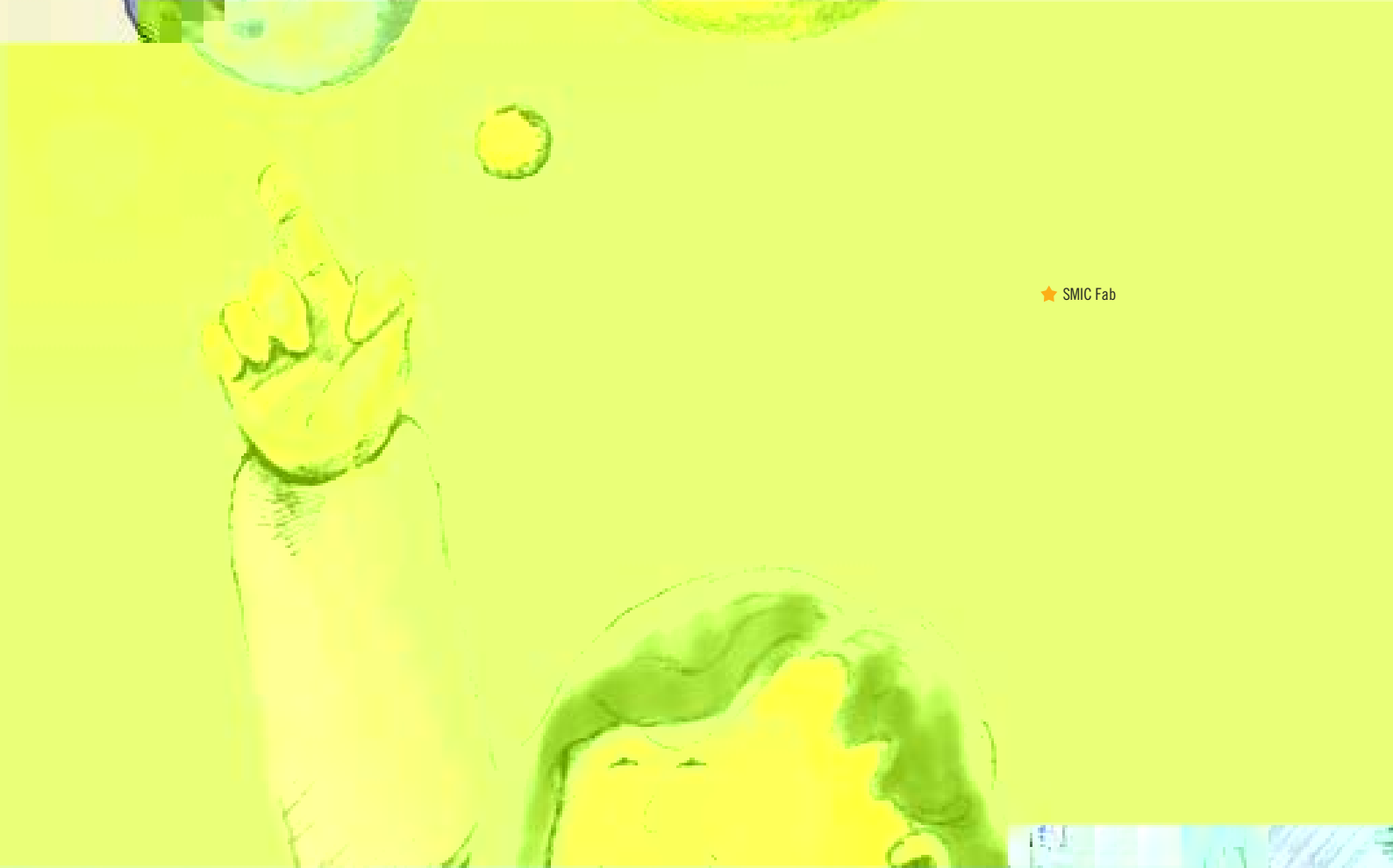


## Building Network

- Largest foundry in China and one of the top players in global IC market
- New IC production project in Shenzhen
- Comprehensive foundry network in China for capturing growth opportunities



▲ SMIC Japan



★ SMIC Fab



0.13 $\mu$ m-90nm

65nm


45nm





# Transcending Technology Boundaries

- 0.13 $\mu$ m and more advanced technologies made up 53.1% of total wafer revenue
- Roadmap was extended to 45nm technologies through licensing agreement with IBM
- Strategic agreement was signed with Spansion for 65nm NOR flash development



# 12"

## Expanding Capacity

- 300mm Shanghai fab commenced production in July 2007
- 200mm Chengdu managed fab commenced production in March 2007



# 8”

## Enhancing Ability

- 90nm reached over 25% of total wafer revenue
- Logic based products from 90nm to 65nm began pilot production, with 45nm products under development





A purple showerhead is shown at the top, spraying water droplets. On the left side, there is a large, detailed illustration of a yellow and orange leaf with visible veins. The background is white with scattered blue dots.

## Nurturing Talents and Community

- Nurture our staff with SMIC's values and devotion to excellence
- Focus on caring for the environment and creating a more sustainable society
- Help build a brighter China





**Moving Ahead** ▣



# Corporate Information

Registered name	Semiconductor Manufacturing International Corporation (the “Company”)
Chinese name (for identification purposes only)	中芯國際集成電路製造有限公司
Registered office	PO Box 309 Ugland House Grand Cayman, KY1-1104 Cayman Islands
Head office and place of business in PRC	18 Zhangjiang Road Pudong New Area Shanghai 201203 PRC
Place of business in Hong Kong registered under Part XI of the Companies Ordinance	Suite 3003 30th Floor 9 Queen’s Road Central Hong Kong
Website address	<a href="http://www.smics.com">http://www.smics.com</a>
Company secretary	Anne Wai Yui Chen
Authorized representatives	Richard Ru Gin Chang Anne Wai Yui Chen
Places of listing	The Stock Exchange of Hong Kong Limited (“HKSE”) New York Stock Exchange (“NYSE”)
Stock code	0981 (HKSE) SMI (NYSE)

## Financial Calendar

Announcement of 2007 results	April 25, 2008
Book closure peri	



# Chairman's Statement



# Chief Executive Officer's Statement



Dear Shareholders,

2007 was a challenging year for SMIC, as we faced a difficult DRAM environment and increasing global competition. However, our success in developing cutting edge technologies, converting DRAM capacity to logic, expanding capacity, and cultivating the China market, has paved the way for continued growth in 2008.

I am pleased to report that SMIC has continued to grow its revenues despite unprecedented depressed conditions in the DRAM market. Our total revenue increased by 5.8% over 2006 to \$1.55 billion in 2007. Gross profit was up by 20% to \$152.7 million in 2007 from \$127.2 million in 2006 due to solid growth in our non-DRAM business. Gross margin was 9.9% in 2007, compared to 8.7% in 2006. Operationally, our capacity at the end of the fourth quarter of 2007 increased to 185,250 8-inch-equivalent wafers per month, an 18% increase over 2006.



As the overall semiconductor market continues to expand rapidly in China, SMIC has participated in this significant growth trend, demonstrated by a 56% growth in our China sales in 2007. We are pleased to see continuous progress from our customers in China and remain committed to further growth and expansion within the China market.

In 2007, we saw strong foundry demand for handset ICs, power management ICs, WLAN, and consumer applications such as STB, DTV and MP3/MPEG4, indicative of demand in the industry at large. We also enjoyed the addition of 77 new customers worldwide in 2007, a large number of which are PRC-based, representing a 23.3% increase in our customer base.

In addition, 2007 was marked by several strategic agreements. SMIC entered into a strategic agreement with Spansion Inc. (NASDAQ:SPSN), in which Spansion will transfer its 65nm MirrorBit® technology to SMIC for foundry services on 300 mm wafers in China. This move would allow SMIC to enter selected segments of the Flash memory market with a license to manufacture and sell 90 nm and 65 nm and potentially future Spansion MirrorBit® Quad products for the China content delivery market.

To complement our ongoing in-house research and development, and to strengthen our capabilities in serving customers, we are pleased to announce that we have entered into a content delivery market



In 2007, SMIC continued to grow its business despite severe DRAM pricing erosion in the latter half of the year. The overall semiconductor market continued to expand rapidly in China, represented by a 56% growth in our China sales in 2007, thereby affirming SMIC's business strategy.

## Overview of Business Developments

Our operations continue to remain strong. At the end of 2007, we had increased our monthly capacity to 185,250 8-inch wafers per month. Our wafer shipments increased from 1,614,888 8-inch wafers in 2006 to 1,849,957 8-inch wafers in 2007, representing a 14.6% increase. According to a leading IC industry market research company, we held 8% of the foundry market in 2007, which represented a growth rate of approximately 24%, the 3rd highest growth rate among the top 10 foundries.

We generated US\$672.5 million in cash from operations in 2007. However, our depreciation expenses remain among the highest in the foundry industry. Furthermore, because we are a relatively new foundry with only six years of commercial operations and have continued to expand our capacity to meet the increasing capacity demands of our customers, our depreciation expense as a percentage of revenues remain the highest in the foundry industry.

We believe that we will become profitable by continually improving our product mix, developing leading edge technologies, and establishing key partnerships. In 2007, we entered into a licensing agreement with IBM for 45nm technology, partnered with Spansion for 65nm NOR flash development and worked to keep cost down on maturing technologies. In 2007, 53.1% of our wafer sales came from products that utilized advanced technology of 0.13 micron and below. Revenues generated from 0.13 micron and below technology nodes as a percentage of our logic revenues increased from 26.8% in 2006 to 35.7% in 2007. We expect this upward trend to continue in 2008 as some of our fabless and IDM customers continue to migrate a significant portion of their products to the 0.13 micron and below technology nodes.

## Customers and Markets

We target a diversified and global customer base, consisting of leading IDMs, fabless semiconductor companies, and systems and other companies and seek to maintain our leadership position in China.

During year 2007 the worldwide semiconductor industry went through a 3% growth despite the troubled DRAM market since the beginning of the year (according to Gartner and iSuppli sources). Semiconductors for consumer electronics growth also appeared slow and in addition to many players competing for market share, resulted in faster price erosion. SMIC increased its revenue by 5.8% while shipments increased to 14.6% compared to 2006.

Geographically, SMIC's revenue is still led by North America at 42.5%, followed by Europe at 21.2%, Asia Pacific (excluding Japan) at 26.5%, and Japan at 9.8%. Our US customers including both leading IDM and fabless IC companies, showed strong demand in broad application categories such as mobile phone base-band, WLAN (Wireless Local Area Network), Audio and Video, STB (Set-top Box) and PMU (Power Management Units) at 90nm, 130nm and 180nm technology nodes. Our customers in Taiwan showed significant growth in flash controllers and multimedia processors. In 2007, we engaged 77 new customers, bringing the total number of customers to 401. Notably our China revenue has been increasing steadily from both increased shipments and from the number of new designs using more advanced technology nodes such as 130nm and 90nm. New leaders emerged in multimedia processors, RF devices, CMOS image sensors, MP3/MP4 players, DTV/STB and new devices such as Digital Picture Frames. SMIC also has significant participation in implementing China's own standards in communications and broadcasting, such as TD-SCDMA for 3G mobile networks, DMB-T/H for DTV demodulation and CMMB for satellite based mobile TV broadcasting.

As China's largest and most advanced foundry, SMIC reached several milestones in 2007. First, SMIC signed 45nm technology licensing agreement with IBM, allowing a leap forward technology capability in first wave applications from first tier customers. Secondly, our 90nm entered mass production in Beijing's 300mm facility. Thirdly, SMIC's 300mm Fab in Shanghai (Fab 8) went into pilot production and will expand capacity for foundry services for logic-based products from 90nm down to 45nm. In addition, SMIC strengthened its role in advanced NOR flash foundry by signing a foundry agreement with Spansion in manufacturing 65nm MirrorBit® Products.

As our customer base continues to grow, our business becomes capacity constrained, in both 300mm, driven by advanced logic and flash memories, and 200mm, driven by power management, power MOSFET's, analog devices, and LCD/LED driver IC's. SMIC also successfully explored new business models in working with Chinese city or provincial governments in Chengdu and Wuhan. Under this business model, the governments funded the facilities while SMIC manages and operates them, allowing SMIC to expand our service offering for our customers. Additionally, with the support of the Shenzhen municipal government, SMIC plans to begin wafer production operations and research development activities that will introduce advanced process technology licensed from IBM. On the DRAM side, due to the persistent low prices starting at the beginning of 2007, SMIC has decided to reduce DRAM foundry production level aggressively and start converting DRAM fab equipment for logic products.

In summary, during 2007 SMIC continued to demonstrate healthy growth in revenue and in its customer base, a strong influence in China, and a broadened service spectrum by a planned conversion of DRAM capacity into logic production which allowed SMIC to restructure its capacity mix and position itself toward improved profitability and risk diversification in 2008.



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# Management's Discussion and Analysis of Financial Condition and Results of Operation



## Consolidated Financial Data

The summary consolidated financial data presented below as of and for the years ended December 31, 2005, 2006 and 2007 are derived from, and should be read in conjunction with, and are qualified in their entirety by reference to, the audited consolidated financial statements, including the related notes, included elsewhere in this Annual Report. The selected consolidated financial data as of December 31, 2003 and 2004 and for the two years then ended is derived from audited consolidated financial statements not included in this Annual Report. The summary consolidated financial data presented below has been prepared in accordance with United States generally accepted accounting principles (the "U.S. GAAP").

























# Directors and Senior Management

Members of the Board who served during 2007 were:

Yang Yuan Wang (Chairman of the Board and Independent Non-executive Director);  
Richard Ru Gin Chang (Executive Director, President and Chief Executive Officer of the Company);  
Fang Yao (ex Non-executive Director who resigned as of August 30, 2007);  
Wang Zheng Gang (Non-executive Director who was appointed as of August 30, 2007);  
Ta-Lin Hsu (Independent Non-executive Director);  
Tsuyoshi Kawanishi (Independent Non-executive Director);  
Henry Shaw (Independent Non-executive Director);  
Lip-Bu Tan (Independent Non-executive Director);  
Albert Y. C. Yu (Independent Non-executive Director); and  
Jiang Shang Zhou (Independent Non-executive Director).

## Re-election of Class I and Class III Directors

Shareholders are invited to re-elect Class I Directors at the 2008 annual general meeting of the Company's shareholders (the "2008 AGM") to fill the vacancies available due to the retirements of the Directors mentioned below.

Three Class I Directors, Richard Ru Gin Chang, Henry Shaw and Albert Y. C. Yu, whose initial appointments as Directors took effect on April 3, 2000, September 25, 2001 (in respect of Richard Ru Gin Chang and Henry Shaw who were re-appointed as Directors and designated as Class I Directors on March 18, 2004 and at the annual general meeting of shareholders held on May 6, 2005) and May 30, 2006 (in respect of Albert Y. C. Yu), respectively, will retire from office at the 2008 AGM pursuant to Article 90 of the Company's Articles of Association. Each of Dr. Chang and Mr. Shaw will offer himself for re-election as a Class I Director. If re-elected, each of Dr. Chang and Mr. Shaw would hold office until the 2011 annual general meeting of the Company.

One Class III Director, Wang Zheng Gang, whose initial appointment as a Director took effect on August 30, 2007, will retire from office at the AGM pursuant to Article 126 of the Articles of Association of the Company. Mr. Wang will offer himself for re-election as a Class III Director. If re-elected, Mr. Wang would hold office until the 2010 annual general meeting of the Company.

Details of the proposed candidates for re-election as Directors at the 2008 AGM are set out in the circular to the shareholders sent together with this annual report.















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# Corporate Governance Report

The Company is committed to remaining an exemplary corporate citizen and maintaining a high level of corporate governance in order to protect the interests of its shareholders.

## Corporate Governance Practices

The HKSE's Code on Corporate Governance Practices (the "CG Code") as set out in Appendix 14 of the Listing Rules, which contains code provisions to which an issuer such as the Company, are expected to comply or advise as to reasons for deviations (the "Code Provisions") and recommended best practices to which an issuer is encouraged to comply (the "Recommended Practices"). At the meeting of the Board on January 25, 2005, the Board approved the Corporate Governance Policy (the "CG Policy") with effect from such date. The updated CG Policy, a copy of which can be obtained on the Company's website at [www.smics.com](http://www.smics.com) under "Corporate Governance", incorporates all of the Code Provisions of the CG Code and many of the Recommended Practices.

In addition, the Company has adopted or put in place various policies, procedures, and practices in compliance with the provision of the CG Policy. None of the Directors is aware of any information which would reasonably indicate that the Company is not, or was not, during the financial period from January 1, 2007 to December 31, 2007, in compliance with the CG Policy.

## Model Code for Securities Transactions by Directors of Listed Issuers

The Company has adopted an Insider Trading Compliance Program (the "Insider Trading Policy") which encompasses the requirements of the Model Code as set out in Appendix 10 of the Listing Rules. The Company, having made specific enquiry of all Directors, confirms that all members of the Board have complied with the Insider Trading Policy and the Model Code throughout the year ended December 31, 2007. The senior management as well as all officers, Directors, and employees of the Company and its subsidiaries are also required to comply with the provisions of the Insider Trading Policy.

## The Board

The Board has a duty to the Company's shareholders to direct and oversee the affairs of the Company in order to maximize shareholder value. The Board acting itself and through the various committees of the Board, actively participates in and is responsible for the determination of the overall strategy of the Company, the establishment and monitoring of the achievement, of corporate goals and objectives, the oversight of the Company's financial performance and the preparation of the accounts, the establishment of corporate governance practices and policies, and the review of the Company's system of internal controls. The management of the Company is responsible for the implementation of the overall strategy of the Company and its daily operations and administration. The Board has access to the senior management of the Company to discuss enquiries on management information.

The Board consists of nine Directors as at the date of the annual report. 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 the Company's outstanding shares being entitled to vote in person or by proxy at such meeting. The Board is divided into three classes with no more than one class eligible for re-election at any annual general meeting of shareholders.

Each class of Director will serve terms of three years. The Class I Directors were re-elected for a term of three years at the 2005 AGM (except Dr. Albert Y. C. Yu who was elected at the 2006 AGM) and are eligible for re-election at the 2008 AGM for a term of three years. The Class II Directors were re-elected for a term of three years at the 2006 AGM (except Mr. Jiang Shang Zhou who was elected at the 2008 AGM). The Class III Directors (except Mr. Wang Zheng Gang who was appointed as a Director by the Board on August 30, 2007 and is eligible for re-election at the 2008 AGM to hold office until 2010 AGM) were re-elected at the 2007 AGM for a term of three years.

The following table sets forth the names, classes and categories of the Directors:

Name of Director	Category of Director	Class of Director
Yang Yuan Wang	Chairman, Independent Non-executive Director	Class III
Richard Ru Gin Chang	President, Chief Executive Officer, Executive Director	Class I
Henry Shaw	Independent Non-executive Director	Class I
Albert Y. C. Yu	Independent Non-executive Director	Class I
Ta-Lin Hsu	Independent Non-executive Director	Class II
Jiang Shang Zhou	Independent Non-executive Director	Class II
Lip-Bu Tan	Independent Non-executive Director	Class II
Tsuyoshi Kawanishi	Independent Non-executive Director	Class III
Wang Zheng Gang	Non-executive Director	Class III

Brief biographical details for Board members are set out on pages 38 through 41. During the year ended December 31, 2007, the Board at all times exceeded the minimum requirements of the Listing Rules relating to the appointment of at least three Independent Non-executive Directors on the board, and complied with the requirement that these should include one such director with appropriate professional qualifications or accounting or related financial management expertise. The roles of the chairman and chief executive officer are segregated and such roles are exercised by Prof. Yang Yuan Wang and Dr. Richard Ru Gin Chang, respectively.



During the year ended December 31, 2007, the Board held a total of nine (9) meetings. Details of Directors' attendance at the Board meetings for the period of their appointments are set forth below:

	Number of Meetings Attended	Attendance Rate
<b>From January to August, 2007</b>		
Wang Yang Yuan	7/7	100%
Richard Ru Gin Chang	7/7	100%
Fang Yao <sup>(1)</sup>	6/7	86%
Ta-Lin Hsu	7/7	100%
Jiang Shang Zhou <sup>(2a)</sup>	6/7	86%
Tsuyoshi Kawanishi <sup>(3a)</sup>	5/7	72%
Henry Shaw	7/7	100%
Lip-Bu Tan	7/7	100%
Albert Y. C. Yu <sup>(4a)</sup>	5/7	72%
Average Attendance Rate		91%
<b>From September to December, 2007</b>		
Wang Yang Yuan	2/2	100%
Richard Ru Gin Chang	2/2	100%
Wang Zheng Gang <sup>(5)</sup>	2/2	100%
Ta-Lin Hsu	2/2	100%
Jiang Shang Zhou <sup>(2b)</sup>	2/2	100%
Tsuyoshi Kawanishi <sup>(3b)</sup>	2/2	100%
Henry Shaw	2/2	100%
Lip-Bu Tan	2/2	100%
Albert Y. C. Yu <sup>(4b)</sup>	2/2	100%
Average Attendance Rate		100%

<sup>(1)</sup> Mr. Yao resigned as Non-executive Director on August 30, 2007

<sup>(2a)</sup> 4 of these meetings were attended by proxy

<sup>(2b)</sup> 1 of these meetings was attended by proxy

<sup>(3a)</sup> 3 of these meetings were attended by proxy

<sup>(3b)</sup> 1 of these meetings was attended by proxy

<sup>(4a)</sup> 2 of these meetings were attended by proxy

<sup>(4a)</sup> 1 of these meetings was attended by proxy

<sup>(5)</sup> Mr. Wang Zheng Gang was appointed as Non-executive Director on August 30, 2007





In 2007, the Compensation Committee reviewed the total compensation package for Richard Ru Gin Chang, who is the President and Chief Executive Officer of the Company and an Executive Director. The Compensation Committee awarded Richard Ru Gin Chang an annual salary of US\$157,477. In 2006, the Compensation Committee reviewed and approved the total compensation package for Richard Ru Gin Chang, who is the President and Chief Executive Officer of the Company and an Executive Director, as well as that of the other members of the management team of the Company. Based on the Compensation Committee's review of the Company's corporate goals for 2006 and comparable total compensation packages for presidents and chief executive officers of other publicly-listed companies in the same or a similar industry, the Compensation Committee awarded Richard Ru Gin Chang an annual salary of US\$155,076. In 2005, the Compensation Committee granted Dr. Chang fifteen million (15,000,000) options to purchase ordinary shares under the 2004 Stock Option Plan and awarded him two million (2,000,000) RSUs under the 2004 Equity Incentive Plan. As of December 31, 2007, none of such options have been exercised and 50% of such RSUs have vested.

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. 50% of these options were vested on May 30, 2007, the remaining 50% will be vested on May 30, 2008. These options will expire as to 50% on the earlier of September 29, 2016 or 120 days after termination of the director's service to the Board. Mr. Fang Yao (who resigned as Non-executive Director on August 30, 2007) and Mr. Jiang Shang Zhou have declined such option.

On September 29, 2006, the Board granted to Dr. Albert Y. C. Yu 500,000 Restricted Share Units. 50% of such Restricted Share Units automatically vested on May 30, 2007 and the remaining 50% of such Restricted Share Units will be vested on May 30, 2008.

On November 10, 2004, the Board granted to each independent Non-executive Director and Non-executive Director, an option to purchase 500,000 ordinary shares at a price per ordinary share of US\$0.22. These options were fully vested on March 19, 2005 and will expire on November 9, 2009. As of December 31, 2007, these options have not been exercised. Lai Xing Cai (who resigned as an Non-executive Director on February 6, 2006) has declined such option. The option granted to Mr.



- reviewing any legal matters that may have a material impact and the adequacy and effectiveness of the Company's legal and regulatory compliance procedures;
- establishing procedures for the treatment of complaints received by the Company regarding accounting, internal accounting controls, auditing matters, potential violations of law and questionable accounting or auditing matters; and
- obtaining and reviewing reports from management, the Company's internal auditor and the Company's independent auditor regarding compliance with applicable legal and regulatory requirements.

During 2007, the Audit Committee reviewed:

- the financial reports for the year ended December 31, 2006 and the six month period ended June 30, 2007;
- the quarterly earnings releases and any updates thereto;
- the report and management letter submitted by the Company's outside auditors summarizing the findings of and recommendations from their audit of the Company's financial reports;
- the Company's budget for 2007;
- the findings and recommendations of the Company's outside consultants regarding the Company's compliance with the requirements of the Sarbanes-Oxley Act of 2002 (the "Sarbanes-Oxley Act");
- the effectiveness of the Company's internal control structure in operations, 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 the Company's Risk Management Committee (as defined and discussed below) which assesses risks relating to the Company and the compliance office, which ensures compliance with the CG Code and Insider Trading Policy;
- the audit fees and other non-audit fees such as fees relating to transfer pricing, Sarbanes-Oxley compliance testing, for the Company's outside auditors; and
- the Company's outside auditors' engagement letters.

The Audit Committee reports its work, findings and recommendations to the Board during each Board meeting.

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 meeting schedule for a year is planned in the preceding year. The Company Secretary assists the co-chairmen of the Audit Committee in preparing the agenda for meetings and assists the Compensation Committee in complying with the relevant rules and regulations. The relevant papers for the Audit Committee meetings were dispatched to the Audit Committee in accordance with the CG Code. 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 a subsequent Audit Committee meeting.



## Internal Controls

In June 2004, the Public Company Accounting Oversight Board, or PCAOB, adopted rules for purposes of implementing Section 404 of the Sarbanes-Oxley Act. Pursuant to the Sarbanes-Oxley Act and the various rules and regulations adopted pursuant thereto or in conjunction therewith, the Company is required to perform, on an annual basis, an evaluation of the Company's internal control over financial reporting and, beginning in fiscal year 2006, to include management's assessment of the effectiveness of the Company's internal control over financial reporting in the Company's annual report on Form 20-F to be filed with the United States Securities and Exchange Commission. Beginning in fiscal year 2006, the Company's external auditors are required to attest to such assessment.

The Board, through the Audit Committee which receives reports on at least a quarterly basis from the Internal Audit Department, is responsible to ensure that the Company maintains sound and effective internal controls. The Company's system of internal control is designed to ensure the achievement of business objectives in operations, financial reporting integrity and compliance with applicable laws and regulations. The system of internal control is designed to manage, rather than completely eliminate, risks impacting the Company's ability to achieve its business objectives. Accordingly, the system can only provide reasonable but not absolute assurance that the financial statements do not contain a material misstatement or loss.

The Company assists the Board with respect to its duty to identify, evaluate, and manage the significant risks faced by the Company. The Company implements the Board's policies and procedures to mitigate such risks by (i) identifying and assessing the risks the Company faces and (ii) designing, operating and monitoring a system of internal controls to mitigate and control such risks. The Company has established an Internal Audit Department and the Risk Management Committee and other policies and procedures, for such purposes.

The Board, through the Audit Committee, has reviewed the effecti is a mater

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## Disclosure Committee

The Disclosure Committee oversees all information disseminated by the Company, including regulatory filings and submissions made pursuant to the Exchange Act or the Listing Rules, being properly recorded, processed, summarized, and reported to the management of the Company to allow timely decisions regarding the required disclosure. Accordingly, the Disclosure Committee has established a disclosure policy and procedure, which establishes the procedures for the handling and disseminating of price-sensitive information.

With respect to the Company's periodic filings pursuant to the Exchange Act or the Listing Rules, the Disclosure Committee identifies and communicates the extent and nature of all disclosures to be made in such filings, reviews the filings, with a particular focus on "Management's Discussion and Analysis of Financial Conditions and Results of Operations"; reviews and discusses with the Chief Financial Officer whether the Company's filings provide a fair representation of the Company's financial condition, results of operation, and cash flows, assesses the materiality of specific events and developments to the Company; and reviews financial reporting issues that are significant to the Company and other material reporting matters.

The Disclosure Committee consists of members of the Company's management team, including two executive officers of the Company.

## Compliance Office

The Compliance Office monitors the Company's compliance under applicable corporate governance laws and regulations. In particular, the Compliance Office monitors and implements the Company's anti-fraud policy and investigates any reported cases of breach; and monitors the Company's compliance with the Code of Business Conduct and Ethics (as described and defined below) and the Insider Trading Policy. The anti-fraud policy sets forth the Company's policy regarding the prevention, detection and management of fraud and fair dealing in matters pertaining to fraud. The Company has established an email address for the Compliance Officers and the Audit Committee, dedicated to respond to any allegations of fraud and breaches of the Code of Business Conduct and Ethics or the Insider Trading Policy of the Company. The Code of Business Conduct and Ethics provides employees with guidelines pertaining to proper behavior in the workplace and appropriate representation of the Company when outside the workplace. The Insider Trading Policy sets forth the policy and procedures governing the dealing in the Company's securities by employees, including the Chief Executive Officer and members of the Company's management, and members of the Board (and their associates).

On at least a quarterly basis, the Compliance Office will report to the Audit Committee regarding any breaches of any of these policies.

The Compliance Office consists of members of the Company's management team, including an executive officer of the Company.





A key element of effective communication with shareholders and investors is the timely dissemination of information relating to the Company. In addition to announcing annual and interim reports, the Company announces its quarterly financial results approximately one month after the end of each quarter. In connection with such announcement, the Company holds conference calls which are open and available to the Company's shareholders. During these conference calls, the President and Chief Executive Officer and the Acting Chief Financial Officer report about the latest developments in the Company and answer questions from participants. The members of the Company's Investor Relations Department and senior members of the Company's management also hold regular meetings with equity research analysts and other institutional shareholders and investors.

In addition to the 2007 AGM and the above referenced conference calls, the Company's shareholders were invited to a gathering in Hong Kong to meet members of the management of the Company.

A table setting forth information regarding the beneficial ownership as of December 31, 2007 of the ordinary shares, of each shareholder who is known by the Company to beneficially own more than 5% of the Company's outstanding shares, is contained on page 53.

The market capitalization of the Company as of December 31, 2007 was HK\$15,218,314,163.8 (issued share capital of 18,558,919,712 ordinary shares at the closing market price of HK\$0.82 per ordinary share). The public float as of such date was approximately 88.55%.

The AGM is scheduled to be held at the Company's headquarters at 18 Zhangjiang Road, PuDong New Area, Shanghai 201203, China on June 2, 2008 at 3:00 p.m. All shareholders are invited to attend.

## Code of Business Conduct and Ethics

The Board has adopted a code of business conduct and ethics (the "Code of Conduct") which provides guidance about doing business with integrity and professionalism. The Code of Conduct addresses issues including among others, fraud, conflicts of interest, corporate opportunities, protection of intellectual property, transactions in the Company's securities, use of the Company's assets, and relationships with customers and third parties. Any violation of the Code of Conduct is reported to the Compliance Office, which will subsequently report such violation to the Audit Committee.

### US Corporate Governance Practices

Companies listed on the New York Stock Exchange must comply with certain corporate governance standards under Section 303A of the New York Stock Exchange Listed Company Manual. However, foreign private issuers such as the Company are permitted to follow home country practices in lieu of the provisions of Section 303A, except that such companies are required to comply with the rules relating to the audit committee. Please refer to the following website at <http://www.smics.com/website/enVersion/IR/corporateGovernance.htm> for a summary of the significant differences between the Company's corporate governance practices and those required of U.S. companies under New York Stock Exchange listing standards.

# Social Responsibility

SMIC strives to recycle, reduce, and reuse energy and materials utilized in our manufacturing facilities and offices. Our manufacturing plants feature state of the art water recycling systems, which recycle and reuse wastewater in a multitude of ways. The wastewater treatment plants at every SMIC fab recycles up to 70 percent of the wastewater back into the fab. The rest of the wastewater is reused in office toilets and sprinkler systems. At SMIC's Beijing fab, large rain water collection facilities and air cooling systems take advantage of the cold winter air to help cool the manufacturing facilities. In all office buildings, recycling bins are strategically located near bathrooms, walkways, and cafeterias to promote employee participation in recycling waste materials.

SMIC's core belief in renewable energy is embedded directly in the future direction of our business as evidenced by our Fab 10 that is used to manufacture solar cell panels and modules. We believe that not only will the solar power market be beneficial to our business, but more importantly, we believe that we can contribute in aiding the migration to renewable energy sources through technological advances, increase in manufacturing capacity, and reduction of manufacturing costs.

## Employee Well-Being

At SMIC, we focus on quality control and product innovation while placing emphasis on preventing environmental pollution, conserving energy and natural resources, protecting our human resources, and preventing property loss. We hope to improve employee well-being, protect the environment, and raise environmental protection, safety, and health ("ESH") standards for all SMIC employees and the environment we operate in. Through continuous improvement, we strive to be environmentally responsible and aim to strengthen our operational risk management.

To achieve these goals, SMIC is committed to:

- ensuring employee health and safety and improving environmental quality for employees and lands we operate are the primary responsibilities of every SMIC manager;
- establishing a culture of ownership by instilling ESH values into each SMIC employee, process, product, and service;
- providing regular ESH training to increase employees' knowledge and communication levels;
- exploring and developing new technologies to reclaim, reduce, reuse and recycle;
- following ESH regulations and international protocols while fulfilling customer requirements;
- strengthening new equipment and material auditing and change-management;
- communicating ESH regulations to all SMIC suppliers and contractors; and
- implementing preventative measures and emergency response capabilities to prevent accidents.



# Report by Management on Internal Control over Financial Reporting

The management of Semiconductor Manufacturing International Corporation ("SMIC") is responsible for establishing and maintaining adequate internal control over financial reporting. SMIC's internal control system was designed to provide reasonable assurance to our management and board of directors regarding the reliability of financial reporting and the preparation and fair presentation of financial statements issued for external purposes in accordance with generally accepted accounting principles.

All internal control systems, no matter how well designed, have inherent limitations and may not prevent or detect misstatements. Therefore, even those systems determined to be effective can only provide reasonable assurance with respect to financial reporting reliability and financial statement preparation and presentation.

SMIC management assessed the effectiveness of internal control over financial reporting as of December 31, 2007. In making this assessment, we used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO criteria) in *Internal Control – Integrated Framework*. Based on our assessment we believe that, as of December 31, 2007, our internal control over financial reporting is effective based on the COSO criteria.

SMIC's independent registered public accounting firm, Deloitte Touche Tohmatsu, has issued an audit report on our internal control over financial reporting, which immediately follows this report.

April 25, 2008

# Report of Independent Registered Public Accounting Firm

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# Consolidated Balance Sheets

(In US dollars, except share data)





## Consolidated Balance Sheets

(In US dollars, except share data)

	NOTES	December 31,		
		2007	2006	2005
Long-term liabilities:				
Promissory notes	14	51,057,163	77,601,657	103,254,436
Long-term debt	15	616,294,743	719,570,905	494,556,385
Long-term payables relating to license agreements	16	62,833,433	16,992,950	24,686,398
Other long term liabilities		—	3,333,333	—
Deferred tax liabilities	17	604,770	210,913	—
<b>Total long-term liabilities</b>		<b>730,790,109</b>	<b>817,709,758</b>	<b>622,497,219</b>
<b>Total liabilities</b>		<b>1,660,980,229</b>	<b>1,495,071,574</b>	<b>1,518,535,344</b>
Commitments	21			
Minority interest		34,944,408	38,800,666	38,781,863
Stockholders' equity:				
Ordinary shares, \$0.0004 par value, 50,000,000,000 shares authorized; 18,558,919,712, 18,432,756,463 and 18,301,680,867 shares issued and outstanding at December 31, 2007, 2006 and 2005, respectively		7,423,568	7,373,103	7,320,673
Additional paid-in capital		3,313,375,972	3,288,765,465	3,291,439,835
Accumulated other comprehensive (loss) income		(1,881)	91,840	138,978
Deferred share-based compensation		—	—	(24,881,919)
Accumulated deficit		(308,278,637)	(288,810,490)	(244,701,412)
<b>Total stockholders' equity</b>		<b>3,012,519,022</b>	<b>3,007,419,918</b>	<b>3,029,316,155</b>
<b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY</b>		<b>\$ 4,708,443,659</b>	<b>\$ 4,541,292,158</b>	<b>\$ 4,586,633,362</b>
Net current assets		\$ 145,111,502	\$ 372,304,679	\$ 151,426,762
<b>Total assets less current liabilities</b>		<b>\$ 3,778,253,539</b>	<b>\$ 3,863,930,342</b>	<b>\$ 3,690,595,237</b>

The accompanying notes are an integral part of these consolidated financial statements.

# Consolidated Statements of Operations

(In US dollars, except share data)

	NOTES	Year ended December 31,		
		2007	2006	2005
Sales	23	\$ 1,549,765,288	\$ 1,465,322,867	\$ 1,171,318,735
Cost of sales		1,397,037,881	1,338,155,004	1,105,133,544
Gross profit		152,727,407	127,167,863	66,185,191
Operating expenses (income):				
Research and development		97,034,208	94,170,750	78,865,306
General and administrative		74,489,877	47,364,533	35,700,768
Selling and marketing		18,715,961	18,231,048	17,713,228
Amortization of acquired intangible assets		27,070,617	24,393,561	20,946,051
Income from sale of plant and equipment and other fixed assets	10	(28,651,446)	(43,121,929)	—
Total operating expenses (income), net		188,659,217	141,037,963	153,225,353
Loss from operations	27	(35,931,810)	(13,870,100)	(87,040,162)
Other income (expense):				
Interest income		12,348,630	14,916,323	11,355,972
Interest expense		(37,936,126)	(50,926,084)	(38,784,323)
Foreign currency exchange gain (loss)		11,249,889	(21,912,234)	(3,355,279)
Others, net		2,237,902	1,821,337	4,461,925
Total other expense, net		(12,099,705)	(56,100,658)	(26,321,705)
Loss before income tax		(48,031,515)	(69,970,758)	(113,361,867)
Income tax benefit (expense)	17	29,719,775	24,927,744	(284,867)
Minority interest		2,856,258	(18,803)	251,017
Loss from equity investment	12	(4,012,665)	(4,201,247)	(1,379,110)
Net loss before cumulative effect of a change in accounting principle		(19,468,147)	(49,263,064)	(114,774,827)
Cumulative effect of a change in accounting principle	2	—	5,153,986	—
Net loss		(19,468,147)	(44,109,078)	(114,774,827)
On the basis of net loss before accounting change per share, basic and diluted	19	\$ (0.00)	\$ (0.00)	\$ (0.01)
Cumulative effect of an accounting change per share, basic and diluted	19	\$ —	\$ 0.00	\$ —
Loss per share, basic and diluted	19	\$ (0.00)	\$ (0.00)	\$ (0.01)
Shares used in calculating basic and diluted loss per share	19	18,501,940,489	18,334,498,923	18,184,429,255

The accompanying notes are an integral part of these consolidated financial statements.

# Consolidated Statements of Stockholders' Equity And Comprehensive Income (Loss)

(In US dollars, except share data)

	Share	Ordinary Amount	Additional paid-in capital	Notes receivable from stockholder	Accumulated other comprehensive income (loss)	Deferred stock compensation, net	Accumulated deficit	Total stockholders equity	Comprehensive income (loss)
Balance at December 31, 2004	18,232,179,139	7,292,872	3,289,757,272	(391,375)	387,776	(51,177,675)	(129,926,585)	3,115,942,285	\$ 96,391,145
Net profit of a subsidiary attributable to minority interest upon injection	—	—	(32,880)	—	—	—	—	(32,880)	
Exercise of stock options	75,617,262	30,247	2,371,933	—	—	—	—	2,402,180	
Repurchase of restricted ordinary shares	(6,115,534)	(2,446)	(96,583)	—	—	—	—	(99,029)	
Collection of note receivables from employees	—	—	—	391,375	—	—	—	391,375	
Deferred stock compensation, net	—	—	(559,907)	—	—	26,295,756	—	25,735,849	
Net loss	—	—	—	—	—	—	(114,774,827)	(114,774,827)	\$ (114,774,827)
Foreign currency translation adjustments	—	—	—	—	(192,246)	—	—	(192,246)	(192,246)
Unrealized loss on investments	—	—	—	—	(56,552)	—	—	(56,552)	(56,552)
Balance at December 31, 2005	18,301,680,867	\$ 7,320,673	\$ 3,291,439,835	\$ —	\$ 138,978	\$ (24,881,919)	\$ (244,701,412)	\$ 3,029,316,155	\$ (115,023,625)
Exercise of stock options	132,744,596	53,098	3,912,210	—	—	—	—	3,965,308	
Repurchase of restricted ordinary shares	(1,669,000)	(668)	(57,522)	—	—	—	—	(58,190)	
Deferred stock compensation adjustment	—	—	(24,881,919)	—	—	24,881,919	—	—	
Share-based compensation	—	—	23,506,847	—	—	—	—	23,506,847	
Cumulative effect of a change in accounting principle	—	—	(5,153,986)	—	—	—	—	(5,153,986)	

# Consolidated Statements of Cash Flows

(In US dollars)

	Year ended December 31,		
	2007	2006	2005
Operating activities:			
Loss attributable to holders of ordinary shares	\$ (19,468,147)	\$ (44,109,078)	\$ (114,774,827)
Less: Cumulative effect of a change in accounting principle	—	(5,153,986)	—
Net loss	(19,468,147)	(49,263,064)	(114,774,827)
Adjustments to reconcile net loss to net cash provided by operating activities:			
Minority interest	(2,856,258)	18,803	(251,017)
Deferred taxes	(31,234,415)	(25,075,987)	—
Gain on sale of plant and equipment and assets held for sale	(28,651,446)	(43,121,929)	(3,001,881)
Depreciation and amortization	706,277,464	919,616,493	769,471,853
Non-cash interest expense on promissory note and long-term payable relating to license agreements	4,762,343	5,702,607	5,395,177
Amortization of acquired intangible assets	27,070,616	24,393,561	20,946,051
Share-based compensation	20,643,341	23,506,847	25,735,849
Loss from equity investment	4,012,665	4,201,247	1,379,110
Changes in operating assets and liabilities:			
Accounts receivable, net	(46,202,677)	(10,851,061)	(72,145,627)
Inventories	26,869,187	(83,941,316)	(47,219,784)
Prepaid expense and other current assets	(9,339,779)	(8,926,442)	(5,172,942)
Accounts payable	19,852,824	24,705,615	26,425,817
Accrued expenses and other current liabilities	2,982,369	(14,722,249)	41,469,028
Income tax payable	1,080,213	72,417	(152,000)
Other long term liabilities	(3,333,333)	3,333,333	—
Net cash provided by operating activities	672,464,967	769,648,875	648,104,807
Investing activities:			
Purchase of plant and equipment			

# Consolidated Statements of Cash Flows

(In US dollars)



# Notes to the Consolidated Financial Statements

## 1. Organization and Principal Activities

Semiconductor Manufacturing International Corporation was incorporated under the laws of the Cayman Islands on April 3, 2000 and its subsidiaries as of December 31, 2007 include the following:

Name of company	Place and date of incorporation/ establishment	Attributable equity interest held	Principal activity
Garrison Consultants Limited ("Garrison")	Samoa April 5, 2000	100%	Provision of consultancy services
Better Way Enterprises Limited ("Better Way")	Samoa April 5, 2000	100%	Provision of marketing related activities
Semiconductor Manufacturing International (Shanghai) Corporation ("SMIS")*#	The People's Republic of China (the "PRC") December 21, 2000	100%	Manufacturing and trading of semiconductor products
SMIC, Americas	United States of America June 22, 2001	100%	Provision of marketing related activities
Semiconductor Manufacturing International (Beijing) Corporation ("SMIB")*	The PRC July 25, 2002	100%	Manufacturing and trading of semiconductor products
SMIC Japan Corporation#	Japan October 8, 2002	100%	Provision of marketing related activities
SMIC Europe S.R.L	Italy July 3, 2003	100%	Provision of marketing related activities
SMIC Commercial (Shanghai) Limited Company (formerly SMIC Consulting Corporation)*	The PRC September 30, 2003	100%	Operation of a convenience store
Semiconductor Manufacturing International (Tianjin) Corporation ("SMIT")*#	The 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")*	The PRC August 16, 2004	57.3%	Manufacturing and trading of semiconductor products
Semiconductor Manufacturing International (Solar Cell) Corporation ("Solar Cell")	Cayman Islands June 30, 2005	100%	Investment holding

## 1. Organization and Principal Activities *(Continued)*

Name of company	Place and date of incorporation/ establishment	Attributable equity interest held	Principal activity
SMIC Energy Technology (Shanghai) Corporation ("Energy Science")*#	The PRC September 9, 2005	100%	Manufacturing and trading of solar cell related semiconductor products
SMIC Development (Chengdu) Corporation*#	The 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 ("SMIC (BVI)")	British Virgin Islands April 26, 2007	100%	Investment holding
SMIC Solar Cell (HK) Company Limited (formerly known as "Regent Century Limited") ("SMIC Solar Cell (HK)")	Hong Kong October 23, 2007	100%	Investment holding
SMIC AT (HK) Company Limited (formerly known as "Brilliant Ford Limited") ("SMIC AT (HK)")	Hong Kong October 22, 2007	57.3%	Investment holding
SMIC Shanghai (HK) Company Limited (formerly known as "Hill Wealth Limited") ("SMIC SH (HK)")	Hong Kong November 1, 2007	100%	Investment holding
SMIC Beijing (HK) Company Limited (formerly known as "Best Harvest Holdings Limited") ("SMIC BJ (HK)")	Hong Kong November 2, 2007	100%	Investment holding
SMIC Tianjin (HK) Company Limited (formerly known as "Wisdom Faith Limited") ("SMIC TJ (HK)")	Hong Kong November 2, 2007	100%	Investment holding





## 2. Summary of Significant Accounting Policies *(Continued)*

### (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) Investments

Short-term investments consisting primarily of debt instruments, mutual funds, corporate notes and corporate bonds are classified either as held to maturity, available for sale or trading securities.

Held to maturity securities have been recorded at amortized cost.

Available for sale securities have been recorded at fair market value. Unrealized gains and losses are recorded as accumulated other comprehensive income (loss). Unrealized losses, which are deemed other than temporary, are recorded in the statement of operations as other expenses. The unrealized gains and losses are reclassified to earnings once the available-for-sale investments are settled.

Trading securities are recorded at fair value with unrealized gains and losses classified in earnings.

### (f) 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 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.

### (g) Inventories

Inventories are stated at the lower of cost (weighted average) or market. Cost comprises direct materials and where applicable, direct labors costs and those overheads that have been 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 2007, 2006 and 2005, inventory was written down by \$22,676,608, \$16,106,471 and \$13,808,698, respectively, to reflect the lower of cost or market.

### (h) 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 term of the agreements, which range from 50 to 70 years.

## Notes to the Consolidated Financial Statements



## 2. Summary of Significant Accounting Policies *(Continued)*

### (l) Revenue recognition *(Continued)*

The Company was contracted to provide 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 collection is reasonably assured.

### (m) 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. Capitalized interest of \$7,697,890, \$4,798,002 and \$7,617,123, in 2007, 2006 and 2005, respectively, has been added to the cost of the underlying assets during the respective year. Net interest expense is as follows:

	For the year ended December 31		
	2007	2006	2005
Total actual interest expense	\$ 72,686,950	\$ 78,120,699	\$ 50,392,052
Less: Government subsidy	27,083,604	22,396,613	3,990,606
Less: Capitalized interest	7,667,220	4,798,002	7,617,123
Net interest expense	\$ 37,936,126	\$ 50,926,084	\$ 38,784,323

### (n) Government subsidies

The Company receives government subsidies in the following five forms:

#### (1) Reimbursement of certain interest costs incurred on borrowings

The Company received government cash subsidies of \$27,083,604, \$13,878,353 and \$12,390,652 in 2007, 2006 and 2005, respectively, which were calculated based on the interest expense on the Company's budgeted borrowings. The Company recorded, on an accrual basis, government subsidies as a reduction of interest expense.

#### (2) Value added tax refunds

The Company received subsidies of nil, \$82,960 and \$3,747,951 in 2007, 2006 and 2005, respectively, for value added taxes paid by the Company in respect of export sales of semiconductor products. The value added tax refunds have been recorded as a reduction of the cost of sales.

#### (3) Sales tax refunds

The Company received sales tax refunds of nil, \$97,079 and \$609,461 in 2007, 2006 and 2005, respectively, which were recorded as an offset of sales tax expense, a component of the general and administrative expenses.

## Notes to the Consolidated Financial Statements



## 2. Summary of Significant Accounting Policies *(Continued)*

### (r) 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 upon the weight of available evidence, it is more likely than not that some or all of the deferred tax assets will not be realized.

Effective 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. The adoption of FIN 48 did not have any material impact on the Company's financial position or results of operations.

### (s) Comprehensive income (loss)

Comprehensive income (loss) includes such items as net loss, foreign currency translation adjustments and unrealized gains (loss) on available-for-sales securities. Comprehensive income (loss) is reported in the statements of stockholders' equity and comprehensive income (loss).

### (t) Fair value of financial instruments

Financial instruments include cash and cash equivalents, short-term investments, short-term borrowings, promissory note, long-term payables relating to license agreements, long-term debt, accounts payables, accounts receivables and receivables for sale of equipments. The carrying values of cash and cash equivalents, short-term investments and short-term borrowings approximate their fair values based on quoted market values or due to their short-term maturities. The carrying value of long-term promissory notes and payables relating to license agreements exceeded its fair value by approximately \$1,026,000 as of December 31, 2007. The carrying value of long-term debt approximates its fair value due to variable interest rates that approximate market rates.

## Notes to the Consolidated Financial Statements



## 2. Summary of Significant Accounting Policies *(Continued)*

### (v) 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 recognition of gains or losses resulting from changes in the values of those derivative instruments is based on the use of each derivative instrument and whether it qualifies for hedge accounting.

### (w) Recently issued accounting standards

In September 2006, the Financial Accounting Standard Board ("FASB") issued Statement of Financial Accounting Standards No. 157, "Fair Value Measurements" ("SFAS 157"), which defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. SFAS 157 applies under most other accounting pronouncements that require or permit fair value measurements and does not require any new fair value measurements. This statement is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years, with earlier application encouraged. The provisions of SFAS 157 should be applied prospectively as of the beginning of the fiscal year in which the statement is initially applied, except for a limited form of retrospective application for certain financial instruments. The adoption of SFAS 157 will not have a material impact on the Company's consolidated financial position or results of operations.

In February 2007, the FASB issued Statement No. 159, "Fair Value Option for Financial Assets and Financial Liabilities – including an amendment of FASB Statement No. 115" ("SFAS 159"). SFAS 159 permits companies to measure certain financial instruments and certain other items at fair value. The standard requires that unrealized gains and losses on items for which the fair value option has been elected be reported in earnings. SFAS 159 is effective for the Company on January 1, 2008, as earlier adoption was not elected. The Company does not expect the adoption of SFAS 159 to have a material impact on the Company's consolidated financial position or results of operations.

In December 2007, the FASB issued Statement No. 141 (revised 2007) "Business Combinations" ("SFAS 141(R)"). SFAS 141(R) retains the fundamental requirements of the original pronouncement requiring that the purchase method be used for all business combinations. SFAS 141(R) defines the acquirer as the entity that obtains control of one or more businesses in the business combination, establishes the acquisition date as the date that the acquirer achieves control and requires the acquirer to recognize the assets acquired, liabilities assumed and any non-controlling interest at their fair values as of the acquisition date. SFAS 141(R) also requires that acquisition-related costs be recognized separately from the acquisition. SFAS 141(R) is applicable to the Company's business combinations, if any, occurring after January 1, 2009. SFAS 141(R) has no impact on previously consummated business combinations. The Company is currently evaluating the impact, if any, of the statement on its consolidated financial statements.

In December 2007, the FASB issued Statement No. 160 "Non-controlling Interests in Consolidated Financial Statements, an amendment of ARB 51" ("SFAS 160"). SFAS 160 requires non-controlling interests in subsidiaries initially to be measured at fair value and classified as a separate component of equity. SFAS 160 also requires that when a parent company acquires control of a subsidiary, it must include 100% of the fair value of all the acquired company's assets and liabilities in its consolidated financial statements. SFAS 160 is effective for us on January 1, 2009. SFAS 160 is to be applied prospectively to business combinations; certain disclosure and presentation requirements are to be applied retrospectively upon adoption. The Company is currently evaluating the impact, if any, of the statement on its consolidated financial statements.

## Notes to the Consolidated Financial Statements





#### 4. Accounts Receivable, Net of Allowances *(Continued)*

The change in the allowance for doubtful accounts is as follows:

	2007	2006	2005
Balance, beginning of year	\$ 4,048,845	\$ 1,091,340	\$ 1,105,165
Provision of the year	486,920	2,957,505	(13,825)
Write-offs in the year	(43,675)	—	—
Balance, end of year	\$ 4,492,090	\$ 4,048,845	\$ 1,091,340

#### 5. Short-term Investments

##### Held-to-maturity security

December 31, 2007				
	Amortized Cost	Gross unrealized gains	Gross unrealized losses	Fair value
Debt instruments	\$ 7,637,870	\$ —	\$ —	\$ 7,637,870

##### Available-for-sale security

The following is a summary of short-term available-for-sale listed securities:

December 31, 2006				
	Cost	Gross unrealized gains	Gross unrealized losses	Fair value
Mutual fund	\$ 52,866,825	\$ —	\$ —	\$ 52,866,825

December 31, 2005				
	Cost	Gross unrealized gains	Gross unrealized losses	Fair value
Commercial paper	\$ 3,482,033	\$ 9,450	\$ —	\$ 3,491,483
Mutual fund	10,283,573	20,803	—	10,304,376
	\$ 13,765,606	\$ 30,253	\$ —	\$ 13,795,859

## Notes to the Consolidated Financial Statements



## 6. Derivative Financial Instruments *(Continued)*

In 2006 and 2005, 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 and 2005, gains or losses on the interest rate swap contracts were recognized in the statement of operations. As of December 31, 2006 and 2005, the Company had outstanding interest rate swap contracts with notional amounts of \$250,000,000 and \$340,000,000, respectively.

In addition to the abovementioned interest rate swap contracts, in 2007 and 2006, the Company entered into a cross-currency interest rate swap agreement 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 agreement does not qualify for hedge accounting. In 2007 and 2006, gains or losses on the interest rate swap contracts were recognized in the statement of operations. As of December 31, 2007 and 2006, the Company had outstanding cross-currency interest rate swap contracts with notional amounts of \$51,057,531 and \$15,947,874, respectively.

The fair values of each derivative instrument are as follows:

	December 31		
	2007	2006	2005
Forward foreign exchange contracts	\$ 530,354	\$ (2,694,415)	\$ (2,607,714)
Interest rate swap contracts	1,003,275	(5,317,837)	(1,270,811)
	\$ 1,533,629	\$ (8,012,252)	\$ (3,878,525)

As of December 31, 2007, the fair value of the derivative instruments was recorded in prepaid expense and other current assets, and as of December 31, 2006 and 2005, the fair value of these derivative instruments was recorded in accrued expenses and other current liabilities, with the change in fair value of forward foreign exchange contracts recorded as part of other income (expense) and the change in fair value of interest rate swap contract and cross currency interest rate swap contracts recorded as part of interest expense.

## Notes to the Consolidated Financial Statements





## Notes to the Consolidated Financial Statements



### 13. Accounts Payable

An aging analysis of the accounts payable is as follows:

	2007	2006	2005
Current	\$ 223,527,856	\$ 238,864,239	\$ 209,142,167
Overdue:			
Within 30 days	46,571,502	43,364,820	22,479,945
Between 31 to 60 days	10,226,533	9,594,873	4,593,542
Over 60 days	21,666,848	17,305,267	26,102,778
	\$ 301,992,739	\$ 309,129,199	\$ 262,318,432

### 14. Promissory Note

In 2005, the Company reached a settlement and license agreement with TSMC as detailed in Note 24. 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 has been recorded as a reduction of the face amounts of the promissory notes. The Company repaid \$30,000,000 and \$30,000,000 in 2007 and 2006 respectively. The outstanding promissory notes are as follows:

Maturity	December 31, 2007	
	Face value	Discounted value
2008	\$ 30,000,000	\$ 29,242,001
2009	30,000,000	28,259,668
2010	25,000,000	22,797,495
	85,000,000	80,299,164
Less: Current portion of promissory notes	30,000,000	29,242,001
Long-term portion of promissory notes	\$ 55,000,000	\$ 51,057,163

In 2007, 2006 and 2005, the Company recorded interest expense of \$3,455,506, \$4,347,221 and \$4,527,146 respectively, relating to the amortization of the discount.

## Notes to the Consolidated Financial Statements







## Notes to the Consolidated Financial Statements



## 15. Indebtedness *(Continued)*

### (b) Long-term debt *(Continued)*

#### *EUR syndicate loan*

On December 15, 2005, the Company entered into the EUR syndicate loan, a long-term loan facility agreement in the aggregate principal amount of EUR 85 million with a syndicate of banks and ABN Amro Bank N.V. Commerz Bank (Nederland) N.V. as the leading bank. 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) 26 months after the effective 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 2007 and 2006, SMIS and SMIT had drawn down EUR 28,390,000 (\$41,863,894), and EUR 15,122,775 (\$19,934,841), respectively. SMIS and SMIT repaid an aggregated amount of EUR 5,863,555 (\$8,173,357), and EUR 3,024,555 (\$3,986,968) in 2007 and 2006, respectively. As of December 31, 2007 and 2006, the outstanding balance was EUR 34,624,665 (\$51,057,531) and EUR 12,098,220 (\$15,947,873). In 2007, the interest rate loan ranged from 3.95% to 5.87%. The interest expense incurred in 2007 and 2006 was \$996,706 and \$279,908, of which \$82,036 and \$65,072 were capitalized as additions to assets under construction in 2007 and 2006, respectively.

The total outstanding balance of the facility is collateralized by certain plant and equipment at the original cost of EUR 17.8 million for SMIT and EUR 33.4 million for SMIS as of December 31, 2007.

#### *Tianjin USD syndicate loan*

In May 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 fabs. In 2007, SMIT had drawn down \$12,000,000 from this loan facility. The principal amount is repayable starting from starting from 2010 in six semi-annual installments. In 2007, the interest rate range on the loan ranged from 6.03% to 6.58%. The interest expense incurred in 2007 was \$285,253, of which \$24,344 was capitalized as additions to assets under construction in 2007.

The total outstanding balance of the facility is collateralized by certain plant and equipment with an original cost of \$207.0 million as of December 31, 2007.

The long-term debt arrangements contain financial covenants as defined in the loan agreements and also set out in the section entitled "Management Discussion and Analysis" of this annual report.

## Notes to the Consolidated Financial Statements





## Notes to the Consolidated Financial Statements



## 17. Income Taxes *(Continued)*

Details of deferred tax assets and liabilities are as follows:

	2007	2006	2005
Deferred tax assets:			
Allowances and reserves	\$ —	\$ 1,962,410	\$ 1,682,244
Start-up costs	53,698	958,105	1,844,170
Net operating loss carry forwards	—	5,201,545	5,172,687
Unrealized exchange loss	—	47,860	295,646
Depreciation of fixed assets	75,886,896	33,715,867	—
Subsidy on long lived assets	479,817	295,654	—
Accrued sales return	—	137,719	23,764
<b>Total deferred tax assets</b>	<b>76,420,411</b>	<b>42,319,160</b>	<b>9,018,511</b>
Valuation allowance	(19,505,239)	(17,032,260)	(8,905,021)
<b>Net deferred tax assets – non-current</b>	<b>\$ 56,915,172</b>	<b>\$ 25,286,900</b>	<b>\$ 113,490</b>
Deferred tax liability:			
Capitalized interest	(604,770)	(210,913)	(113,490)

The Company adopted the provisions of FIN 48 effective January 1, 2007. Based on its FIN 48 analysis documentation, the Company has made its assessment of the level of tax authority for each tax position (including the potential application of interest and penalties) based on the technical merits. The adoption of FIN 48 did not have any impact on the Company total liabilities or shareholders' equity. The Company has no material uncertain tax positions as of December 31, 2007 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, 2007, 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.

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 \$19.0 million and \$8.4 million to reduce the deferred tax asset of \$75.9 million and \$33.7 million to the amount that is more-likely-than-not to be realized as of December 31, 2007 and 2006, respectively. Accordingly, an income tax benefit of US\$31.6 million and \$25.3 million was recorded in 2007 and 2006. The deferred tax asset recognized relates specially to one of the Company's subsidiaries on the basis that this subsidiary has achieved profitability consistently since 2004 and is expected to continue to be profitable based on the current forecast.

## Notes to the Consolidated Financial Statements





## 18. 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 completion of the IPO, the Company began issuing 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, 2007, options to purchase 655,089,237 ordinary shares were outstanding, and options to purchase 661,227,253 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 plans, options are generally granted at prices equal to the fair market value as estimated by the Board of Directors, 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, 2007, options to purchase 387,309,245 ordinary shares were outstanding.

A summary of the stock option activity is as follows:

	Ordinary shares		Weighted Average Remaining Contractual Term	Aggregated Intrinsic Value
	Number of Options	Weighted Average Exercise Price		
Options outstanding at December 31, 2006	998,025,093	\$0.14		
Granted	223,112,000	\$0.13		
Exercised	(82,947,298)	\$0.05		
Cancelled	(95,791,313)	\$0.17		
Options outstanding at December 31, 2007	1,042,398,482	\$0.14	5.17	38,481,747
Vested or expected to vest at December 31, 2007	836,646,879	\$0.14	5.42	31,863,984
Exercisable at December 31, 2007	514,657,338	\$0.13	5.75	35,801,843

## Notes to the Consolidated Financial Statements



Notes to the Consolidated Financial Statements



## 19. Reconciliation of Basic and Diluted Loss per Share *(Continued)*

The following table sets forth the securities comprising of these anti-dilutive ordinary share equivalents for the years indicated:

	December 31,		
	2007	2006	2005
Outstanding options			
to purchase ordinary shares	72,685,282	62,339,207	177,325,981
Outstanding unvested restricted share units			
to purchase ordinary shares	75,302,939	161,479,670	129,093,152
	147,988,221	223,818,877	306,419,133

## 20. Transactions With Managed Government-Owned Foundries

The Company provides management services to Cension Semiconductor Manufacturing Corporation (“Cension”) and Wuhan Xinxin Semiconductor Manufacturing Corporation, which are government-owned foundries. Management service revenues under these arrangements for 2007, 2006 and 2005 were \$42,000,000, \$4,151,238 and \$200,000, respectively.

In 2007, the Company sold plant, equipment and other fixed assets with a carrying value of \$19,530,909 for \$42,300,258 to Cension, which resulted in a gain on sale of \$22,769,349. In 2006, the Company sold plant, equipment and other fixed assets with a carrying value of \$19,411,553 for \$61,182,652 to Cension, which resulted in a gain on sale of \$41,771,099.

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 will receive a guarantee fee from Cension based on 1.5% of the guarantee amount, or \$2.4 million. Some 200mm wafer processing equipment purchased under the Agreement, with the total amount of \$160 million, was held as collateral under the guarantee. As of December 31, 2007, the carrying amount of the liability related to the guarantee was approximately \$2.4 million, which was presented in other current liabilities.

Of the \$320 million of processing equipment (“Equipment”), a portion remained in Hiroshima and continues to be operated by Elpida. 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 when the equipment acquired by Cension is relocated from Hiroshima to Chengdu.

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 roughly half of the Equipment from Cension for approximately US\$150 million. These equipment will be used for SMIC’s future expansion.

## 21. Commitments

### (a) Purchase commitments

As of December 31, 2007 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, 2008.

Facility construction	\$	57,080,000
Machinery and equipment		239,555,000
	\$	296,635,000

### (b) Royalties

The Company has entered into several license and technology agreements with third parties. The terms of the contracts range from three to ten years. The Company is subject to royalty payments based on a certain percentage of product sales, using the third parties' technology or license. In 2007, 2006 and 2005, the Company incurred royalty expense of \$13,118,570, \$7,724,704 and \$8,710,935, respectively, which is included as part of cost of sales in the statement of operations.

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 2007, 2006 and 2005, the Company earned royalty income of \$1,428,603, \$1,384,137 and \$705,217, respectively, which was included as part of other income in the statement of operations.

### (c) Operating leases

The Company owns apartment facilities that are leased to the Company's employees at negotiated prices. The apartment rental agreement i

## 22. 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.

	2007	2006	2005
Total sales:			
United States	\$ 657,603,189	\$ 602,506,213	\$ 478,162,160
Europe	328,710,235	440,327,872	316,576,024
Asia Pacific (Excluding Japan and Taiwan)	227,973,648	168,607,598	175,846,284
Taiwan	183,113,880	153,057,616	138,153,755
Japan	152,364,336	100,823,568	62,580,512
	\$ 1,549,765,288	\$ 1,465,322,867	\$ 1,171,318,735

Revenue is attributed to countries based on headquarter of operations.

Substantially all of the Company's long-lived assets are located in the PRC.

## 23. Significant Customers

The following table summarizes net revenue and accounts receivable for customers which accounted for 10% or more of our accounts receivable and net sales:

	Net revenue Year ended December 31,			Accounts receivable December 31,		
	2007	2006	2005	2007	2006	2005
A	18%	28%	26%	15%	29%	32%
B	16%	17%	15%	14%	14%	17%
C	8%	2%	0%	13%	7%	0%

## 24. 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 31, 2005, the Company entered into a settlement agreement, without admission of liability, which provided for the dismissal of all pending legal actions without prejudice between the two companies (the “Settlement Agreement”). The terms of the Settlement Agreement also included:

- 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 .15 $\mu$ m and larger processes subject to certain conditions (“TSMC Covenant”). The TSMC Covenant did not cover .13 $\mu$ m and smaller technologies after 6 months following execution of the Settlement Agreement (July 31, 2005). Excluding the .13 $\mu$ m 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 .13 $\mu$ m 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.

### 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.

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 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.



## 24. Litigation *(Continued)*

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.

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.

## 24. Litigation *(Continued)*

### Recent TSMC Legal Developments:

On August 25, 2006, TSMC filed a lawsuit against the Company and certain subsidiaries (SMIC (Shanghai), SMIC (Beijing) and SMIC (Americas)) in the Superior Court of the State of California, County of Alameda for alleged breach of the 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 the 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, nor has it set a trial date.

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, 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.

TSMC filed with the California court in January 2007 a motion seeking to enjoin the PRC action. In February 2007, TSMC filed with the Beijing High Court a jurisdictional objection, challenging the competency of the Beijing High Court's jurisdiction over the PRC action.

In March 2007, the California Court denied TSMC's motion to enjoin the PRC action. TSMC has appealed this ruling to California Court of Appeal. On March 11, 2008, the Court of Appeal, in a written opinion, denied TSMC's appeal. TSMC has not yet indicated whether it will petition the California Supreme Court for further review.

In July 2007, the Beijing High Court denied TSMC's jurisdictional objection and issued a court order holding that the Beijing High Court shall have proper jurisdiction to try the PRC action. TSMC has appealed this order to the Supreme Court of the People's Republic of China. On January 7, 2008, the Supreme Court heard TSMC's appeal. It has not yet issued a ruling.

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 attempted to file additional claims that the Company breached the Settlement Agreement by filing an action in the Beijing High Court. Upon the Company's motion, the California Court struck TSMC's new claims as procedurally improper, but granted TSMC leave to replead its claims. The Company thereafter demurred to the new claims as repleaded. The Court sustained a portion of the Company's demurrer, but again gave TSMC leave to replead.

## 24. Litigation *(Continued)*

### **Recent TSMC Legal Developments:** *(Continued)*

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.

On January 25, 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 will oppose the motion. A hearing has been set on the motion for May 14, 2008.

On March 11, 2008, TSMC filed an application for a right to attach order in the California Court. By its application, TSMC seeks an order securing an amount equal to the remaining balance on the promissory notes issued by the Company in connection with the Settlement Agreement. The order, if granted, would apply only to property of the Company in the State of California. The Company has opposed the application. A hearing was held on April 3, 2008. The court has not yet issued a ruling.

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 preliminary 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 preliminary stages, the Company is unable to evaluate the likelihood of an unfavorable outcome or to estimate the amount or range of potential loss.

## 25. Retirement y stages, the Company ii

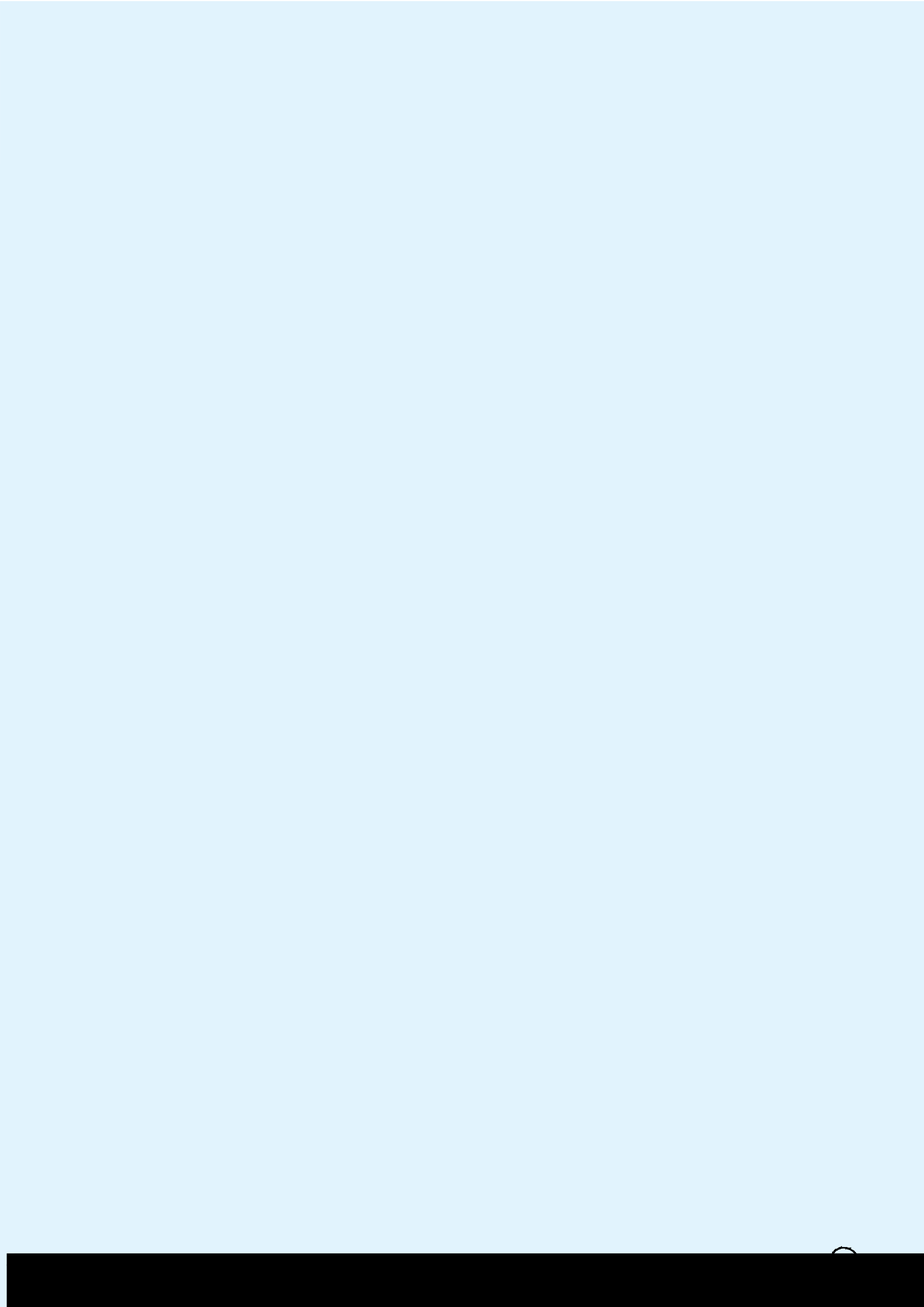
## 26. Distribution of Profits

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 \$15,640,153, \$11,956,185, and \$10,432,239 in 2007, 2006 and 2005, respectively.

## 27. Components of loss (income) from operations

	2007	2006	2005
Loss (income) from operations is arrived at after charging (crediting):			
Auditors' remuneration	\$ 1,698,293	\$ 1,577,928	\$ 1,121,131
Depreciation and amortization	705,391,171	919,038,915	768,586,770
Amortization of land use rights	886,293	577,578	885,083
Foreign currency exchange loss (gain)	3,117,962	3,939,745	(5,198,253)
(Income) loss on sale of plant and equipment	(28,651,446)	(43,121,929)	—
(Reversal of) bad debt expense	486,920	2,957,505	(13,825)
Inventory write-down	6,570,137	2,297,773	3,088,238
Staff costs inclusive of directors' remuneration	\$ 151,447,470	\$ 108,742,094	\$ 102,163,244



## 28. Directors' Remuneration and Five Highest Paid Individuals *(Continued)*

In 2007, 2006 and 2005, 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 2005, one director has declined an option to purchase 500,000 Ordinary Shares which the Board granted in November 2004. In 2006, two directors have declined an option to purchase 500,000 Ordinary Shares for each director which the Board granted in September 2006.

### 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 2007, 2006 and 2005 are as follows:

	2007	2006	2005
Salaries and other benefits	\$ 586,065	\$ 518,198	\$ 513,570
Bonus	237,969	233,662	92,455
Stock option benefits	283,125	268,528	325,880
Total emoluments	\$ 1,107,159	\$ 1,020,388	\$ 931,905

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:

	2007	2006	2005
	Number of individuals	Number of individuals	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)	—	—	—
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)	4	1	1
HK\$2,500,001 (\$321,550) to HK\$4,500,000 (\$578,790)	1	1	1
HK\$4,500,001 (\$578,790) to HK\$5,000,000 (643,100)	—	—	—

## 29. Dividend

No dividend has been paid or declared by the Company in 2007, 2006 and 2005.

### 30. Subsequent Events

During the first quarter of 2008, the Company took the decision to exit the commodity DRAM business. The Company considers this an indicator of impairment in regard to the long-lived assets of SMIB in accordance with SFAS 144. The Company is in the process of evaluating whether or not such assets have been impaired. As of December 31, 2007, the carrying value of the total property, plant and equipment at SMIB amounted to approximately \$1.2 billion.

### 31. Differences 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.

Under US GAAP, prior to the adoption of the SFAS 123(R), the Company was able to account for stock-based compensation issued to employees using one of the two following methods,

- (a) Intrinsic value based method

Under the intrinsic value based 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.

- (b) Fair value based method

For stock options, fair value is determined using an option pricing model that takes into account the stock price at the grant date, the exercise price, the expected life of the option and the annual rate of quarterly dividends.

Under either approach compensation expense, if any, is recognized over the applicable service period, which is usually the vesting period.

The Company adopted the intrinsic value method of accounting for its stock options to employees in 2005 and the share-based compensation recorded by the Company was \$25,735,849. Compensation expense under the fair value based method is presented for disclosure purposes (See Note 2(u)).

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 based method for the years prior to January 1, 2006. The additional share-based compensation under the fair value based method was \$7,261,778 for year ended December 31, 2005.

### 31. Differences Between US GAAP And International Financial Reporting Standards *(Continued)*

Effective January 1, 2006, the Company adopted the provision 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 share-based compensation related to unvested share options in stockholder's equity, consistent with IFRS 2.

- (ii) Under IFRS, minority interest is presented in the equity section while under US GAAP minority interest is presented outside of equity, between liabilities and equity.

Under IFRS, the portion of profit and loss attributable to the minority interest and to the parent entity is separately disclosed on the face of the income statement. Under US GAAP, amounts attributable to the minority interest are presented as a component of net income or loss.

- (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 is 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.

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.



### 31. Differences Between US GAAP And International Financial Reporting Standards *(Continued)*

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 are in excess of the carrying amount of the relevant long-lived assets and no impairment loss is required to be recognized under US GAAP. However, under IFRS, the estimated recoverable value derived from a discounted expected future cash flow is less than the carrying value of those long-lived assets. Discount rate of 8.3% has been used on the expected cash flows to be generated over the remaining useful lives of manufacturing machinery and equipment of 5.25 years. As such, the Company has recognized an impairment loss of US\$105,774,000 for the year ended December 31, 2007 under IFRS.

- (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).

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.

	2007	2006	2005
Net loss under US GAAP	\$ (19,468,147)	\$ (44,109,078)	\$ (114,774,827)
IFRS adjustments:			
i) Recognizing an expense for share-based payment	—	—	(7,261,778)
i) Reverse of cumulative effect of a change in accounting principle	—	(5,153,986)	—
v) Impairment of long-lived assets	(105,774,000)	—	—
vi) Presentation of minority interest	(2,856,258)	18,803	(251,017)
Net loss under IFRS	\$ (128,098,405)	\$ (49,244,261)	\$ (122,287,622)
Net loss per share under IFRS	\$ (0.01)	\$ (0.00)	\$ (0.01)
Stockholders' equity as reported under US GAAP	\$ 3,012,519,022	\$ 3,007,419,918	\$ 3,029,316,155
ii) Presentation of minority interest	34,944,408	38,800,666	38,781,863
v) Impairment of long-lived assets	(105,774,000)	—	—
Stockholders' equity under IFRS	\$ 2,941,689,430	\$ 3,046,220,584	\$ 3,068,098,018
Land use rights, net – current portion as reported under US GAAP	\$ —	—	—
IFRS adjustment			
iv) Current portion adjustment for land use right	1,054,777	712,521	650,581
Under IFRS	\$ 1,054,777	\$ 712,521	\$ 650,581

### 31. Differences Between US GAAP And International Financial Reporting Standards *(Continued)*

	2007	2006	2005
Plant and equipment			
As reported	\$ 3,202,957,665	3,244,400,822	3,285,631,131
IFRS adjustments			
iv) Impairment of long-lived assets	(105,774,000)	—	—
Under IFRS	\$ 3,097,183,665	\$ 3,244,400,822	\$ 3,285,631,131
Additional paid-in capital			
as reported under US GAAP	3,313,375,972	3,288,733,078	3,291,407,448
IFRS adjustments			
i) Reverse the deferred stock compensation, net under APB25	—	—	(24,881,919)
i) Retrospective adjustment on adoption of IFRS 2	30,388,316	30,388,316	23,126,538
i) Additional share-based compensation under IFRS 2	—	—	7,261,778
i) Reverse of cumulative effect of a change in accounting principle	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	\$ 3,292,962,223	\$ 3,268,319,329	\$ 3,240,957,794
Deferred stock compensation, net			
as reported under US GAAP	—	—	(24,881,919)
IFRS adjustments			
i) Deferred stock compensation, net under APB 25	—	—	24,881,919
Under IFRS	\$ —	\$ —	\$ —
Accumulated deficit			
as reported under US GAAP	(308,278,637)	(288,810,490)	(244,701,412)
IFRS adjustments			
i) Additional share-based compensation under IFRS 2	—	—	(7,261,778)
i) Carried over impact under IFRS 2	(30,388,316)	(30,388,316)	(23,126,538)
i) Reverse of cumulative effect of a change in accounting principle	(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)	—	—
Under IFRS	\$ (393,638,888)	\$ (268,396,741)	\$ (219,133,677)
Cost of sales			
as reported under US GAAP	1,397,037,881	1,338,155,004	1,105,133,544
IFRS adjustments			
i) Recognizing an expense for share-based payment	—	—	3,366,722
Under IFRS	\$ 1,397,037,881	\$ 1,338,155,004	\$ 1,108,500,266

### 31. Differences Between US GAAP And International Financial Reporting Standards *(Continued)*

	2007	2006	2005
Operating expenses			
as reported under US GAAP	188,659,217	141,037,963	153,225,353
IFRS adjustments			
i) Recognizing an expense for share-based payment	—	—	3,895,056
v) Impairment of long-lived assets	105,774,000	—	—
Under IFRS	\$ 294,433,217	\$ 141,037,963	\$ 157,120,409
Income (Loss) before tax			
as reported under US GAAP	(48,031,515)	(69,970,758)	(113,361,867)
IFRS adjustments			
vi) Presentation of income (loss) from equity investment	(4,012,665)	(4,201,247)	(1,379,110)
Under IFRS	\$ (52,044,180)	\$ (74,172,005)	\$ (114,740,977)

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 2007, 2006 and 2005, 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

## 31. Differences Between US GAAP And International Financial Reporting Standards *(Continued)*

### (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 policies used for internal reporting purposes that are not necessarily consistent with the accounting policies used in consolidated financial statements.

## 31. Differences Between US GAAP And International Financial Reporting Standards *(Continued)*

### (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.

The general requirement to write off expenditure on research and development as incurred is extended to research and development acquired in a business combination.

## 31. Differences Between US GAAP And International Financial Reporting Standards *(Continued)*

### (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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