The Subsidiary Committee may permit any Incentive Stock Option to convert into a Non-Qualified Stock Option as of a Participant's termination of employment for purposes of providing such Participant with the benefit of any extended exercise period applicable to Non-Qualified Stock Options when the contract of employment of the holder of Incentive Stock Option terminates.

( ) C a C a

The Subsidiary Committee must seek the prior approval of the Board of Directors of the Company and may, subject to such prior approval by the Board of Directors of the Company, specify at or after the date of grant of a Stock Option the effect that a Change in Control (as defined in the Subsidiary Plan) will have on such Stock Option. The Subsidiary Committee may also, subject to such prior approval by the Board of Directors of the Company, in contemplation of a Change in Control, accelerate the vesting, exercisability or payment of Stock Options to a date prior to the Change in Control, if the Subsidiary Committee determines that such action is necessary or advisable to allow the participants to realise fully the value of their share options in connection with such Change in Control.

( ) C a a a C a

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

( ) P S b a P a

The form of the Subsidiary Plan shall be approved by the shareholders of the Company and of the relevant subsidiary respectively, and shall become effective upon its approval by the Subsidiary Board in accordance with the terms thereof. Each Subsidiary Plan shall remain in force for a period of ten years commencing on the date of Subsidiary Board approval of the relevant Subsidiary Plan.

( ) A a T a

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

The Subsidiary Board may, subject to prior approval by the Board of Directors of the Company, at any time and from time to time make such changes, alterations or amendments to the Subsidiary Plan as may be necessary or desirable, including (without limitation) changes, alterations or amendments:

(i) relating to local legal, regulatory and/or taxation requirements and/or implications applicable to the relevant subsidiary and/or Eligible Participants; and/or

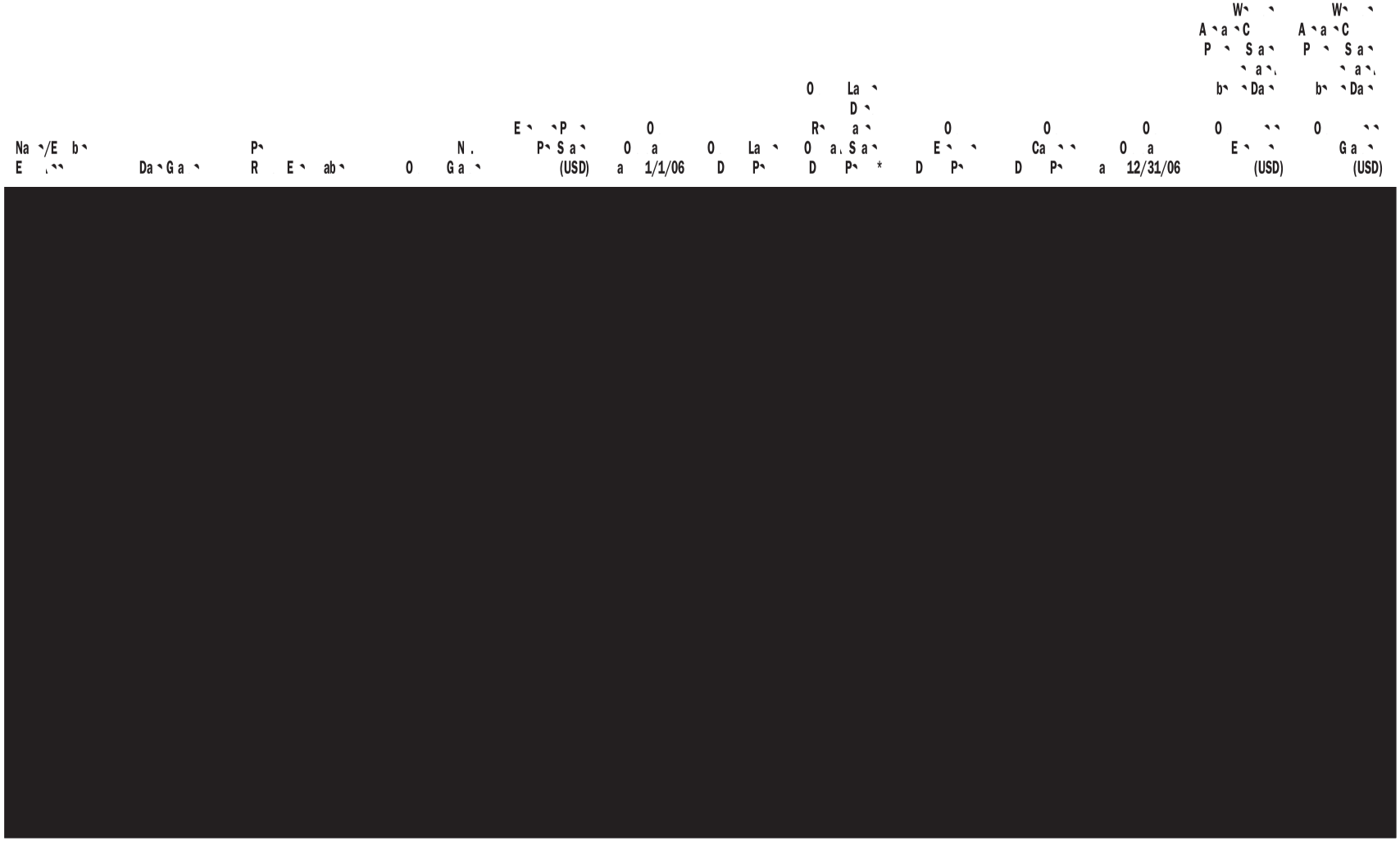
(ii) for the purposes of clarification, improvement or facilitation of the interpretation, and/or application of the terms of the Subsidiary Plan and/or for the purposes of improving or facilitating the administration of the Subsidiary Plan, and other changes, alterations or amendments of a similar nature.

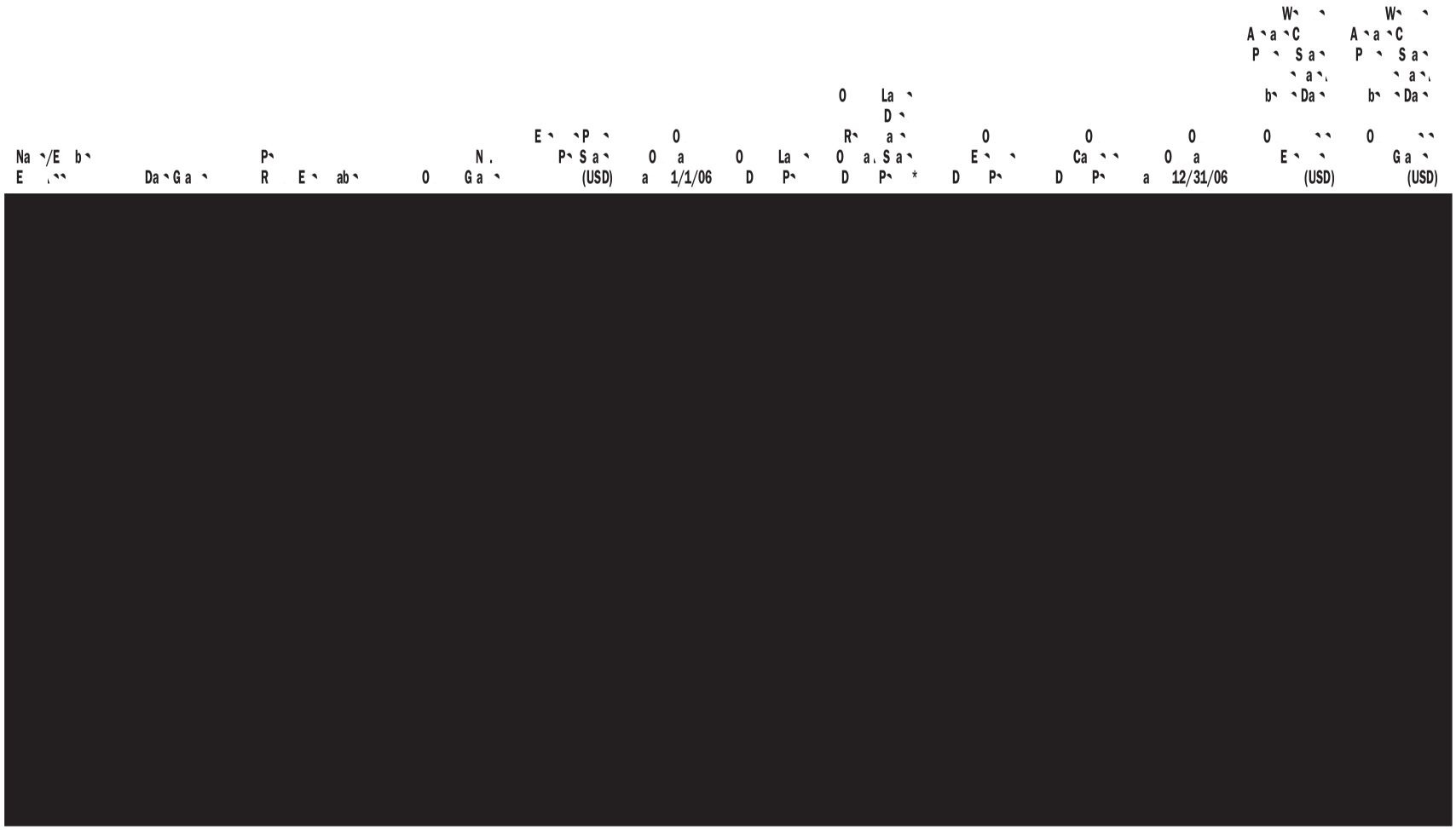
If the Subsidiary Plan is terminated early by the Subsidiary Board, subject to prior approval by the Board of Directors of the Company, no further Stock Options may be offered but unless otherwise stated in the Subsidiary Plan, Stock Options granted before such termination shall continue to be valid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

Outstanding Share Options

Details of the Stock Option Plans and the Stock Option Plan are as follows:

2001 S O P a

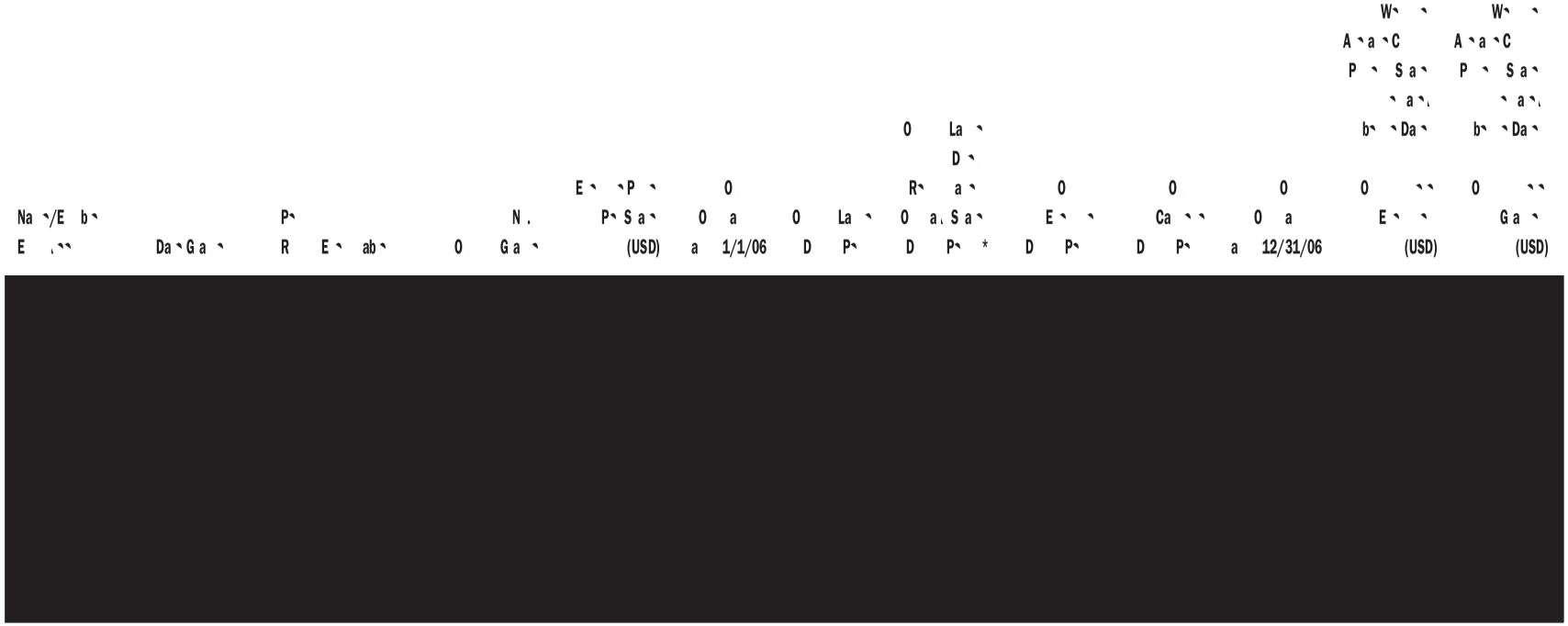




Options to purchase ordinary shares issued to new employees generally vest at a rate of 10% upon the second anniversary, an additional 20% on the third anniversary and an additional 70% upon the fourth anniversary of the vesting commencement date. Beginning in January 2004, options to purchase ordinary shares issued to then-existing employees generally vest at a rate of 25% upon the first, second, third, and fourth anniversaries of the vesting commencement date.

The Company has not issued stock options under the 2001 Stock Option Plans since the completion of the Global Offering.

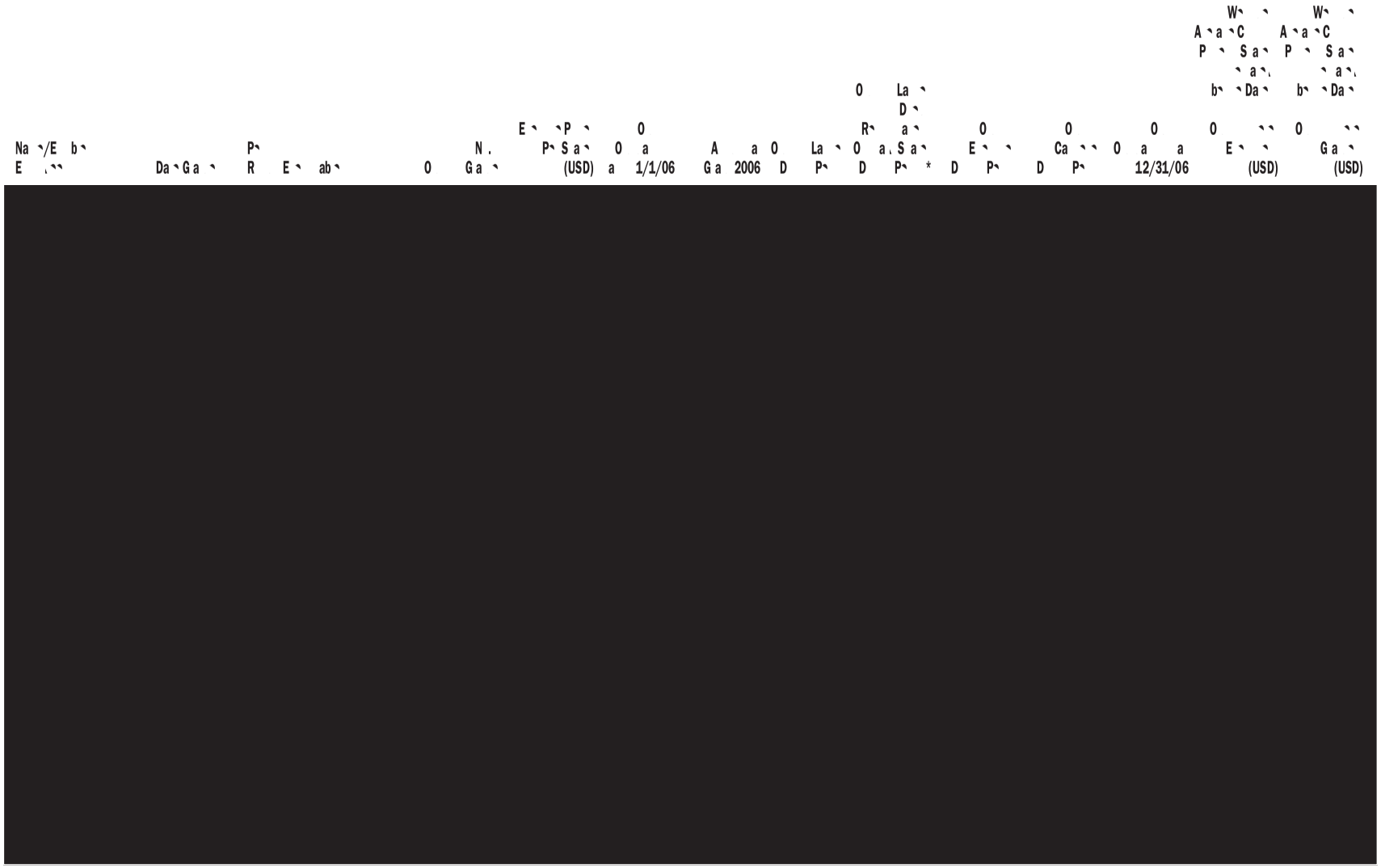
2001 P ` ` ` ` S a ` P a



Options to purchase preference shares issued to new employees generally vest at a rate of 10% upon the second anniversary, an additional 20% on the third anniversary and an additional 70% upon the fourth anniversary of the vesting commencement date. Employees may early exercise their options to purchase preference shares. If an employee early exercises 100% of his or her options, the options vest at a rate of 25% upon each first, second, third, and fourth anniversary of the vesting commencement date. Furthermore, in this case, if the employee remains employed by the Company and the Company has completed its initial public offering as of the third anniversary of the vesting commencement date, all options shall vest.

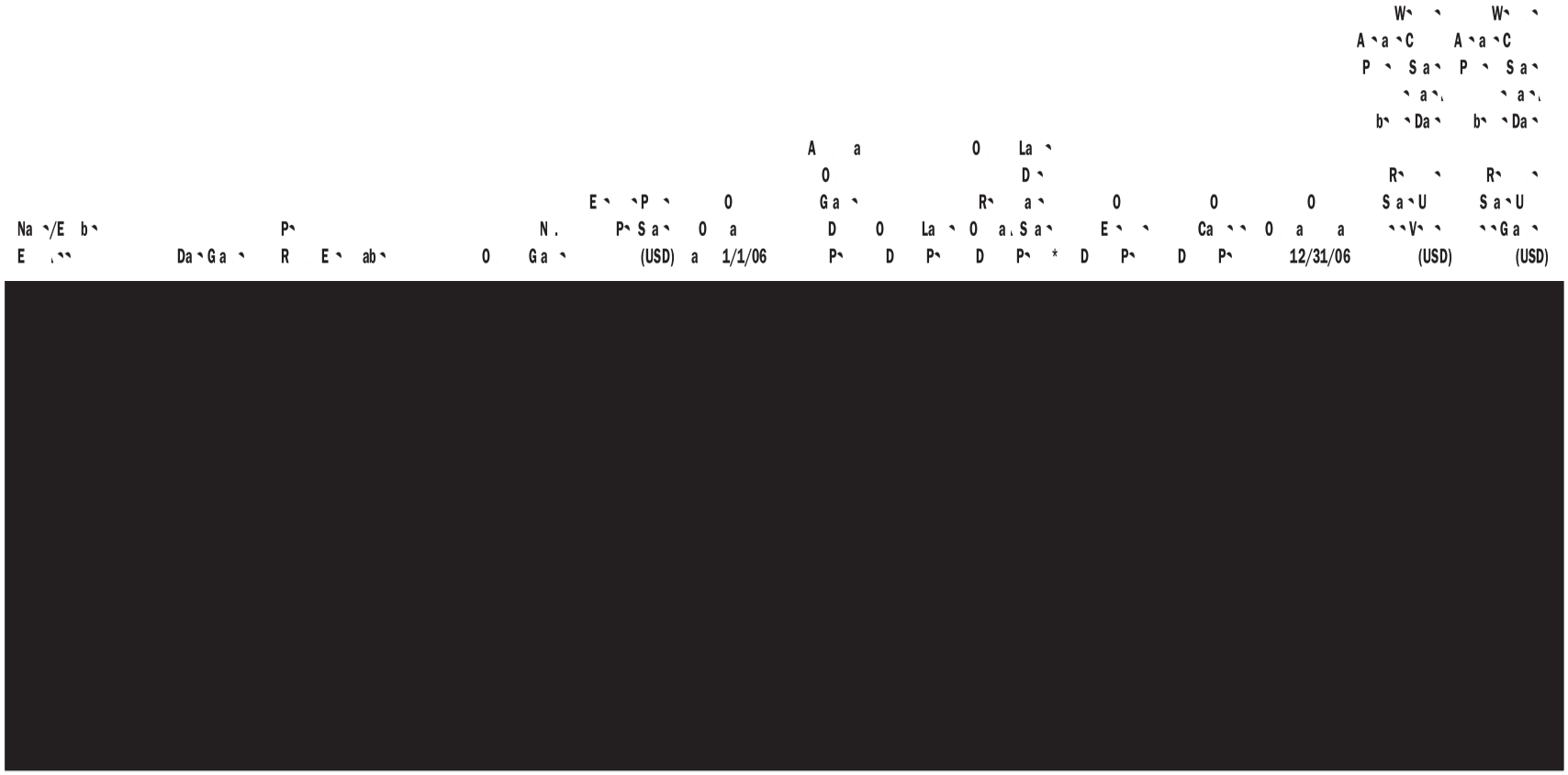
The options to purchase preference shares converted into options to purchase ordinary shares immediately prior to the completion of the Global Offering.

2004 S O P a



Options to purchase ordinary shares issued to new employees generally vest at a rate of 10% upon the second anniversary, an additional 20% on the third anniversary and an additional 70% upon the fourth anniversary of the vesting commencement date. Options to purchase ordinary shares issued to then-existing employees generally vest at a rate of 25% upon the first, second, third, and fourth anniversaries of the vesting commencement date.

2004 E . I . P a



Awards of the RSUs issued to new employees generally vest at a rate of 10% upon the second anniversary, an additional 20% on the third anniversary and an additional 70% upon the fourth anniversary of the vesting commencement date. Awards of the RSUs issued to then-existing employees generally vest at a rate of 25% upon the first, second, third, and fourth anniversaries of the vesting commencement date.

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

In November 2004, the HKSE issued its report entitled the "Code on Corporate Governance Practices and Corporate Governance Report", which subject to a grace period, has taken effect for accounting periods commencing on or after January 1, 2005. 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 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, 2006 to December 31, 2006, 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, 2006. 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 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 responsibility for preparing 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 or re-elect 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 elected for a term of three years at the 2005 AGM (except Dr. Albert Y. C. Yu who was elected at the 2006 AGM). The Class II Directors were re-elected for a term of three years at the 2006 AGM. The Class III Directors will be re-elected at the 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
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Heie147T24.9(w)e5142rClass I		
Heie147T24.9(w)e5142rClasss I		
Heie147T24.9(w)e5142rClasss I		
Heie147T24.9(w)e5142rClasss I		

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All Directors have access to the Company Secretary who is responsible for assisting the Board in complying with applicable procedures regarding compliance matters. Every Board member is entitled to have access to documents provided at the Board meeting or filed into the Company's minute-book. Furthermore, the

(6) 2 of these meetings were attended by proxy. Mr. Jiang was elected as Director at the 2006 AGM.
(7) 1 of these meetings was attended by proxy
(8) 2 of these meetings were attended by proxy. Dr. Yu was elected as Director at the 2006 AGM.

Procedure regarding the Appointment of Directors

The standard procedures regarding the appointment of Directors, which was adopted by the Board on September 22, 2005, sets forth the process by which individuals are appointed as members of the Board. Under the policy, the Board will consider, among other factors, (i) the skills, qualifications and experience of the nominee, including other directorships held in listed public companies in the last three years and other major appointments; (ii) the nominee's shareholdings in the Company; (iii) the independence of the nominee under United States and/or Hong Kong listing rules; and (iv) the impact with respect to the Company's status as a "foreign private issuer" under the United States securities laws. The Board will then decide whether to appoint such nominee to fill a casual vacancy on the Board or to add the nominee to the existing Directors and to appoint such nominee into one of the three classes of directors as stipulated in the Articles of Association.

Board Committees

The Board has established the following principal committees to assist it in exercising its obligations. These committees consist of only Independent Non-executive Directors who have been invited to serve as members. The committees are governed by their respective charters setting out clear terms of reference.

Compensation Committee

As of December 31, 2006, the members of the Company's compensation committee (the "Compensation Committee") were Ta-Lin Hsu (chairman of Compensation Committee), Tsuyoshi Kawanishi and Lip-Bu Tan. None of these members of the Compensation Committee has been an executive officer or employee of the Company or any of its subsidiaries. See "Connected Transactions" for a description of transactions between the Company and the members of the Compensation Committee.

The responsibilities of the Compensation Committee include, among other things:

- approving and overseeing the total compensation package for the Company's executive officers and any other officer, evaluating the performance of and determining and approving the compensation to be paid to the Company's Chief Executive Officer and reviewing the results of the Chief Executive Officer's evaluation of the performance of the Company's other executive officers;

- reviewing and making recommendations to the Board with respect to Director compensation, including equity-based compensation;

- administering and periodically reviewing and making recommendations to the Board regarding the long-term incentive compensation or equity plans made available to the Directors, employees and consultants;

- reviewing and making recommendations to the Board regarding executive compensation philosophy, strategy and principles and reviewing new and existing employment, consulting, retirement and severance agreements proposed for the Company's executive officers; and

- ensuring appropriate oversight of the Company's human resources policies and reviewing strategies established to fulfill the Company's ethical, legal and human resources responsibilities.

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 emolument of US$348,968. 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, 2006, 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. These options will be vested as to 50% on May 30, 2007 and as to 50% on May 30, 2008, and both options will expire on the earlier of September 29, 2016 or 120 days after termination of the director's service to the Board. Mr. Fang Yao 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. Shares under the Restricted Share Units are to be automatically vested as to 50% per year starting from May 30, 2007.

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, 2006, 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. Yen-Pong Jou (who retired as an Independent Non-executive Director at the annual general meeting held on May 30, 2006) lapsed and cancelled on September 27, 2006.

In addition to reviewing the remuneration of the Non-executive Directors and the members of the Company's management, the Compensation Committee reviewed:

(i) the remuneration policy for employees for the fiscal year 2006;

(ii) the profit-sharing and bonus policies;

(iii) the long term compensation strategy, including a review of the issuance of the shares under the Option Plans;

(iv) the accounting treatment and financial implications of the employees' share options under U.S. GAAP; and

(v) the attrition rate.

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

The Compensation Committee meets in person at least on a quarterly basis and on such other occasions as may be required to discuss and vote upon significant issues affecting the compensation policy of the Company. The meeting schedule for a year is planned in the preceding year. The Company Secretary assists the chairman of the Compensation 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

- approving the remuneration and terms of engagement of the Company's independent auditor;
- reviewing reports from the Company's independent auditor regarding its internal quality-control procedures and any material issues raised in the most recent review or investigation of such procedures and regarding all relationships between the Company and the independent auditor;
- pre-approving the hiring of any employee or former employee of the Company's independent auditor who was a member of the audit team during the preceding two years;
- reviewing the Company's annual and interim financial statements, earnings releases, critical accounting policies and practices used to prepare financial statements, alternative treatments of financial information, the effectiveness of the Company's disclosure controls and procedures and important trends and developments in financial reporting practices and requirements;
- reviewing the planning and staffing of internal audits, the organization, responsibilities, plans, results, budget and staffing of the Company's Internal Audit Department (as defined and discussed below) and the quality and effectiveness of the Company's internal controls;
- reviewing the Company's risk assessment and management policies;
- 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 2006, the Audit Committee reviewed:

- the financial reports for the year ended December 31, 2005 and the six month period ended June 30, 2006;
- 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 2006;
- 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;

- 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 quarterly 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.

During the year ended December 31, 2006, the Audit Committee held a total of eight (8) meetings. Details of Directors' attendance at the Audit Committee are set forth below:

	Number of Meetings Attended	Attendance Rate
Henry Shaw	8/8	100%
Lip-Bu Tan[1]	8/8	100%
Yang Yuan Wang[2]	8/8	100%
Average Attendance Rate		100%

[1] 1 of these meetings was attended by proxy

[2] 4 of these meetings were attended by proxy

At each quarterly Audit Committee meeting, the Audit Committee reviews with the Acting Chief Financial Officer and the Company's outside auditors, the financial statements for the financial period and the financial and accounting principles, policies and controls of the Company and its subsidiaries. In particular, the Committee discusses (i) the changes in accounting policies and practices, if any; (ii) the going concern assumptions, (iii) compliance with accounting standards and applicable rules and other legal requirements in relation to financial reporting and (iv) the internal controls of the Company relating to financial reporting. Upon the recommendation of the Audit Committee, the Board will approve the financial statements.

Auditors' Remuneration

The following table sets forth the aggregate audit fees, Sarbanes-Oxley compliance testing fee, audit-related fees, tax fees and all other fees we paid or incurred for audit services, audit-related services, tax services and other services rendered by our principal accountants during the fiscal year ended December 31, 2006.

	2006
Audit Fees	$1,460,000
Audit-Related Fees	–
Tax Fees	$33,789
All Other Fees	$85,597
Total	$1,579,386

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 controls over financial reporting and, beginning in fiscal year 2006, to include management's assessment of the effectiveness of the Company's internal controls over financial reporting in the Company's annual report on Form 20F 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.

Internal Audit Department

Internal Audit Department works with and supports the Company's management team and the Audit Committee to evaluate and contribute to the improvement of risk management, control, and governance systems. On an annual basis, the Audit Committee will review and approve an annual internal audit plan, which is based on a risk assessment methodology, which assists in determining business risks and establishing appropriate audit frequencies.

Based on this annual audit plan, the Internal Audit Department will audit the practices, procedures, expenditure and internal controls of the various departments in the Company. The scope of the audit includes:

- reviewing management's control to ensure the reliability and integrity of financial and operating information and the means used to identify, measure, classify, and report such information;
- reviewing the systems established or to be established to ensure compliance with policies, plans, procedures, laws, and regulations that could have a significant impact on operations and reports, and determining whether the Company is in compliance;
- reviewing the means of safeguarding assets and, when appropriate, verifying the existence of assets;
- appraising the economy and efficiency with which resources are employed;
- identifying significant risks to the ability of the Company to meet its business objectives, communicating them to management and ensuring that management has taken appropriate action to guard against those risks; and
- evaluating the effectiveness of controls supporting the operations of the Company and providing recommendations as to how those controls could be improved.

In addition, the Internal Audit Department will audit areas of concern identified by the Risk Management Committee or conduct reviews and investigations on an ad hoc basis. In conducting these audits, the Internal Audit Department has free and full access to all necessary functions, records, properties and personnel.

After completing an audit, the Internal Audit Department furnishes the Company's management team with analysis, appraisals, recommendations, counsel, and information concerning the activities reviewed. Appropriate managers of the Company will be notified of any deficiencies cited by the Internal Audit Department, which will follow up with the implementation of audit recommendations. In addition, the Internal Audit Department will report their findings directly to the Audit Committee on at least a quarterly basis.

The Internal Audit Department has direct access to the Board through the co-chairmen of the Audit Committee. The Internal Audit Department may upon request meet privately with the Audit Committee, without the presence of members of the Company's management or the independent accounting firm. The Internal Audit Department consists of members of the Company's management team.

Risk Management Committee

The Risk Management Committee identifies, analyzes, and assesses enterprise-wide risks, monitors the Company's risk management efforts, and reports on the effectiveness of the Company's enterprise risk management programs. The Risk Management Committee is responsible for developing the Company's risk management strategy; establishing, reviewing, and approving policies and procedures to control risks as well as to prevent fraud; determining risk tolerances for measurement; preparing a risk management implementation plan and assigning responsibilities; and designing and preparing education and awareness programs and its implementation plans. Such risks can include without limitation, legal risks, credit risks, market risks, operational risks, environmental risks, and systemic risks. The Risk Management Committee consists of members of the Company's management team, including three executive officers of the Company.

The Risk Management Committee reports to the Chief Executive Officer periodically, and to the Audit Committee on a quarterly basis. If requested, the chair of the Risk Management Committee will report to the Board on major issues of the enterprise risk management programs.

The Board, through the Audit Committee, has reviewed the effectiveness of the Company's system of internal control and believes that the system of internal controls in place at December 31, 2006 and at the date of this annual report, is effective and adequate.

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

Shareholder Communications and Investor Relations

The Company and the Board recognizes the importance of maintaining open and frequent communications with its shareholders. At the 2006 AGM, the President of the Company, as well as the Company's outside auditors, were present to answer questions from the shareholders. Together with this annual report, an annual general meeting circular is distributed to all shareholders within the prescribed time period required by the Listing Rules, notifying the shareholders about the AGM. The circular and the accompanying materials set forth the procedures for demanding and conducting a poll, including applicable notice requirements, and other relevant information relating to the proposed resolutions. Separate resolutions are proposed at these annual general meetings on each substantially separate issue, including the election of individual Directors. The Chairman reveals how many proxies for and against have been filed in respect to each resolution. The results of the poll are published in newspapers with circulation in Hong Kong and on the web sites of the Company and HKSE.

On the first business day after the 2006 AGM, which was held on May 30, 2006 at the Company's headquarters in Shanghai, China, the results of the poll were published in two newspapers with circulation in Hong Kong and on the web sites of the Company and HKSE. During the 2006 AGM, the Company's shareholders:

- received and considered the audited financial statements and the reports of the Directors and Auditors of the Company for the year ended December 31, 2005;
- elected Albert Y. C. Yu as Class I Director to hold office until 2008 AGM and authorized the Board to fix his remuneration;
- re-elected Ta-Lin Hsu and Lip-Bu Tan as Class II Directors and elected Jiang Shang Zhou as Class II Director for terms of three years and authorised the Board to fix their remuneration;
- re-elected Fang Yao as Class III Director to hold office until 2007 AGM and authorised the Board to fix his remuneration;
- re-elected Deloitte Tohmatsu as Auditors of the Company and authorised the Audit Committee to fix their remuneration;
- approved the general mandate to Directors to allot, issue, grant, distribute, and otherwise deal with additional shares in the Company not exceeding 20% of the issued share capital of the Company as of the date of the 2006 AGM;
- approved the general mandate to Directors to repurchase shares in the Company not exceeding 10% of the issued share capital of the Company as of the date of the 2006 AGM;
- approved amendments to the 2004 Stock Option Plan;
- approved amendments to the 2004 EIP;

- approved amendments to the 2004 ESPP; and

- approved a standard form of stock option plan for subsidiaries 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 2006 AGM and the above referenced conference calls, the Company's shareholders were invited to gatherings 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, 2006 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 51.

The market capitalization of the Company as of December 31, 2006 was HK$18,617,084,027.6 (issued share capital of 18,432,756,463 ordinary shares at the closing market price of HK$1.01 per ordinary share). The public float as of such date was approximately 84.59%.

The AGM is scheduled to be held at the Company's headquarters at 18 Zhangjiang Road, PuDong New Area, Shanghai, China 201203 on May 23, 2007 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 Compantuniti(s,useization of the Compan)24.9(y')1at ats,egrirestor Re-14businessenior

Social Responsibility

SMIC in the Community

Support for Education

Support for the Environment

Employee Well-Being

Employee Health & Safety

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Report by Management on Internal Control over Financial Reporting

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Report of Independent Registered Public Accounting Firm

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We have audited the accompanyin
its subsidiaries (the "Company") a
tions, stockholders' equity and co

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls my become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2006, 2005 and 2004 and the results of its operations and cash flows for each of the three years in the period ended December 31, 2006, in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, management's assessment that the Company maintained effective internal control over financial reporting as of December 31, 2006, is fairly stated, in all material respects, based on criteria established in *Internal Control – Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Furthermore, in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2006, based on criteria established in *Internal Control – Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

Deloitte Touche Tohmatsu
Certified Public Accountants

Hong Kong
April 24, 2007

Consolidated Balance Sheets

(In US dollars, except share data)

	Notes	December 31, 2006	2005 (As Restated, see Note 31)	2004 (As Restated, see Note 31)
ASSETS				
Current assets:				
Cash and cash equivalents		**$ 363,619,731**	$ 585,796,887	$ 607,172,570
Short-term investments	6	**57,950,603**	13,795,859	20,364,184
Accounts receivable, net of allowances of $4,048,845 in 2006, $1,091,340 in 2005 and $1,105,165 in 2004	5	**252,184,975**	241,333,914	169,188,287
Inventories	7	**275,178,952**	191,237,636	144,017,852
Prepaid expense and other current assets		**20,766,945**	9,810,591	12,842,994
Receivable for sale of manufacturing equipments		**70,544,560**	5,490,000	–
Assets held for sale	8	**9,420,729**	–	1,831,972
Total current assets		**1,049,666,495**	1,047,464,887	955,417,859
Land use rights, net	9	**38,323,333**	34,767,518	39,197,774
Plant and equipment, net	10	**3,244,400,822**	3,285,631,131	3,311,924,599
Acquired intangible assets, net	11	**71,692,498**	80,667,737	77,735,299
Deferred cost, net	24	**94,183,034**	117,728,792	–
Equity investment	12	**13,619,643**	17,820,890	–
Other long-term prepayments		**4,119,433**	2,552,407	–
Deferred tax assets	17	**25,286,900**	–	–
TOTAL ASSETS		**$ 4,541,292,158**	$ 4,586,633,362	$ 4,384,275,531
LIABILITIES AND STOCKHOLDERS' EQUITY				
Current liabilities:				
Accounts payable	13	**$ 309,129,199**	$ 262,318,432	$ 364,333,613
Accrued expenses and other current liabilities		**97,121,231**	92,916,030	76,399,187
Short-term borrowings	15	**71,000,000**	265,481,082	91,000,000
Current portion of promissory note	14	**29,242,001**	29,242,001	–
Current portion of long-term debt	15	**170,796,968**	246,080,580	191,986,372
Income tax payable		**72,417**	–	152,000
Total current liabilities		**677,361,816**	896,038,125	723,871,172

Consolidated Balance Sheets

(In US dollars, except share data)

	Notes	December 31, 2006	2005 (As Restated, see Note 31)	2004 (As Restated, see Note 31)
Long-term liabilities:				
Promissory note	14	**77,601,657**	103,254,436	–
Long-term debt	15	**719,570,905**	494,556,385	544,462,074
Long-term payables relating to license agreements	16	**16,992,950**	24,686,398	–
Other long term liabilities		**3,333,333**	–	–
Deferred tax liabilities	17	**210,913**	–	–
Total long-term liabilities		**817,709,758**	622,497,219	544,462,074
Total liabilities		**1,495,071,574**	1,518,535,344	1,268,333,246
Commitments	21			
Minority interest		**38,800,666**	38,781,863	–
Stockholders' equity:				
Ordinary shares, $0.0004 par value, 50,000,000,000 authorised in 2006, 2005 and 2004, shares issued and outstanding 18,432,756,463 in 2006, 18,301,680,867 in 2005 and 18,232,179,139 in 2004, respectively	18	**7,373,103**	7,320,673	7,292,872
Warrants	19	**32,387**	32,387	32,387
Additional paid-in capital		**3,288,733,078**	3,291,407,448	3,289,724,885
Notes receivable from stockholders	19	**–**	–	(391,375)
Accumulated other comprehensive income		**91,840**	138,978	387,776
Deferred share-based compensation		**–**	(24,881,919)	(51,177,675)
Accumulated deficit		**(288,810,490)**	(244,701,412)	(129,926,585)
Total stockholders' equity		**3,007,419,918**	3,029,316,155	3,115,942,285
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY		**$ 4,541,292,158**	$ 4,586,633,362	$ 4,384,275,531
Net current assets		**$ 372,304,679**	$ 151,426,762	$ 231,546,687
Total assets less current liabilities		**$ 3,863,930,342**	$ 3,690,595,237	$ 3,660,404,359

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, 2006	2005 (As Restated, see Note 31)	2004 (As Restated, see Note 31)
Sales	22	**$ 1,465,322,867**	$ 1,171,318,735	$ 974,664,696
Cost of sales	2	**1,338,155,004**	1,105,133,544	716,225,372
Gross profit		**127,167,863**	66,185,191	258,439,324
Operating expenses and income:				
Research and development	2	**94,170,750**	78,865,306	74,113,116
General and administrative	2	**47,364,533**	35,700,768	54,038,382
Selling and marketing	2	**18,231,048**	17,713,228	10,383,794
Litigation settlement	24		–	16,694,741
Amortization of acquired intangible assets	2	**24,393,561**	20,946,051	14,368,025
Income from sale of plant and equipment and other fixed assets	10	**(43,121,929)**	–	–
Total operating expenses (income), net		**141,037,963**	153,225,353	169,598,058
(Loss) income from operations	27	**(13,870,100)**	(87,040,162)	88,841,266
Other income (expense):				
Interest income		**14,916,323**	11,355,972	10,587,244
Interest expense		**(50,926,084)**	(38,784,323)	(13,697,894)
Foreign currency exchange (loss) gain		**(21,912,234)**	(3,355,279)	8,217,567
Others, net		**1,821,337**	4,461,925	2,441,057
Total other (expense) income, net		**(56,100,658)**	(26,321,705)	7,547,974
(Loss) income before income tax		**(69,970,758)**	(113,361,867)	96,389,240
Income tax credit (expense)	17	**24,927,744**	(284,867)	(186,044)
Minority interest		**(18,803)**	251,017	–
Loss from equity investment	12	**(4,201,247)**	(1,379,110)	–
Net (loss) income before cumulative effect of a change in accounting principle		**(49,263,064)**	(114,774,827)	96,203,196
Cumulative effect of a change in accounting principle	3	**5,153,986**	–	–

Consolidated Statements of Operations

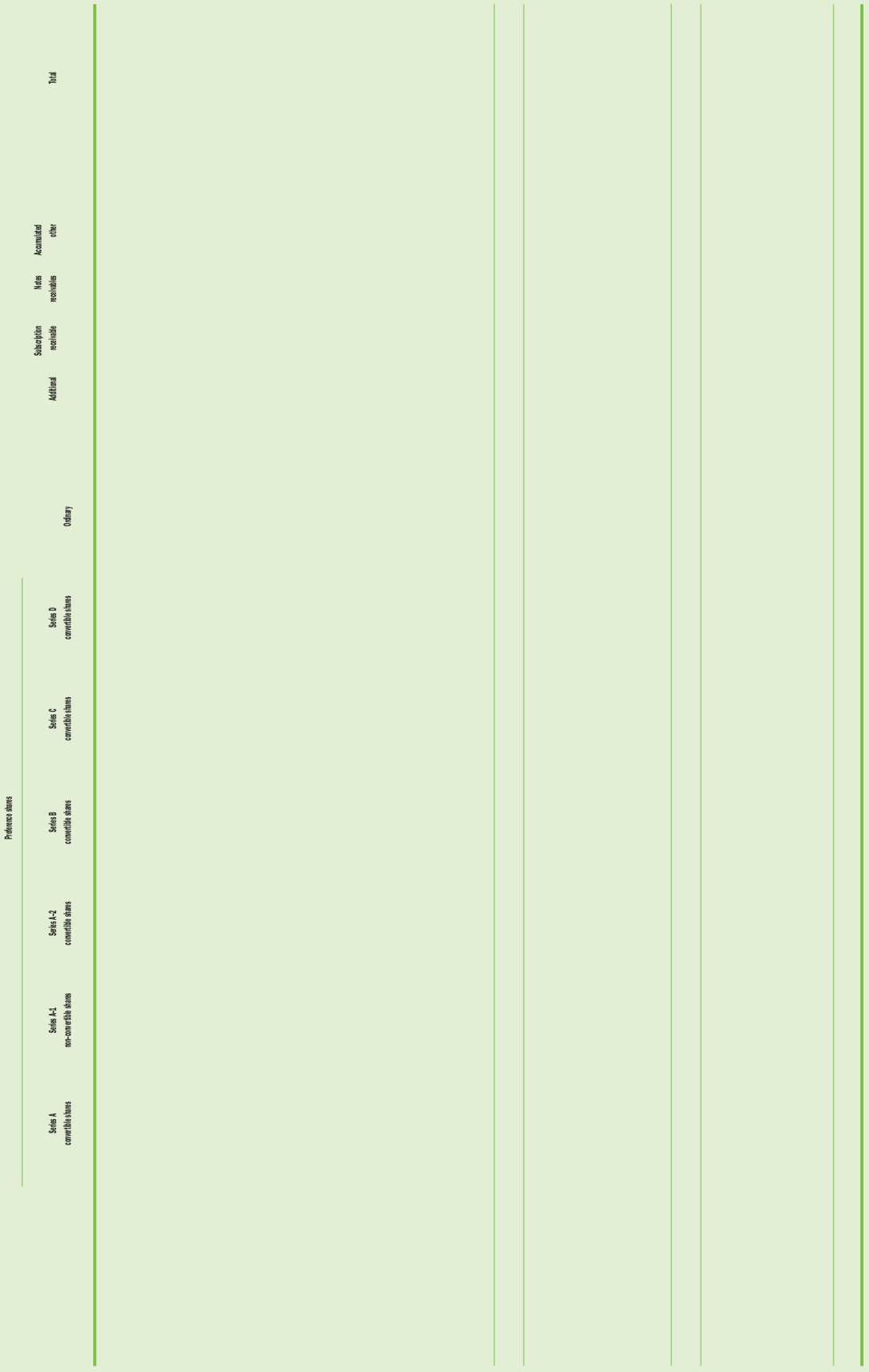
(In US dollars, except share data)

	Notes	Year ended December 31, 2006	2005 (As Restated, see Note 31)	2004 (As Restated, see Note 31)
Net (loss) income		**$ (44,109,078)**	$ (114,774,827)	$ 96,203,196
Deemed dividends on preference shares	29		–	18,839,426
(Loss) income attributable to holders of ordinary shares		**$ (44,109,078)**	$ (114,774,827)	$ 77,363,770
On the basis of net loss before accounting change per share, basic	20	**$ (0.00)**	$ (0.01)	$ 0.01
On the basis of net loss before accounting change per share, diluted	20	**$ (0.00)**	$ (0.01)	$ 0.00
Cumulative effect of an accounting change per share, basic and diluted	20	**$ 0.00**	$ –	$ –
(Loss) income per share, basic	20	**$ (0.00)**	$ (0.01)	$ 0.01
(Loss) income per share, diluted	20	**$ (0.00)**	$ (0.01)	$ 0.00
Shares used in calculating basic (loss) income per share	20	**18,334,498,923**	18,184,429,255	14,199,163,517
Shares used in calculating diluted (loss) income per share	20	**18,334,498,923**	18,184,429,255	17,934,393,066

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)



Consolidated Statements of Cash Flows

(In US dollars, except share data)

Consolidated Statements of Cash Flows

(In US dollars, except share data)

	Year ended December 31,		
	2006	2005 (As Restated, see Note 31)	2004 (As Restated, see Note 31)
Financing activities:			
Proceeds from short-term borrowings	**255,003,999**	394,158,994	91,000,000
Repayment of short-term borrowings	**(449,485,081)**	(219,677,912)	–
Repayment of note payable to stockholder for land use rights	**–**	–	(12,778,797)
Proceeds from long-term debt	**785,344,546**	253,432,612	256,487,871
Repayment of long-term debt	**(635,613,638)**	(249,244,093)	–
Repayment of promissory note	**(30,000,000)**	(30,000,000)	(15,000,000)
Payment of loan initiation fee	**(3,596,938)**	–	–
Proceeds from issuance of Series D convertible preference shares	**–**	–	30,000,000
Proceeds from issuance of ordinary shares from initial public offering	**–**	–	1,016,859,151
Collection of subscription receivables, net	**–**	–	105,420,031
Proceeds from exercise of employee stock options	**3,907,118**	2,303,151	681,339
Collection of notes receivables from employees	**–**	391,376	35,245,774
Change in deposits received from stockholders	**–**	–	(38,151,407)
Proceeds from minority investor (note 1)	**–**	39,000,025	–
Net cash (used in) provided by financing activities	**(74,439,994)**	190,364,153	1,469,763,962
Effect of exchange rate changes	**(16,885)**	(192,246)	256,389
NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	**(222,177,156)**	(21,375,683)	161,896,236
CASH AND CASH EQUIVALENTS, beginning of year	**585,796,887**	607,172,570	445,276,334
CASH AND CASH EQUIVALENTS, end of year	**$ 363,619,731**	$ 585,796,887	$ 607,172,570
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:			
Income taxes paid	**$ 164,409**	$ 436,867	$ 34,044
Interest paid	**$ 46,808,533**	$ 47,113,456	$ 20,104,223

Consolidated Statements of Cash Flows

(In US dollars, except share data)

	Year ended December 31,		
	2006	2005 (As Restated, see Note 31)	2004 (As Restated, see Note 31)
SUPPLEMENTAL DISCLOSURES OF NON-CASH INVESTING AND FINANCING ACTIVITIES			
Note payable waived by stockholder in exchange for land use rights	**$ –**	$ –	$ (14,239,246)
Series D convertible preference shares issued to acquire assets and assume liabilities from Motorola and MCEL	**$ –**	$ –	$ 278,180,024
Issuance of Series D convertible preference share warrants	**$ –**	$ –	$ 27,663,780
Series D convertible preference shares issued in exchange for certain software licenses	**$ –**	$ –	$ 5,060,256
Series B convertible preference shares issued in exchange for acquired intangible assets	**$ –**	$ –	$ 2,739,853
Series B convertible preference shares issued to a service provider	**$ –**	$ –	$ 45,090
Conversion of preference shares into ordinary shares upon initial public offering	**$ –**	$ –	$ 5,971,115
Ordinary shares and warrants issued to a service provider	**$ –**	$ –	$ (79,590)
Ordinary shares issued in exchange for equipment	**$ –**	$ –	$ 5,222,180
Ordinary and preference shares issued in exchange for employee note receivable	**$ –**	$ –	$ (388,924)
Inception of accounts payable for plant and equipment	**$ (165,828,795)**	$ (143,723,643)	$ (272,164,643)
Issuance of promissory note for acquired intangible assets	**$ –**	$ (132,496,437)	$ –
Inception of long-term payable for acquired intangible assets	**$ (16,992,950)**	$ (24,686,398)	$ –
Inception of other receivable for sales of manufacturing equipment	**$ 70,544,560**	$ 5,490,000	$ –

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