(444,211)	(4,012,665)	(4,201,247)
Profit (loss) from investment in subsidiaries	(516,747,273)	90,724,346	75,854,065
Net loss before cumulative effect of a change in accounting principle	**(440,231,120)**	**(19,468,147)**	**(49,263,064)**
Cumulative effect of a change in accounting principle			5,153,986
Net loss	**$ (440,231,120)**	**$ (19,468,147)**	**$ (44,109,078)**

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SEMICONDUCTOR MANUFACTURING INTERNATIONAL CORPORATION
FINANCIAL INFORMATION OF PARENT COMPANY
STATEMENTS OF CASH FLOWS
(In US dollars)

	Year ended December 31,		
	2008	**2007**	**2006**
Operating activities			
Loss attributable to holders of ordinary shares	$ (440,231,120)	$ (19,468,147)	$ (44,109,078)
Less: Cumulative effect of a change in accounting principle			(5,153,986)
Net loss	(440,231,120)	(19,468,147)	(49,263,064)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:			
Loss (profit) from investment in subsidiaries	516,747,273	(90,724,346)	(75,854,065)
Loss from equity investment	444,211	4,012,665	4,201,247
Depreciation and amortization	51,733,790	48,381,796	47,322,544
Impairment loss of long-lived assets	966,667		
Share-based compensation	11,617,572	20,643,341	23,506,847
Non-cash interest expense on promissory note and long-term payable relating to license agreements	6,208,530	4,579,116	5,702,607
Changes in operating assets and liabilities:			
Accounts receivable, net	10,710,359	(10,970,690)	
Amount due from subsidiaries	(102,943,505)	117,115,344	552,254,977
Prepaid expense and other current assets	(18,489,522)	(3,788,061)	1,151,816
Accounts payable	1,482,771	4,811,093	
Amount due to subsidiaries	(15,250,847)	(7,317,250)	71,206,587
Accrued expenses and other current liabilities	50,055,886	(5,397,776)	(11,229,650)
Other long term liabilities		(3,333,333)	3,333,333
Income tax payable	(675,000)	1,149,983	
Dividend received from a subsidiary	47,000,000	315,000,000	
Net cash provided by operating activities	**119,377,065**	**374,693,735**	**572,333,179**
Investing activities:			
Purchase of plant and equipment	(145,071,160)	(1,734,514)	(5,235,928)
Proceeds from sell of plant and equipment	81,720,082		
Purchases of acquired intangible assets	(75,639,710)	(87,295,157)	(9,573,524)
Sale of short-term investments			6,352,678
Investment in subsidiaries	(122,038,065)	(256,736,240)	(426,974,644)
Net cash used in investing activities	**(261,028,853)**	**(345,765,911)**	**(435,431,418)**

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	Year ended December 31,		
	2008	2007	2006
Financing activities:			
Proceeds from short-term borrowing	418,357,773	154,383,000	225,003,998
Repayment of short-term debt	(257,100,000)	(165,383,000)	(369,485,080)
Repayment of promissory notes	(30,000,000)	(49,260,000)	(42,740,000)
Proceeds from exercise of employee stock options	796,269	4,039,131	3,965,308
Repurchase of restricted ordinary shares		(21,500)	(58,190)
Proceeds from issuance of ordinary shares	168,100,000		
Net cash provided by (used in) financing activities	**300,154,042**	**(56,242,369)**	**(183,313,964)**
Effect of exchange rate changes	(437,242)	(93,720)	(47,138)
NET DECREASE IN CASH AND CASH EQUIVALENTS	**158,065,012**	**(27,408,265)**	**(46,459,341)**
CASH AND CASH EQUIVALENTS, beginning of period	6,042,030	33,450,295	79,909,636
CASH AND CASH EQUIVALENTS, end of period	$ 164,107,042	$ 6,042,030	$ 33,450,295
SUPPLEMENTAL DISCLOSURES OF NON-CASH INVESTING AND FINANCIAL ACTIVITIES			
Inception of accounts payable for plant and equipment	$ (20,231,796)	$ (4,811,094)	$
Inception of long-term payable for acquired intangible assets	$ (9,208,881)	$ (51,054,737)	$ (16,992,950)

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SEMICONDUCTOR MANUFACTURING INTERNATIONAL CORPORATION
FINANCIAL INFORMATION OF PARENT COMPANY NOTES TO SCHEDULE I

1. The financial statements of Semiconductor Manufacturing International Corporation (the Company) have been prepared in accordance with accounting principles generally accepted in the United States of America (US GAAP) except for accounting of the Company s subsidiaries and certain footnote disclosures as described below.
2. Certain information and footnote disclosures normally included in financial statements prepared in accordance with US GAAP have been condensed or omitted. The footnote disclosures contain supplemental information relating to the operations of the Company and, as such, these statements should be read in conjunction with the notes to the Consolidated Financial Statements of the Company.
3. As of December 31, 2008, 2007 and 2006, there were no material contingencies, significant provisions of long-term obligations, mandatory dividend or redemption requirements of redeemable stocks or guarantees of the Company, except for those which have been separately disclosed in the Consolidated Financial Statement, if any.
4. For the year ended December 31, 2008, $47,000,000 cash dividend was paid to the Company by SMIS. For the year ended December 31, 2007, $315,000,000 cash dividend was paid to the Company by SMIS. For the years ended December 31, 2006, there was no cash dividends paid to the Company by its consolidated subsidiaries.

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Annex A
GLOSSARY OF TECHNICAL TERMS

ASIC	Application Specific Integrated Circuit. A proprietary integrated circuit designed and manufactured to meet a customer s specific functional requirements.
Cell	A primary unit that normally repeats many times in an integrated circuit. Cells represent individual functional design units or circuits that may be reused as blocks in designs. For example, a memory cell represents a storage unit in a memory array.
CIS	CMOS Image Sensor. CIS can be used in applications such as still and video cameras and embedded cameras in mobile telephones. It is a fast growing imaging sensor technology. The fabrication of CIS is fully compatible with the mainstream CMOS process, which enables system-on-chip capability, low power consumption and low cost of fabrication.
Clean room	Area within a fab in which the wafer fabrication takes place. The classification of a clean room relates to the maximum number of particles of contaminants per cubic foot within that room. For example, a class 100 clean room contains less than 100 particles of contaminants per cubic foot.
CMOS	Complementary Metal Oxide Silicon. A fabrication process that incorporates n-channel and p-channel CMOS transistors within the same silicon substrate. Currently, this is the most commonly used integrated circuit fabrication process technology and is one of the latest fabrication techniques to use metal oxide semiconductor transistors.
CVD	Chemical Vapor Deposition. A process in which gaseous chemicals react on a heated wafer surface to form solid film.
Die	One individual chip cut from a wafer before being packaged.
Dielectric material	A type of non-conducting material used for isolation purposes between conductors, such as metals.
DRAM	Dynamic Random Access Memory. A device that temporarily stores digital information but requires regular refreshing to ensure data is not lost.
DSP	Digital Signal Processor. A type of integrated circuit that processes and manipulates digital information after it has been converted from an analog source.
EEPROM	Electrically Erasable Programmable Read-Only Memory. An integrated circuit that can be electrically erased and electrically programmed with user-defined information.
EPROM	Erasable Programmable Read-Only Memory. A form of PROM that is programmable electrically yet erasable using ultraviolet light.

FCRAM	Fast Cycle Random Access Memory. A proprietary form of RAM developed by Fujitsu Limited.
Fill factor	The percentage of LCOS metal surface area used for light reflection as compared to the total surface area. The higher the fill factor, the more light will be reflected from a given surface area.
Flash memory	A type of non-volatile memory where data is erased in blocks. The name flash is derived from the rapid block erase operation. Flash memory requires only one transistor per memory cell versus two transistors per memory cell for EEPROMs, making flash memory less expensive to produce. Flash memory is the most popular form of non-volatile semiconductor memory currently available.
Gold Bumping	The fabrication process of forming gold bump termination electrodes on a finished wafer.
High voltage semiconductor	High voltage semiconductors are semiconductor devices that can drive relatively high voltage potential to systems that require higher voltage of between five volts to several hundred volts.
IDM	Integrated Device Manufacturer.
Integrated circuit	An electronic circuit where all the elements of the circuit are integrated together on a single semiconductor substrate.

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Interconnect	Conductive materials such as aluminum, doped polysilicon or copper that form the wiring circuitry to carry electrical signals to different parts of the chip.
I/O	Inputs/Outputs.
LCOS	Liquid Crystal On Silicon. A type of micro-display technology.
Logic device	A device that contains digital integrated circuits that perform a function rather than store information.
Low leakage	Characteristic of a transistor that has a low amount of current leakage. Low leakage allows for power-saving. Low leakage semiconductors are primarily used in applications such as cellular telephones, calculators and automotive applications.
Mask	A glass plate with a pattern of transparent and opaque areas used to create patterns on wafers. Mask is commonly used to refer to a plate that has a pattern large enough to pattern a whole wafer at one time, as compared to a reticle, where a glass plate can contain the pattern for one or more dies but is not large enough to transfer a wafer-sized pattern all at once.
Mask ROM	A type of non-volatile memory that is programmed during fabrication (mask-defined) and the data can be read but not erased.
Memory	A device that can store information for later retrieval.
Micro-display	A small display that is of such high resolution that it is only practically viewed or projected with lenses or mirrors. A micro-display is typically magnified by optics to enlarge the image viewed by the user. For example, a miniature display smaller than one inch in size may be magnified to provide a 12-inch to 60-inch viewing area.
Micron	A term for micrometer, which is a unit of linear measure that equals one one-millionth (1/1,000,000) of a meter. There are 25.4 microns in one one-thousandth of an inch.
Mixed-signal	The combination of analog and digital circuitry in a single semiconductor.
MOS	Metal Oxide Semiconductor. A type of semiconductor device fabricated with a conducting layer and a semiconducting layer separated by an insulating layer.
NAND Flash	A type of flash memory commonly used for mass storage applications such as MP3 players and digital cameras.
Nanometer	A term for micrometer, which is a unit of linear measure that equals one thousandth (1/1,000) of a micron.

Non-volatile memory	Memory products that maintain their content when the power supply is switched off.
OTP	One-time programmable memory used for program and data storage, usually used in applications that require only a one-time data change.
PROM	Programmable Read-Only Memory. Memory that can be reprogrammed once after manufacturing.
RAM	Random Access Memory. Memory devices where any memory cell in a large memory array may be accessed in any order at random.
Redistribution Layer Manufacturing	The manufacturing process of fabricating additional dielectric and copper interconnect layers to redistribute the pads to new locations on a finished wafer.
Reticle	See Mask above.
RF	Radio Frequency. Radio frequency semiconductors are primarily used in communications devices such as cell phones.
ROM	Read-Only Memory. See Mask ROM above.
Scanner	An aligner that scans light through a slit across a mask to produce an image on a wafer.

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Semiconductor	An element with an electrical resistivity within the range of an insulator and a conductor. A semiconductor can conduct or block the flow of electric current depending on the direction and magnitude of applied electrical biases.
Solder bumping	The fabrication processes of forming solder bump termination electrodes, which are elevated metal structures, or lead free bump termination electrodes.
SRAM	Static Random Access Memory. A type of volatile memory product that is used in electronic systems to store data and program instructions. Unlike the more common DRAM, it does not need to be refreshed.
Stepper	A machine used in the photolithography process in making wafers. With a stepper, a small portion of the wafer is aligned with the mask upon which the circuitry design is laid out and is then exposed to strong light. The machine then steps to the next area, repeating the process until the entire wafer has been done. Exposing only a small area of a wafer at a time allows the light to be focused more strongly, which gives better resolution of the circuitry design.
System-on-chip	A chip that incorporates functions usually performed by several different devices and therefore generally offers better performance and lower cost.
Systems companies	Companies that design and manufacture complete end market products or systems for sale to the market.
Transistor	An individual circuit that can amplify or switch electric current. This is the building block of all integrated circuits.
Volatile memory	Memory products that lose their content when the power supply is switched off.
Wafer	A thin, round, flat piece of silicon that is the base of most integrated circuits.

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EXHIBIT INDEX

Exhibit 1.1	Eleventh Amended and Restated Articles of Association, as adopted at the Registrant s annual general meeting of shareholders on June 2, 2008 (1)
Exhibit 4.1	Settlement Agreement dated January 31, 2005 by and between Semiconductor Manufacturing International Corporation and Taiwan Semiconductor Manufacturing Corporation, Ltd., including Patent License Agreement (2)
Exhibit 4.2	English language summary of Chinese language Syndicate Loan Agreement dated May 26, 2005, between Semiconductor Manufacturing International (Beijing) Corporation, Semiconductor Manufacturing International Corporation, as guarantor, and China Development Bank, China Construction Bank, Bank of China, Agricultural Bank of China, China Merchants Bank, HuaXia Bank, China Mingsheng Bank, Bank of Communications, Bank of Beijing, Industrial and Commercial Bank of China (Asia) and CITIC Ka Wah Bank (2)
Exhibit 4.3	Form of Indemnification Agreement, as adopted at the Registrant s annual general meeting of shareholders on May 6, 2005(2)
Exhibit 4.4	Form of Service Contract between the Company and each of its executive officers
Exhibit 4.5	Form of Service Contract between the Company and each of its directors
Exhibit 4.6	English language summary of Chinese language Syndicate Loan Agreement dated May 31, 2006, between Semiconductor Manufacturing International (Tianjin) Corporation, Semiconductor Manufacturing International Corporation, as guarantor, and China Construction Bank, China Minsheng Bank, China Development Bank, Industrial and Commercial Bank of China, Agricultural Bank of China, Bank of China, China Merchants Bank, China Bo Hai Bank, Bank of Communications and Bangkok Bank (3)
Exhibit 4.7	English language summary of Chinese language Syndicate Loan Agreement dated June 8, 2006, between Semiconductor Manufacturing International (Shanghai) Corporation, Semiconductor Manufacturing International Corporation, as guarantor, and ABN AMRO Bank N.V., Bank of China (Hong Kong) Limited, Bank of Communications, The Bank of Tokyo-Mitsubishi UFJ, Ltd., China Construction Bank, DBS Bank Ltd., Fubon Bank (Hong Kong) Limited, Industrial and Commercial Bank of China and Shanghai Pudong Development Bank (3)
Exhibit 4.8	Share Purchase Agreement, dated November 6, 2008, by and between the Company and Datang Telecom Technology & Industry Holdings Limited Co., Ltd.(4)
Exhibit 4.9	English language translation of Strategic Cooperation Agreement, dated December 24, 2008 by and between the Company and Datang Telecom Technology & Industry Holdings Co., Ltd. (5)
Exhibit 8.1	List of Subsidiaries
Exhibit 12.1	Certification of CEO under Section 302 of the U.S. Sarbanes-Oxley Act of 2002

Exhibit 12.2	Certification of Acting CFO under Section 302 of the U.S. Sarbanes-Oxley Act of 2002
Exhibit 13.1	Certification of CEO and Acting CFO under Section 906 of the U.S. Sarbanes-Oxley Act of 2002
Exhibit 99.1	Consent of Deloitte Touche Tohmatsu

(1) Previously filed as an exhibit to the Registrant s Annual Report on Form 20F for the fiscal year ended December 31, 2007, filed June 27, 2008 and amended November 28, 2008.

(2) Previously filed as an exhibit to the Registrant s Annual Report on Form 20F for the fiscal year ended December 31, 2004, filed June 28, 2005. With respect to Exhibit 4.1, please refer to Item 8 Litigation in the Registrant s Annual Report on Form 20F for the fiscal year ended December 31, 2008.

(3) Previously filed as an exhibit to the Registrant s Annual Report on Form 20F for

the fiscal year ended December 31, 2005, filed June 28, 2006.

(4) Previously filed as an exhibit to the Registrant s Form 6-K dated November 17, 2008. Portions of this exhibit were omitted and filed separately with the Commission pursuant to Rule 24b-2 of the Securities Exchange Act of 1934, as amended, concerning confidential treatment.

(5) Previously filed as an exhibit to the Registrant s Form 6-K dated January 5, 2009. Portions of this exhibit were omitted and filed separately with the Commission pursuant to Rule 24b-2 of the Securities Exchange Act of 1934, as amended, concerning confidential treatment.