

MAGNACHIP SEMICONDUCTOR Corp

Form 10-Q

August 07, 2015

[Table of Contents](#)

**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**FORM 10-Q**

**x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE  
ACT OF 1934**

**For the quarterly period ended June 30, 2015**

**or**

**.. TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE  
ACT OF 1934**

**For the transition period from \_\_\_\_\_ to \_\_\_\_\_.**

**Commission File Number: 001-34791**

**MagnaChip Semiconductor Corporation**

**(Exact name of registrant as specified in its charter)**

**Delaware**  
**(State or other jurisdiction of**  
**incorporation or organization)**  
**c/o MagnaChip Semiconductor S.A.**  
**1, Allée Scheffer, L-2520**  
**Luxembourg, Grand Duchy of Luxembourg**  
**(352) 45-62-62**

**83-0406195**  
**(I.R.S. Employer**  
**Identification No.)**

**(Address, zip code, and telephone number, including area code, of registrant's principal executive offices)**

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. ☒ Yes ☐ No

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer ☐ Accelerated filer ☒  
Non-accelerated filer ☐ (Do not check if a smaller reporting company) Smaller reporting company ☐  
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). ☐ Yes ☒ No

As of August 1, 2015, the registrant had 34,565,717 shares of common stock outstanding.

**Table of Contents**

**MAGNACHIP SEMICONDUCTOR CORPORATION AND SUBSIDIARIES**

**TABLE OF CONTENTS**

|                                                                                                                                                                        | <b>Page No.</b> |
|------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------|
| <b><u>PART I FINANCIAL INFORMATION</u></b>                                                                                                                             | <b>3</b>        |
| Item 1. <u>Interim Consolidated Financial Statements (Unaudited)</u>                                                                                                   | 3               |
| <u>MagnaChip Semiconductor Corporation and Subsidiaries Consolidated Balance Sheets as of June 30, 2015 and December 31, 2014</u>                                      | 3               |
| <u>MagnaChip Semiconductor Corporation and Subsidiaries Consolidated Statements of Operations for the Three and Six Months Ended June 30, 2015 and 2014</u>            | 4               |
| <u>MagnaChip Semiconductor Corporation and Subsidiaries Consolidated Statements of Comprehensive Income for the Three and Six Months Ended June 30, 2015 and 2014</u>  | 5               |
| <u>MagnaChip Semiconductor Corporation and Subsidiaries Consolidated Statements of Changes in Stockholders' Equity for the Six Months Ended June 30, 2015 and 2014</u> | 6               |
| <u>MagnaChip Semiconductor Corporation and Subsidiaries Consolidated Statements of Cash Flows for the Six Months Ended June 30, 2015 and 2014</u>                      | 7               |
| <u>MagnaChip Semiconductor Corporation and Subsidiaries Notes to Consolidated Financial Statements</u>                                                                 | 8               |
| Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>                                                                   | 24              |
| Item 3. <u>Quantitative and Qualitative Disclosures About Market Risk</u>                                                                                              | 45              |
| Item 4. <u>Controls and Procedures</u>                                                                                                                                 | 46              |
| <b><u>PART II OTHER INFORMATION</u></b>                                                                                                                                | <b>48</b>       |
| Item 1. <u>Legal Proceedings</u>                                                                                                                                       | 48              |
| Item 1A. <u>Risk Factors</u>                                                                                                                                           | 48              |
| Item 6. <u>Exhibits</u>                                                                                                                                                | 49              |
| <b><u>SIGNATURES</u></b>                                                                                                                                               | <b>50</b>       |

**Table of Contents****PART I FINANCIAL INFORMATION****Item 1. Interim Consolidated Financial Statements (Unaudited)****MAGNACHIP SEMICONDUCTOR CORPORATION AND SUBSIDIARIES****CONSOLIDATED BALANCE SHEETS****(Unaudited; in thousands of US dollars, except share data)**

|                                            | <b>June 30,<br/>2015</b> | <b>December 31,<br/>2014</b> |
|--------------------------------------------|--------------------------|------------------------------|
| <b>Assets</b>                              |                          |                              |
| Current assets                             |                          |                              |
| Cash and cash equivalents                  | \$ 72,672                | \$ 102,434                   |
| Accounts receivable, net                   | 67,780                   | 72,957                       |
| Inventories, net                           | 71,800                   | 75,334                       |
| Other receivables                          | 5,450                    | 10,616                       |
| Prepaid expenses                           | 7,142                    | 7,560                        |
| Current deferred income tax assets         | 43                       | 237                          |
| Hedge collateral                           | 6,380                    |                              |
| Other current assets                       | 7,383                    | 6,898                        |
| <b>Total current assets</b>                | <b>238,650</b>           | <b>276,036</b>               |
| Property, plant and equipment, net         | 208,351                  | 223,766                      |
| Intangible assets, net                     | 2,476                    | 2,451                        |
| Long-term prepaid expenses                 | 9,875                    | 10,916                       |
| Deferred income tax assets                 | 260                      | 415                          |
| Other non-current assets                   | 12,876                   | 14,147                       |
| <b>Total assets</b>                        | <b>\$ 472,488</b>        | <b>\$ 527,731</b>            |
| <b>Liabilities and Stockholders Equity</b> |                          |                              |
| Current liabilities                        |                          |                              |
| Accounts payable                           | \$ 57,432                | \$ 70,767                    |
| Other accounts payable                     | 9,724                    | 10,986                       |
| Accrued expenses                           | 75,556                   | 81,060                       |
| Other current liabilities                  | 5,946                    | 6,460                        |
| <b>Total current liabilities</b>           | <b>148,658</b>           | <b>169,273</b>               |
| Long-term borrowings, net                  | 224,095                  | 224,035                      |
| Accrued severance benefits, net            | 143,727                  | 139,289                      |
| Other non-current liabilities              | 10,703                   | 13,636                       |

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|                                                                                                                                                                                                                  |            |            |
|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------|------------|
| Total liabilities                                                                                                                                                                                                | 527,183    | 546,233    |
| Commitments and Contingencies (Note 16)                                                                                                                                                                          |            |            |
| Stockholders' equity                                                                                                                                                                                             |            |            |
| Common stock, \$0.01 par value, 150,000,000 shares authorized, 40,840,685 shares issued and 34,261,920 outstanding at June 30, 2015 and 40,635,233 shares issued and 34,056,468 outstanding at December 31, 2014 | 408        | 406        |
| Additional paid-in capital                                                                                                                                                                                       | 121,602    | 118,419    |
| Accumulated deficit                                                                                                                                                                                              | (61,998)   | (11,343)   |
| Treasury stock, 6,578,765 shares at June 30, 2015 and December 31, 2014                                                                                                                                          | (90,918)   | (90,918)   |
| Accumulated other comprehensive loss                                                                                                                                                                             | (23,789)   | (35,066)   |
| Total stockholders' equity (deficit)                                                                                                                                                                             | (54,695)   | (18,502)   |
| Total liabilities and stockholders' equity                                                                                                                                                                       | \$ 472,488 | \$ 527,731 |

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

**Table of Contents****MAGNACHIP SEMICONDUCTOR CORPORATION AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF OPERATIONS****(Unaudited; in thousands of US dollars, except share data)**

|                                              | <b>Three Months Ended</b> |                          | <b>Six Months Ended</b>  |                          |
|----------------------------------------------|---------------------------|--------------------------|--------------------------|--------------------------|
|                                              | <b>June 30,<br/>2015</b>  | <b>June 30,<br/>2014</b> | <b>June 30,<br/>2015</b> | <b>June 30,<br/>2014</b> |
| Net sales                                    | \$ 162,015                | \$ 172,070               | \$ 326,900               | \$ 336,234               |
| Cost of sales                                | 126,729                   | 136,613                  | 256,637                  | 260,500                  |
| Gross profit                                 | 35,286                    | 35,457                   | 70,263                   | 75,734                   |
| Operating expenses                           |                           |                          |                          |                          |
| Selling, general and administrative expenses | 28,588                    | 30,746                   | 53,618                   | 55,773                   |
| Research and development expenses            | 21,931                    | 24,059                   | 44,091                   | 47,196                   |
| Total operating expenses                     | 50,519                    | 54,805                   | 97,709                   | 102,969                  |
| Operating loss                               | (15,233)                  | (19,348)                 | (27,446)                 | (27,235)                 |
| Interest expense, net                        | (3,933)                   | (4,007)                  | (7,996)                  | (8,077)                  |
| Foreign currency gain (loss), net            | (12,296)                  | 38,424                   | (15,472)                 | 29,018                   |
| Other income, net                            | 234                       | 597                      | 790                      | 1,158                    |
| Income (loss) before income taxes            | (31,228)                  | 15,666                   | (50,124)                 | (5,136)                  |
| Income tax expenses (benefits)               | (602)                     | 656                      | 531                      | 1,459                    |
| Net income (loss)                            | \$ (30,626)               | \$ 15,010                | \$ (50,655)              | \$ (6,595)               |
| Earnings (loss) per common share             |                           |                          |                          |                          |
| Basic                                        | \$ (0.90)                 | \$ 0.44                  | \$ (1.49)                | \$ (0.19)                |
| Diluted                                      | \$ (0.90)                 | \$ 0.43                  | \$ (1.49)                | \$ (0.19)                |
| Weighted average number of shares            |                           |                          |                          |                          |
| Basic                                        | 34,092,402                | 34,056,359               | 34,074,534               | 34,054,626               |
| Diluted                                      | 34,092,402                | 35,177,915               | 34,074,534               | 34,054,626               |

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

**Table of Contents****MAGNACHIP SEMICONDUCTOR CORPORATION AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME****(Unaudited; in thousands of US dollars)**

|                                                                            | <b>Three Months Ended</b> |                 | <b>Six Months Ended</b> |                 |
|----------------------------------------------------------------------------|---------------------------|-----------------|-------------------------|-----------------|
|                                                                            | <b>June 30,</b>           | <b>June 30,</b> | <b>June 30,</b>         | <b>June 30,</b> |
|                                                                            | <b>2015</b>               | <b>2014</b>     | <b>2015</b>             | <b>2014</b>     |
| Net income (loss)                                                          | \$ (30,626)               | \$ 15,010       | \$ (50,655)             | \$ (6,595)      |
| Other comprehensive income (loss)                                          |                           |                 |                         |                 |
| Foreign currency translation adjustments                                   | 10,123                    | (25,955)        | 13,179                  | (19,336)        |
| Derivative adjustments                                                     |                           |                 |                         |                 |
| Fair valuation of derivatives                                              | (1,417)                   | 8,002           | (1,417)                 | 6,201           |
| Reclassification adjustment for gain on derivatives included in net income |                           | (2,647)         | (485)                   | (2,644)         |
| Investment adjustments                                                     |                           |                 |                         |                 |
| Unrealized gain on investments                                             |                           | 925             |                         | 1,201           |
| Reclassification adjustment for gain on investments included in net income |                           | (1,882)         |                         | (1,882)         |
| Total other comprehensive income (loss)                                    | 8,706                     | (21,557)        | 11,277                  | (16,460)        |
| Total comprehensive loss                                                   | \$ (21,920)               | \$ (6,547)      | \$ (39,378)             | \$ (23,055)     |

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

Table of Contents**MAGNACHIP SEMICONDUCTOR CORPORATION AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY**

(Unaudited; in thousands of US dollars, except share data)

|                                   | <b>Common Stock</b> |               | <b>Additional</b> | <b>Retained</b>     | <b>Treasury</b> | <b>Accumulated</b>   |              |
|-----------------------------------|---------------------|---------------|-------------------|---------------------|-----------------|----------------------|--------------|
|                                   | <b>Shares</b>       | <b>Amount</b> | <b>Paid-In</b>    | <b>Earnings</b>     | <b>Stock</b>    | <b>Other</b>         |              |
|                                   |                     |               | <b>Capital</b>    | <b>(Accumulated</b> |                 | <b>Comprehensive</b> | <b>Total</b> |
|                                   |                     |               |                   | <b>deficit)</b>     |                 | <b>Loss</b>          |              |
| <b>Six Months Ended</b>           |                     |               |                   |                     |                 |                      |              |
| <b>June 30, 2015</b>              |                     |               |                   |                     |                 |                      |              |
| <b>Balance at January 1, 2015</b> | 34,056,468          | \$ 406        | \$ 118,419        | \$ (11,343)         | \$ (90,918)     | \$ (35,066)          | \$ (18,502)  |
| Stock-based compensation          |                     |               | 1,977             |                     |                 |                      | 1,977        |
| Exercise of stock options         | 205,452             | 2             | 1,206             |                     |                 |                      | 1,208        |
| Other comprehensive income, net   |                     |               |                   |                     |                 | 11,277               | 11,277       |
| Net loss                          |                     |               |                   | (50,655)            |                 |                      | (50,655)     |
| <b>Balance at June 30, 2015</b>   | 34,261,920          | \$ 408        | \$ 121,602        | \$ (61,998)         | \$ (90,918)     | \$ (23,789)          | \$ (54,695)  |
| <b>Six Months Ended</b>           |                     |               |                   |                     |                 |                      |              |
| <b>June 30, 2014</b>              |                     |               |                   |                     |                 |                      |              |
| <b>Balance at January 1, 2014</b> | 34,048,366          | \$ 406        | \$ 116,222        | \$ 105,889          | \$ (90,918)     | \$ (50,058)          | \$ 81,541    |
| Stock-based compensation          |                     |               | 1,072             |                     |                 |                      | 1,072        |
| Exercise of stock options         | 6,795               |               | 48                |                     |                 |                      | 48           |
| Exercise of warrants              | 1,202               |               | 19                |                     |                 |                      | 19           |
| Other comprehensive loss, net     |                     |               |                   |                     |                 | (16,460)             | (16,460)     |
| Net loss                          |                     |               |                   | (6,595)             |                 |                      | (6,595)      |
| <b>Balance at June 30, 2014</b>   | 34,056,363          | \$ 406        | \$ 117,361        | \$ 99,294           | \$ (90,918)     | \$ (66,518)          | \$ 59,625    |

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

Table of Contents**MAGNACHIP SEMICONDUCTOR CORPORATION AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF CASH FLOWS****(Unaudited; in thousands of US dollars)**

|                                                                                          | <b>Six Months Ended</b> |                 |
|------------------------------------------------------------------------------------------|-------------------------|-----------------|
|                                                                                          | <b>June 30,</b>         | <b>June 30,</b> |
|                                                                                          | <b>2015</b>             | <b>2014</b>     |
| <b>Cash flows from operating activities</b>                                              |                         |                 |
| Net loss                                                                                 | \$ (50,655)             | \$ (6,595)      |
| Adjustments to reconcile net loss to net cash provided by (used in) operating activities |                         |                 |
| Depreciation and amortization                                                            | 13,667                  | 15,022          |
| Provision for severance benefits                                                         | 11,877                  | 9,426           |
| Bad debt expenses (reversal of allowance)                                                | (3)                     | 3,724           |
| Amortization of debt issuance costs and original issue discount                          | 324                     | 301             |
| Loss (gain) on foreign currency, net                                                     | 17,146                  | (31,969)        |
| Gain on disposal of investments                                                          |                         | (1,524)         |
| Stock-based compensation                                                                 | 1,977                   | 1,072           |
| Other                                                                                    | 1,547                   | 758             |
| Changes in operating assets and liabilities                                              |                         |                 |
| Accounts receivable                                                                      | 3,145                   | 6,712           |
| Inventories, net                                                                         | 1,623                   | (11,537)        |
| Other receivables                                                                        | 5,523                   | 781             |
| Other current assets                                                                     | 2,235                   | 4,590           |
| Deferred tax assets                                                                      | 339                     | 391             |
| Accounts payable                                                                         | (12,431)                | 4,556           |
| Other accounts payable                                                                   | (5,550)                 | (8,560)         |
| Accrued expenses                                                                         | (10,710)                | 20,260          |
| Other current liabilities                                                                | (2,058)                 | 1,230           |
| Other non-current liabilities                                                            | (1,084)                 | 292             |
| Payment of severance benefits                                                            | (4,231)                 | (3,490)         |
| Other                                                                                    | (147)                   | 13              |
| Net cash provided by (used in) operating activities                                      | (27,466)                | 5,453           |
| <b>Cash flows from investing activities</b>                                              |                         |                 |
| Payment of hedge collateral                                                              | (6,555)                 |                 |
| Proceeds from disposal of investments                                                    |                         | 2,003           |
| Purchase of plant, property and equipment                                                | (1,964)                 | (12,058)        |
| Payment for intellectual property registration                                           | (263)                   | (490)           |
| Payment of guarantee deposits                                                            | (642)                   | (308)           |
| Other                                                                                    | 237                     | 39              |
| Net cash used in investing activities                                                    | (9,187)                 | (10,814)        |

**Cash flows from financing activities**

|                                                       |          |          |
|-------------------------------------------------------|----------|----------|
| Proceeds from issuance of common stock                | 1,208    | 67       |
| Net cash provided by financing activities             | 1,208    | 67       |
| Effect of exchange rates on cash and cash equivalents | 5,683    | (7,315)  |
| Net decrease in cash and cash equivalents             | (29,762) | (12,609) |

**Cash and cash equivalents**

|                         |           |            |
|-------------------------|-----------|------------|
| Beginning of the period | 102,434   | 153,606    |
| End of the period       | \$ 72,672 | \$ 140,997 |

**Supplemental cash flow information**

|                            |          |          |
|----------------------------|----------|----------|
| Cash paid for interest     | \$ 7,683 | \$ 7,354 |
| Cash paid for income taxes | \$ 388   | \$ 706   |

**Non-cash investing activities**

|                                                                   |          |          |
|-------------------------------------------------------------------|----------|----------|
| Property, plant and equipment additions in other accounts payable | \$ 1,493 | \$ 1,436 |
|-------------------------------------------------------------------|----------|----------|

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

**Table of Contents**

**MagnaChip Semiconductor Corporation and Subsidiaries**

**Notes to Consolidated Financial Statements**

**(Unaudited; tabular dollars in thousands, except share data)**

**1. Business, Basis of Presentation and Significant Accounting Policies**

***Business***

MagnaChip Semiconductor Corporation (together with its subsidiaries, the Company) is a Korea-based designer and manufacturer of analog and mixed-signal semiconductor products for consumer, computing, communication, industrial, automotive and Internet of Things (IoT) applications. The Company provides technology platforms for analog, mixed signal, power, high voltage, non-volatile memory and Radio Frequency (RF) applications. The Company's business is comprised of two operating segments: Semiconductor Manufacturing Services and Standard Products Group. The Company's Semiconductor Manufacturing Services provide specialty analog and mixed-signal foundry services mainly for fabless and Integrated Device Manufacturer (IDM) semiconductor companies that primarily serve the consumer, computing, communication, industrial, automotive and IoT applications. The Company's Standard Products Group is comprised of two business lines: Display Solutions and Power Solutions. The Company's Display Solutions products provide flat panel display solutions to major suppliers of large and small flat panel displays. The Company's Power Solutions products include discrete and integrated circuit solutions for power management in consumer, communication and industrial applications.

***Basis of Presentation***

The accompanying unaudited interim consolidated financial statements of the Company have been prepared in accordance with generally accepted accounting principles in the United States of America (US GAAP). These interim consolidated financial statements include normal recurring adjustments and the elimination of all intercompany accounts and transactions which are, in the opinion of management, necessary to provide a fair statement of the Company's financial condition and results of operations for the periods presented. These interim consolidated financial statements are presented in accordance with ASC 270, *Interim Reporting* (ASC 270) and, accordingly, do not include all of the information and note disclosures required by US GAAP for complete financial statements. The results of operations for the three and six months ended June 30, 2015 are not necessarily indicative of the results to be expected for a full year or for any other periods.

The December 31, 2014 balance sheet data was derived from the Company's audited financial statements, but does not include all disclosures required by US GAAP.

The segment disclosures reflect the Company's new operating segments. See Note 13, Geographic and Segment Information, for a more detailed discussion and explanation of the change.

***Recent Accounting Pronouncements***

In April 2015, the FASB issued Accounting Standards Update. 2015-03, *Interest Imputation of Interest* (ASU 2015-03). ASU 2015-03 requires that debt issuance costs are presented in the balance sheet as a direct deduction from the carrying amount of debt liability, consistent with debt discounts or premiums. The recognition and measurement guidance for debt issuance costs would not be affected. ASU 2015-03 is effective for annual reporting periods beginning after December 15, 2015, including interim periods within that reporting period. The Company is currently

evaluating the impact of the adoption of ASU 2015-03 on its consolidated financial statements.

In August 2014, the FASB issued Accounting Standards Update No. 2014-15, Presentation of Financial Statements Going Concern (ASU 2014-15), which provides guidance on determining when and how to disclose going-concern uncertainties in the financial statements. ASU 2014-15 requires management to perform interim and annual assessments of an entity's ability to continue as a going concern within one year of the date the financial statements are issued. An entity will be required to provide certain disclosures if conditions of events raise substantial doubt about the entity's ability to continue as a going concern. ASU 2014-15 is effective for annual periods ending after December 15, 2016, and interim periods thereafter, with early adoption permitted. The Company is currently evaluating the impact of the adoption of ASU 2014-15 on its consolidated financial statements.

**Table of Contents****MagnaChip Semiconductor Corporation and Subsidiaries****Notes to Consolidated Financial Statements (Continued)****(Unaudited; tabular dollars in thousands, except share data)**

In May 2014, the FASB issued Accounting Standards Update No. 2014-09, Revenue from Contracts with Customers (ASU 2014-09). ASU 2014-09 supersedes the revenue recognition requirements in Revenue Recognition (Topic 605), and requires entities to recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled to in exchange for those goods or services. ASU 2014-09 is effective for annual reporting periods beginning after December 15, 2016 (the Original Effective Date), including interim periods within that reporting period, and can be adopted either retrospectively to each prior reporting period presented or as a cumulative-effect adjustment as of the date of adoption, with early application permitted as of the Original Effective Date. In July 2015, the FASB decided to delay the effective date of ASU 2014-09 by one year. The Company is currently evaluating the impact of the adoption of ASU 2014-09 on its consolidated financial statements.

**2. Sales of Accounts Receivable and Receivable Discount Program**

The Company has entered into an agreement to sell selected trade accounts receivable to a financial institution from time to time since March 2012. After the sale, the Company does not retain any interest in the receivables and the applicable financial institution collects these accounts receivable directly from the customer. The proceeds from the sales of these accounts receivable totaled \$32,143 thousand and \$5,712 thousand for the six months ended June 30, 2015 and 2014, respectively, and these sales resulted in pre-tax losses of \$37 thousand and \$17 thousand for the six months ended June 30, 2015 and 2014, respectively, which are included in selling, general and administrative expenses in the consolidated statements of operations. Net proceeds of this accounts receivable sale program are recognized in the consolidated statements of cash flows as part of operating cash flows.

The Company uses receivable discount programs with certain customers. While these discount arrangements allow the Company to accelerate collection of customers' receivables, there can be no assurance that these programs will continue in the future.

**3. Inventories**

Inventories as of June 30, 2015 and December 31, 2014 consist of the following:

|                                         | <b>June 30,<br/>2015</b> | <b>December 31,<br/>2014</b> |
|-----------------------------------------|--------------------------|------------------------------|
| Finished goods                          | \$ 36,602                | \$ 40,404                    |
| Semi-finished goods and work-in-process | 55,428                   | 68,153                       |
| Raw materials                           | 8,195                    | 7,520                        |
| Materials in-transit and other          | 2,936                    | 6,745                        |
| Less: inventory reserve                 | (31,361)                 | (47,488)                     |

|                  |           |           |
|------------------|-----------|-----------|
| Inventories, net | \$ 71,800 | \$ 75,334 |
|------------------|-----------|-----------|

|                         | <b>Three Months<br/>Ended<br/>June 30, 2015</b> | <b>Six Months<br/>Ended<br/>June 30, 2015</b> | <b>Three Months<br/>Ended<br/>June 30, 2014</b> | <b>Six Months<br/>Ended<br/>June 30, 2014</b> |
|-------------------------|-------------------------------------------------|-----------------------------------------------|-------------------------------------------------|-----------------------------------------------|
| Beginning balance       | \$ (41,818)                                     | \$ (47,488)                                   | \$ (70,265)                                     | \$ (72,400)                                   |
| Change in reserve       | (4,977)                                         | (5,864)                                       | (562)                                           | (3,326)                                       |
| Write off               | 14,912                                          | 21,240                                        | 8,839                                           | 12,760                                        |
| Translation adjustments | 522                                             | 751                                           | (3,682)                                         | (2,704)                                       |
| Ending balance          | \$ (31,361)                                     | \$ (31,361)                                   | \$ (65,670)                                     | \$ (65,670)                                   |

Inventory reserve represents the Company's best estimate in value lost due to excessive inventory level, physical deterioration, obsolescence, changes in price levels, or other causes based on individual facts and circumstances. Inventory reserve relates to inventory items including finished goods, semi-finished goods and work-in-process. Write off of this reserve is recognized only when the related inventory has been disposed or scrapped.

**Table of Contents****MagnaChip Semiconductor Corporation and Subsidiaries****Notes to Consolidated Financial Statements (Continued)****(Unaudited; tabular dollars in thousands, except share data)****4. Property, Plant and Equipment**

Property, plant and equipment as of June 30, 2015 and December 31, 2014 comprise the following:

|                                    | <b>June 30,<br/>2015</b> | <b>December 31,<br/>2014</b> |
|------------------------------------|--------------------------|------------------------------|
| Buildings and related structures   | \$ 69,589                | \$ 70,552                    |
| Machinery and equipment            | 264,669                  | 269,031                      |
| Vehicles and others                | 24,782                   | 24,812                       |
|                                    | 359,040                  | 364,395                      |
| Less: accumulated depreciation     | (167,031)                | (157,341)                    |
| Land                               | 16,342                   | 16,712                       |
| Property, plant and equipment, net | \$ 208,351               | \$ 223,766                   |

Aggregate depreciation expenses totaled \$13,502 thousand and \$14,161 thousand for the six months ended June 30, 2015 and 2014, respectively.

**5. Intangible Assets**

Intangible assets as of June 30, 2015 and December 31, 2014 are as follows:

|                                | <b>June 30,<br/>2015</b> | <b>December 31,<br/>2014</b> |
|--------------------------------|--------------------------|------------------------------|
| Technology                     | \$ 19,247                | \$ 19,683                    |
| Customer relationships         | 27,642                   | 28,269                       |
| Intellectual property assets   | 8,357                    | 8,359                        |
| Less: accumulated amortization | (52,770)                 | (53,860)                     |
| Intangible assets, net         | \$ 2,476                 | \$ 2,451                     |

Aggregate amortization expenses for intangible assets totaled \$165 thousand and \$861 thousand for the six months ended June 30, 2015 and 2014, respectively.

**6. Accrued Expenses**

Accrued expenses as of June 30, 2015 and December 31, 2014 are as follows:

|                                                                   | <b>June 30,<br/>2015</b> | <b>December 31,<br/>2014</b> |
|-------------------------------------------------------------------|--------------------------|------------------------------|
| Payroll, benefits and related taxes, excluding severance benefits | \$ 20,135                | \$ 18,654                    |
| Withholding tax levied on intercompany interest income            | 29,198                   | 27,497                       |
| Interest on senior notes                                          | 6,874                    | 7,040                        |
| Settlement obligations                                            | 6,031                    | 8,976                        |
| Outside service fees                                              | 4,943                    | 10,640                       |
| Others                                                            | 8,375                    | 8,253                        |
| <b>Accrued expenses</b>                                           | <b>\$ 75,556</b>         | <b>\$ 81,060</b>             |

Settlement obligations included in the table above relate to claims involving the Company's products that may have caused a failure in the customers' products. Although the Company does not agree with the claims, as its products met the customers' specifications, the Company considered a number of factors and decided not to dispute the claims but make certain in-kind payments as demanded by the customers. These settlement obligations are accrued when they are deemed probable and can be reasonably estimated.

**Table of Contents****MagnaChip Semiconductor Corporation and Subsidiaries****Notes to Consolidated Financial Statements (Continued)****(Unaudited; tabular dollars in thousands, except share data)****7. Derivative Financial Instruments**

The Company's Korean subsidiary from time to time has entered into zero cost collar contracts to hedge the risk of changes in the functional-currency-equivalent cash flows attributable to currency rate changes on U.S. dollar denominated revenues.

Details of derivative contracts as of June 30, 2015 are as follows:

| <b>Date of transaction</b> | <b>Type of derivative</b> | <b>Total notional amount</b> | <b>Month of settlement</b> |
|----------------------------|---------------------------|------------------------------|----------------------------|
| May 11, 2015               | Zero cost collar          | \$ 42,000                    | July to December 2015      |
| May 27, 2015               | Zero cost collar          | \$ 42,000                    | July to December 2015      |

The Company did not have any derivative contracts in effect as of December 31, 2014.

The zero cost collar contracts qualify as cash flow hedges under ASC 815, *Derivatives and Hedging*, (ASC 815), since at both the inception of the contracts and on an ongoing basis, the hedging relationship was and is expected to be highly effective in achieving offsetting cash flows attributable to the hedged risk during the term of the contracts. The Company is utilizing the hypothetical derivative method to measure the effectiveness by comparing the changes in value of the actual derivative versus the change in fair value of the hypothetical derivative.

The fair values of the Company's outstanding zero cost collar contracts recorded as liabilities as of June 30, 2015 and December 31, 2014 are as follows:

| <b>Derivatives designated as hedging instruments:</b> | <b>June 30, December 31,</b> |             |
|-------------------------------------------------------|------------------------------|-------------|
|                                                       | <b>2015</b>                  | <b>2014</b> |
| <b>Liability Derivatives:</b>                         |                              |             |
| Zero cost collars                                     | Other current liabilities    |             |
|                                                       | \$ 1,702                     | \$          |

Offsetting of derivative liabilities as of June 30, 2015 is as follows:

| <b>As of June 30, 2015</b> | <b>Gross amounts recognized liabilities</b> | <b>Gross amounts offset in the balance sheets</b> | <b>Net amounts of liabilities presented in the balance sheets</b> | <b>Gross amounts not offset in the balance sheets</b> | <b>Net amount</b>      |
|----------------------------|---------------------------------------------|---------------------------------------------------|-------------------------------------------------------------------|-------------------------------------------------------|------------------------|
|                            |                                             |                                                   |                                                                   | <b>Financial instruments collateral</b>               | <b>Cash collateral</b> |

| pledged                                                                                                                                                                                                                                                                                                                                                                                                                                                  |    |       |    |    |       |    |                   |
|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----|-------|----|----|-------|----|-------------------|
| Liability Derivatives:                                                                                                                                                                                                                                                                                                                                                                                                                                   |    |       |    |    |       |    |                   |
| Zero cost collars                                                                                                                                                                                                                                                                                                                                                                                                                                        | \$ | 1,702 | \$ | \$ | 1,702 | \$ | \$ (1,380) \$ 322 |
| For derivative instruments that are designated and qualify as cash flow hedges, the effective portion of the gain or loss on the derivative is reported as a component of accumulated other comprehensive income ( AOCI ) and reclassified into earnings in the same period or periods during which the hedged transaction affects earnings. Gains and losses on the derivative, representing hedge ineffectiveness, are recognized in current earnings. |    |       |    |    |       |    |                   |

Table of Contents**MagnaChip Semiconductor Corporation and Subsidiaries****Notes to Consolidated Financial Statements (Continued)****(Unaudited; tabular dollars in thousands, except share data)**

The following table summarizes the impact of derivative instruments on the consolidated statement of operations for the three months ended June 30, 2015 and 2014:

|                       | Amount of Gain<br>(Loss) |          | Location of<br>Gain | Amount of Gain      |          | Location of Loss  | Amount of Loss        |         |
|-----------------------|--------------------------|----------|---------------------|---------------------|----------|-------------------|-----------------------|---------|
|                       | Recognized in            |          | Reclassified from   | Reclassified from   |          | Statement of      | Recognized in         |         |
|                       | AOCI on                  |          | AOCI into           | AOCI into           |          | Operations on     | Statement of          |         |
|                       | Derivatives              |          | Statement of        | Statement of        |          | Derivative        | Operations on         |         |
|                       | (Effective Portion)      |          | Operations          | (Effective Portion) |          | (Ineffective      | Derivatives           |         |
|                       | Three Months Ended       |          | (Effective Portion) | Three Months Ended  |          | Portion)          | (Ineffective Portion) |         |
|                       | June 30,                 |          |                     | June 30,            |          |                   | June 30,              |         |
|                       | 2015                     | 2014     |                     | 2015                | 2014     |                   | 2015                  | 2014    |
| Derivatives in ASC    |                          |          |                     |                     |          |                   |                       |         |
| 815 Cash Flow Hedging |                          |          |                     |                     |          |                   |                       |         |
| Relationships         |                          |          |                     |                     |          |                   |                       |         |
| Zero cost collars     | \$ (1,417)               | \$ 8,002 | Net sales           | \$                  | \$ 2,647 | Other income, net | \$ (306)              | \$ (36) |
| Total                 | \$ (1,417)               | \$ 8,002 |                     | \$                  | \$ 2,647 |                   | \$ (306)              | \$ (36) |

The following table summarizes the impact of derivative instruments on the consolidated statement of operations for the six months ended June 30, 2015 and 2014:

|                       | Amount of Gain<br>(Loss) |          | Location of<br>Gain | Amount of Gain      |          | Location of Loss  | Amount of Loss        |         |
|-----------------------|--------------------------|----------|---------------------|---------------------|----------|-------------------|-----------------------|---------|
|                       | Recognized in            |          | Reclassified from   | Reclassified from   |          | Statement of      | Recognized in         |         |
|                       | AOCI on                  |          | AOCI into           | AOCI into           |          | Operations on     | Statement of          |         |
|                       | Derivatives              |          | Statement of        | Statement of        |          | Derivative        | Operations on         |         |
|                       | (Effective Portion)      |          | Operations          | (Effective Portion) |          | (Ineffective      | Derivatives           |         |
|                       | Six Months Ended         |          | (Effective Portion) | Six Months Ended    |          | Portion)          | (Ineffective Portion) |         |
|                       | June 30,                 |          |                     | June 30,            |          |                   | June 30,              |         |
|                       | 2015                     | 2014     |                     | 2015                | 2014     |                   | 2015                  | 2014    |
| Derivatives in ASC    |                          |          |                     |                     |          |                   |                       |         |
| 815 Cash Flow Hedging |                          |          |                     |                     |          |                   |                       |         |
| Relationships         |                          |          |                     |                     |          |                   |                       |         |
| Zero cost collars     | \$ (1,417)               | \$ 6,201 | Net sales           | \$ 485              | \$ 2,644 | Other income, net | \$ (306)              | \$ (52) |
| Total                 | \$ (1,417)               | \$ 6,201 |                     | \$ 485              | \$ 2,644 |                   | \$ (306)              | \$ (52) |

As of June 30, 2015, the amount expected to be reclassified from accumulated other comprehensive income into loss within the next twelve months is \$1,417 thousand.

The Company set aside \$5.0 million cash deposits to a financial institution, the counterparty to the zero cost collar contracts outstanding as of June 30, 2015. The Company is required to deposit cash collateral with the counterparty for any exposure in excess of \$0.5 million and \$1.4 million of cash collateral was required as of June 30, 2015. The Company recorded the cash deposits and cash collateral totaling \$6.4 million as hedge collateral in the consolidated balance sheet as of June 30, 2015. These outstanding zero cost collar contracts are subject to termination if the sum of qualified and unrestricted cash and cash equivalents held by the Company is less than \$30 million on the last day of a fiscal quarter.

**Table of Contents****MagnaChip Semiconductor Corporation and Subsidiaries****Notes to Consolidated Financial Statements (Continued)****(Unaudited; tabular dollars in thousands, except share data)****8. Fair Value Measurements**

The Company's financial liabilities measured at fair value on a recurring basis as of June 30, 2015, and the basis for that measurement is as follows:

|                                                    | Carrying Value | Fair Value Measurement | Quoted Prices in Active Markets for Identical Asset (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
|----------------------------------------------------|----------------|------------------------|---------------------------------------------------------------|-----------------------------------------------|-------------------------------------------|
| <b>Liabilities:</b>                                |                |                        |                                                               |                                               |                                           |
| Derivative liabilities (other current liabilities) | \$ 1,702       | \$ 1,702               | \$                                                            | \$ 1,702                                      | \$                                        |

The Company did not have any assets measured at fair value on a recurring basis as of June 30, 2015 other than cash and cash equivalents, accounts receivable, other receivables, hedge collateral, accounts payable, and other accounts payable, fair value of which approximate carrying values due to the short-term nature of these instruments. The fair value of assets and liabilities whose carrying value approximates fair value is determined using Level 2 inputs, with the exception of cash (Level 1).

As of June 30, 2015, the total carrying value and estimated fair value of the Company's 6.625% Senior Notes due 2021 (the 2021 Notes), which are not measured at fair value on a recurring basis, were \$224,095 thousand and \$180,563 thousand, respectively. The decrease in the fair value of the 2021 Notes from December 31, 2014 to June 30, 2015 was related to the revision of the Company's credit rating in the first quarter of 2015. The estimated fair value is based on Level 2 inputs.

**9. Long-Term Borrowings**

Long-term borrowings as of June 30, 2015 and December 31, 2014 are as follows:

|                                                   | June 30, 2015 | December 31, 2014 |
|---------------------------------------------------|---------------|-------------------|
| 6.625% senior notes due July 2021                 | \$ 225,000    | \$ 225,000        |
| Discount on senior notes                          | (905)         | (965)             |
| Long-term borrowings, net of unamortized discount | \$ 224,095    | \$ 224,035        |

On July 18, 2013, the Company issued \$225,000,000 aggregate principal amount of the 2021 Notes at a price of 99.5%. Interest on the 2021 Notes accrues at a rate of 6.625% per annum, payable semi-annually on January 15 and July 15 of each year, beginning on January 15, 2014.

In connection with the issuance of the 2021 Notes, the Company capitalized certain costs and fees, which are being amortized using the effective interest method over its respective term, 2013 to 2021. Amortization costs, which were included in interest expense in the accompanying statements of operations, amounted to \$133 thousand and \$265 thousand for the three and six months ended June 30, 2015, respectively. The remaining capitalized costs as of June 30, 2015, which were included in other non-current assets in the consolidated balance sheet, were \$4,055 thousand.

**Table of Contents**

**MagnaChip Semiconductor Corporation and Subsidiaries**

**Notes to Consolidated Financial Statements (Continued)**

**(Unaudited; tabular dollars in thousands, except share data)**

The Company can optionally redeem all or a part of the 2021 Notes according to the following schedule: (i) at any time prior to July 15, 2016, the Company may on any one or more occasions redeem up to 35% of the aggregate principal amount of 2021 Notes issued under that certain Indenture, dated as of July 18, 2013, by and between the Company and Wilmington Trust, National Association, as trustee (the Trustee), as supplemented by that certain First Supplemental Indenture, dated as of March 27, 2014 (collectively, the Indenture) at a redemption price equal to 106.625% of the principal amount of the 2021 Notes redeemed, plus accrued and unpaid interest and special interest, if any, to the date of redemption with the net proceeds of a qualified equity offering; (ii) at any time prior to July 15, 2017, the Company may on any one or more occasions redeem all or a part of the 2021 Notes at a redemption price equal to 100% of the principal amount of the notes redeemed, plus the applicable premium as of, and accrued and unpaid interest and special interest, if any, to the date of redemption; and (iii) on or after July 15, 2017, the Company may on any one or more occasions redeem all or a part of the 2021 Notes, at a redemption price equal to 103.313%, 101.656% and 100% of the principal amount of the notes redeemed in 2017, 2018 and 2019 and thereafter, respectively, plus accrued and unpaid interest and special interest, if any, on the notes redeemed, to the applicable date of redemption.

The Indenture contains covenants that limit ability of the Company and its restricted subsidiaries to: (i) declare or pay any dividend or make any payment or distribution on account of or purchase or redeem the Company's capital stock or equity interests of the restricted subsidiaries; (ii) make any principal payment on, or redeem or repurchase, prior to any scheduled repayment or maturity, any subordinated indebtedness; (iii) make certain investments; (iv) incur additional indebtedness and issue certain types of capital stock; (v) create or incur any lien (except for permitted liens) that secures obligations under any indebtedness; (vi) merge with or into or sell all or substantially all of the Company's assets to other companies; (vii) enter into certain types of transactions with affiliates; (viii) guarantee the payment of any indebtedness; (ix) enter into sale-leaseback transactions; (x) enter into agreements that would restrict the ability of the restricted subsidiaries to make distributions with respect to their equity to the Company or other restricted subsidiaries, to make loans to the Company or other restricted subsidiaries or to transfer assets to the Company or other restricted subsidiaries; and (xi) designate unrestricted subsidiaries.

These covenants are subject to a number of exceptions and qualifications. Certain of these restrictive covenants will terminate if the notes are rated investment grade at any time.

As disclosed in the Company's Form 8-K filed on June 25, 2014, the Company received a notice of default on June 20, 2014 (the 10-K and Q1 10-Q Notice of Default) from the Trustee under the Indenture. The 10-K and Q1 10-Q Notice of Default related to the failure by the Company, pursuant to Section 4.03 of the Indenture, to file with the Securities and Exchange Commission (SEC) its Annual Report on Form 10-K for the fiscal year ended December 31, 2013 and its Quarterly Report on Form 10-Q for the fiscal quarter ended March 31, 2014 (the Initial Reporting Defaults). The Company did not cure the Initial Reporting Defaults within the applicable 60-day grace period and the Initial Reporting Defaults ripened into Events of Default. The Company elected, as the sole and exclusive remedy for the Events of Default, to pay additional interest on the 2021 Notes at a rate equal to 0.25% per annum of the principal amount of the 2021 Notes (the Additional Interest) for a period of up to 180 days following the occurrence of the Events of Default (the Additional Interest Period).

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On August 20, 2014, the Company received a notice of default related to its failure to file its Form 10-Q for the fiscal quarter ended June 30, 2014 (the "Q2 10-Q Notice of Default"), and on November 19, 2014, the Company received a notice of default related to its failure to file its Form 10-Q for the fiscal quarter ended September 30, 2014 (the "Q3 10-Q Notice of Default"). These defaults also ripened into Events of Default and on December 29, 2014 and January 15, 2015, respectively, the Company elected to extend the Additional Interest Period for up to 180 days following each additional Event of Default.

Upon the filing with the SEC of the 2013 Form 10-K and the Form 10-Qs for each of the fiscal quarters ended March 31, 2014, June 30, 2014 and September 31, 2014, the Company regained compliance with its reporting obligations under the Indenture and cured all identified covenant defaults in each of the 10-K and the Q1 10-Q Notice of Default, the Q2 10-Q Notice of Default and the Q3 10-Q Notice of Default, and ceased accruing the Additional Interest on the 2021 Notes as of February 12, 2015.

As disclosed in the Company's Form 8-K filed on May 4, 2015, the Company received a notice of default on May 1, 2015 (the "10-K Notice of Default") from the Trustee under the Indenture. The 10-K Notice of Default related to the failure by the Company, pursuant to Section 4.03 of the Indenture, to file with the SEC its Annual Report on Form 10-K for the fiscal year ended December 31, 2014. The Company cured the default referenced in the 10-K Notice of Default within the applicable 60-day grace period under the Indenture by filing the 2014 Form 10-K with the SEC on May 28, 2015.

**Table of Contents****MagnaChip Semiconductor Corporation and Subsidiaries****Notes to Consolidated Financial Statements (Continued)****(Unaudited; tabular dollars in thousands, except share data)****10. Accrued Severance Benefits**

The majority of accrued severance benefits is for employees in the Company's Korean subsidiary. Pursuant to the Employee Retirement Benefit Security Act of Korea, eligible employees and executive officers with one or more years of service are entitled to severance benefits upon the termination of their employment based on their length of service and rate of pay. As of June 30, 2015, 98% of employees of the Company were eligible for severance benefits.

Changes in accrued severance benefits are as follows:

|                                                             | <b>Three<br/>Months<br/>Ended<br/>June 30, 2015</b> | <b>Six<br/>Months<br/>Ended<br/>June 30, 2015</b> | <b>Three<br/>Months<br/>Ended<br/>June 30, 2014</b> | <b>Six<br/>Months<br/>Ended<br/>June 30, 2014</b> |
|-------------------------------------------------------------|-----------------------------------------------------|---------------------------------------------------|-----------------------------------------------------|---------------------------------------------------|
| Beginning balance                                           | \$ 145,598                                          | \$ 140,405                                        | \$ 136,176                                          | \$ 135,356                                        |
| Provisions                                                  | 4,617                                               | 11,877                                            | 5,392                                               | 9,426                                             |
| Severance payments                                          | (2,890)                                             | (4,231)                                           | (1,976)                                             | (3,490)                                           |
| Translation adjustments                                     | (2,525)                                             | (3,251)                                           | 7,331                                               | 5,631                                             |
|                                                             | 144,800                                             | 144,800                                           | 146,923                                             | 146,923                                           |
| Less: Cumulative contributions to the National Pension Fund | (333)                                               | (333)                                             | (387)                                               | (387)                                             |
| Group severance insurance plan                              | (740)                                               | (740)                                             | (825)                                               | (825)                                             |
| Accrued severance benefits, net                             | \$ 143,727                                          | \$ 143,727                                        | \$ 145,711                                          | \$ 145,711                                        |

The severance benefits funded through the Company's National Pension Fund and group severance insurance plan will be used exclusively for payment of severance benefits to eligible employees. These amounts have been deducted from the accrued severance benefit balance.

The Company is liable to pay the following future benefits to its non-executive employees upon their normal retirement age:

|                   | <b>Severance benefit</b> |
|-------------------|--------------------------|
| Remainder of 2015 | \$ 288                   |
| 2016              | 1,104                    |
| 2017              | 1,680                    |

|           |        |
|-----------|--------|
| 2018      | 2,853  |
| 2019      | 2,226  |
| 2020      | 2,887  |
| 2021 2025 | 30,280 |

The above amounts were determined based on the non-executive employees' current salary rates and the number of service years that will be accumulated upon their retirement dates. These amounts do not include amounts that might be paid to non-executive employees that will cease working with the Company before their normal retirement ages.

## 11. Foreign Currency Gain (Loss), Net

Net foreign currency gain or loss includes non-cash translation gain or loss associated with intercompany balances. A substantial portion of the Company's net foreign currency gain or loss is non-cash translation gain or loss associated with intercompany long-term loans to the Company's Korean subsidiary. The loans are denominated in U.S. dollars and are affected by changes in the exchange rate between the Korean won and the U.S. dollar. As of June 30, 2015, the outstanding intercompany loan balance including accrued interests between the Korean subsidiary and the Dutch subsidiary was \$766 million. The Korean won to U.S. dollar exchange rates were 1,124.1:1 and 1,099.2:1 using the first base rate as of June 30, 2015 and December 31, 2014, respectively, as quoted by the Korea Exchange Bank.

**Table of Contents****MagnaChip Semiconductor Corporation and Subsidiaries****Notes to Consolidated Financial Statements (Continued)****(Unaudited; tabular dollars in thousands, except share data)****12. Income Taxes**

The Company files income tax returns in the U.S., Korea, Japan, Taiwan and various other jurisdictions.

The Company's Korean subsidiary is the principal operating entity within the consolidated Company. For the three months ended June 30, 2015 and 2014, no income tax expense for the Korean subsidiary was recorded due to net operating loss carry-forwards available to offset taxable income and full allowance for deferred tax assets.

Income tax expense (benefit) recorded for the three months ended June 30, 2015 and 2014 was \$(602) thousand and \$656 thousand, respectively, and for the six months ended June 30, 2015 and 2014 was \$531 thousand and \$1,459 thousand, respectively, primarily attributable to withholding taxes related to intercompany balances and benefits from the lapse of statute of limitations on unrecognized tax benefits.

**13. Geographic and Segment Information**

The Company previously reported its results of operations under one operating segment. During the second quarter of 2015, organizational changes were made to (i) realign the Company's businesses and organizational structure and (ii) streamline and consolidate certain business processes to achieve greater operating efficiencies. In furtherance of these objectives, the Company combined its business lines of Display Solutions and Power Solutions into a new segment called Standard Products Group. Beginning in the second quarter of 2015, the Company reports its financial results in two operating segments: Semiconductor Manufacturing Services and Standard Products Group. The Company's chief operating decision maker is its Chief Executive Officer who allocates resources and assesses performance of the business and other activities based on gross profit. The two newly established operating segments will be managed prospectively and all prior period amounts related to the segment change have been retrospectively reclassified to conform to the new presentation.

The following sets forth information relating to the operating segments:

|                                      | <b>Three Months Ended</b> |                 | <b>Six Months Ended</b> |                 |
|--------------------------------------|---------------------------|-----------------|-------------------------|-----------------|
|                                      | <b>June 30,</b>           | <b>June 30,</b> | <b>June 30,</b>         | <b>June 30,</b> |
|                                      | <b>2015</b>               | <b>2014</b>     | <b>2015</b>             | <b>2014</b>     |
| <b>Net Sales</b>                     |                           |                 |                         |                 |
| Semiconductor Manufacturing Services | \$ 78,962                 | \$ 90,339       | \$ 153,482              | \$ 182,267      |
| Standard Products Group              |                           |                 |                         |                 |
| Display Solutions                    | 48,918                    | 45,327          | 105,271                 | 85,706          |
| Power Solutions                      | 33,995                    | 36,275          | 67,832                  | 68,050          |
| Total Standard Products Group        | 82,913                    | 81,602          | 173,103                 | 153,756         |

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|                 |            |            |            |            |
|-----------------|------------|------------|------------|------------|
| All other       | 140        | 129        | 315        | 211        |
| Total net sales | \$ 162,015 | \$ 172,070 | \$ 326,900 | \$ 336,234 |

|                                      | <b>Three Months Ended<br/>June 30,<br/>2015</b> | <b>Three Months Ended<br/>June 30,<br/>2014</b> | <b>Six Months Ended<br/>June 30,<br/>2015</b> | <b>Six Months Ended<br/>June 30,<br/>2014</b> |
|--------------------------------------|-------------------------------------------------|-------------------------------------------------|-----------------------------------------------|-----------------------------------------------|
| <b>Gross Profit</b>                  |                                                 |                                                 |                                               |                                               |
| Semiconductor Manufacturing Services | \$ 17,183                                       | \$ 18,601                                       | \$ 32,560                                     | \$ 40,723                                     |
| Standard Products Group              | 17,963                                          | 16,727                                          | 37,388                                        | 34,801                                        |
| All other                            | 140                                             | 129                                             | 315                                           | 210                                           |
| Total gross profit                   | \$ 35,286                                       | \$ 35,457                                       | \$ 70,263                                     | \$ 75,734                                     |

**Table of Contents****MagnaChip Semiconductor Corporation and Subsidiaries****Notes to Consolidated Financial Statements (Continued)****(Unaudited; tabular dollars in thousands, except share data)**

The following is a summary of net sales by region, based on the location of the customer:

|                                 | <b>Three Months Ended</b> |                          |
|---------------------------------|---------------------------|--------------------------|
|                                 | <b>June 30,<br/>2015</b>  | <b>June 30,<br/>2014</b> |
| Korea                           | \$ 61,755                 | \$ 67,320                |
| Asia Pacific (other than Korea) | 75,582                    | 74,337                   |
| U.S.A.                          | 20,310                    | 24,596                   |
| Europe                          | 3,708                     | 5,601                    |
| Others                          | 660                       | 216                      |
| Total                           | \$ 162,015                | \$ 172,070               |

|                                 | <b>Six Months Ended</b>  |                          |
|---------------------------------|--------------------------|--------------------------|
|                                 | <b>June 30,<br/>2015</b> | <b>June 30,<br/>2014</b> |
| Korea                           | \$ 124,225               | \$ 134,333               |
| Asia Pacific (other than Korea) | 154,759                  | 144,558                  |
| U.S.A.                          | 39,680                   | 44,349                   |
| Europe                          | 7,361                    | 12,494                   |
| Others                          | 875                      | 500                      |
| Total                           | \$ 326,900               | \$ 336,234               |

Net sales from the Company's top ten largest customers accounted for 65% and 59% for the three months ended June 30, 2015 and 2014, respectively, and 66% and 57% for the six months ended June 30, 2015 and 2014, respectively.

For the three months ended June 30, 2015, the Company had two customers that represented 14.8% and 10.8% of its net sales, respectively, and for the six months ended June 30, 2015, the Company had three customers that represented 15.1%, 11.3% and 10.1% of its net sales, respectively.

For the three months ended June 30, 2014, we had one customer which represented 10.5% of the Company's net sales, and for the six months ended June 30, 2014, we had no customer which represented over 10% of the Company's net sales.

96% of the Company's property, plant and equipment are located in Korea as of June 30, 2015.

**Table of Contents****MagnaChip Semiconductor Corporation and Subsidiaries****Notes to Consolidated Financial Statements (Continued)****(Unaudited; tabular dollars in thousands, except share data)****14. Accumulated Other Comprehensive Loss**

Accumulated other comprehensive loss consists of the following as of June 30, 2015 and December 31, 2014, respectively:

|                                          | <b>June 30,<br/>2015</b> | <b>December 31,<br/>2014</b> |
|------------------------------------------|--------------------------|------------------------------|
| Foreign currency translation adjustments | \$ (22,372)              | \$ (35,551)                  |
| Derivative adjustments                   | (1,417)                  | 485                          |
| <b>Total</b>                             | <b>\$ (23,789)</b>       | <b>\$ (35,066)</b>           |

Changes in accumulated other comprehensive loss for the three months ended June 30, 2015 and 2014 are as follows:

|                                                                  | <b>Foreign<br/>currency<br/>translation<br/>adjustments</b> | <b>Derivative<br/>adjustments</b> | <b>Unrealized<br/>gain on<br/>investments</b> | <b>Total</b> |
|------------------------------------------------------------------|-------------------------------------------------------------|-----------------------------------|-----------------------------------------------|--------------|
| <b>Three Months Ended June 30, 2015</b>                          |                                                             |                                   |                                               |              |
| Beginning balance                                                | \$ (32,495)                                                 | \$                                | \$                                            | \$ (32,495)  |
| Other comprehensive income (loss) before reclassifications       | 10,123                                                      | (1,417)                           |                                               | 8,706        |
| Amounts reclassified from accumulated other comprehensive income |                                                             |                                   |                                               |              |
| Net current-period other comprehensive income (loss)             | 10,123                                                      | (1,417)                           |                                               | 8,706        |
| Ending balance                                                   | \$ (22,372)                                                 | \$ (1,417)                        | \$                                            | \$ (23,789)  |

|                                                            | <b>Foreign<br/>currency<br/>translation<br/>adjustments</b> | <b>Derivative<br/>adjustments</b> | <b>Unrealized<br/>gain on<br/>investments</b> | <b>Total</b> |
|------------------------------------------------------------|-------------------------------------------------------------|-----------------------------------|-----------------------------------------------|--------------|
| <b>Three Months Ended June 30, 2014</b>                    |                                                             |                                   |                                               |              |
| Beginning balance                                          | \$ (50,707)                                                 | \$ 4,789                          | \$ 957                                        | \$ (44,961)  |
| Other comprehensive income (loss) before reclassifications | (25,955)                                                    | 8,002                             | 925                                           | (17,028)     |

|                                                                  |             |           |         |             |
|------------------------------------------------------------------|-------------|-----------|---------|-------------|
| Amounts reclassified from accumulated other comprehensive income |             | (2,647)   | (1,882) | (4,529)     |
| Net current-period other comprehensive income (loss)             | (25,955)    | 5,355     | (957)   | (21,557)    |
| Ending balance                                                   | \$ (76,662) | \$ 10,144 | \$      | \$ (66,518) |

**Table of Contents****MagnaChip Semiconductor Corporation and Subsidiaries****Notes to Consolidated Financial Statements (Continued)****(Unaudited; tabular dollars in thousands, except share data)**

Changes in accumulated other comprehensive loss for the six months ended June 30, 2015 and 2014 are as follows:

| <b>Six Months Ended June 30, 2015</b>                            | <b>Foreign<br/>currency<br/>translation<br/>adjustments</b> | <b>Derivative<br/>adjustments</b> | <b>Unrealized<br/>gain on<br/>investments</b> | <b>Total</b> |
|------------------------------------------------------------------|-------------------------------------------------------------|-----------------------------------|-----------------------------------------------|--------------|
| Beginning balance                                                | \$ (35,551)                                                 | \$ 485                            | \$                                            | \$ (35,066)  |
| Other comprehensive income (loss) before reclassifications       | 13,179                                                      | (1,417)                           |                                               | 11,762       |
| Amounts reclassified from accumulated other comprehensive income |                                                             | (485)                             |                                               | (485)        |
| Net current-period other comprehensive income (loss)             | 13,179                                                      | (1,902)                           |                                               | 11,277       |
| Ending balance                                                   | \$ (22,372)                                                 | \$ (1,417)                        | \$                                            | \$ (23,789)  |

| <b>Six Months Ended June 30, 2014</b>                            | <b>Foreign<br/>currency<br/>translation<br/>adjustments</b> | <b>Derivative<br/>adjustments</b> | <b>Unrealized<br/>gain on<br/>investments</b> | <b>Total</b> |
|------------------------------------------------------------------|-------------------------------------------------------------|-----------------------------------|-----------------------------------------------|--------------|
| Beginning balance                                                | \$ (57,326)                                                 | \$ 6,587                          | \$ 681                                        | \$ (50,058)  |
| Other comprehensive income (loss) before reclassifications       | (19,336)                                                    | 6,201                             | 1,201                                         | (11,934)     |
| Amounts reclassified from accumulated other comprehensive income |                                                             | (2,644)                           | (1,882)                                       | (4,526)      |
| Net current-period other comprehensive income (loss)             | (19,336)                                                    | 3,557                             | (681)                                         | (16,460)     |
| Ending balance                                                   | \$ (76,662)                                                 | \$ 10,144                         | \$                                            | \$ (66,518)  |

**Table of Contents****MagnaChip Semiconductor Corporation and Subsidiaries****Notes to Consolidated Financial Statements (Continued)****(Unaudited; tabular dollars in thousands, except share data)****15. Earnings (Loss) per Share**

The following table illustrates the computation of basic and diluted earnings (loss) per common share:

|                                           | <b>Three Months Ended</b> |                          |
|-------------------------------------------|---------------------------|--------------------------|
|                                           | <b>June 30,<br/>2015</b>  | <b>June 30,<br/>2014</b> |
| Net income (loss)                         | \$ (30,626)               | \$ 15,010                |
| Weighted average common stock outstanding |                           |                          |
| Basic                                     | 34,092,402                | 34,056,359               |
| Diluted                                   | 34,092,402                | 35,177,915               |
| Earnings (loss) per share                 |                           |                          |
| Basic                                     | \$ (0.90)                 | \$ 0.44                  |
| Diluted                                   | \$ (0.90)                 | \$ 0.43                  |

|                                           | <b>Six Months Ended</b>  |                          |
|-------------------------------------------|--------------------------|--------------------------|
|                                           | <b>June 30,<br/>2015</b> | <b>June 30,<br/>2014</b> |
| Net loss                                  | \$ (50,655)              | \$ (6,595)               |
| Weighted average common stock outstanding |                          |                          |
| Basic                                     | 34,074,534               | 34,054,626               |
| Diluted                                   | 34,074,534               | 34,054,626               |
| Loss per share                            |                          |                          |
| Basic                                     | \$ (1.49)                | \$ (0.19)                |
| Diluted                                   | \$ (1.49)                | \$ (0.19)                |

The following outstanding instruments were excluded from the computation of diluted loss per share, as they have an anti-dilutive effect on the calculation:

|                        | <b>Three Months Ended</b> |                          | <b>Six Months Ended</b>  |                          |
|------------------------|---------------------------|--------------------------|--------------------------|--------------------------|
|                        | <b>June 30,<br/>2015</b>  | <b>June 30,<br/>2014</b> | <b>June 30,<br/>2015</b> | <b>June 30,<br/>2014</b> |
| Options                | 3,341,700                 | 880,267                  | 3,341,700                | 3,166,145                |
| Warrants               |                           | 1,425,129                |                          | 1,425,129                |
| Restricted Stock Units | 129,962                   |                          | 129,962                  |                          |



**Table of Contents**

**MagnaChip Semiconductor Corporation and Subsidiaries**

**Notes to Consolidated Financial Statements (Continued)**

**(Unaudited; tabular dollars in thousands, except share data)**

***Rights Plan***

On March 5, 2015, the Board of Directors of the Company, authorized and declared a dividend of one preferred stock purchase right (a Right and collectively, the Rights) for each share of the Company's common stock, par value \$0.01 per share, outstanding at the close of business on March 16, 2015. Each Right, once exercisable, will entitle the registered holder to purchase from the Company one one-thousandth of a share of Series A Junior Participating Preferred Stock, par value \$0.01 per share, at a purchase price of \$24, subject to adjustment (the Purchase Price). The Rights are not presently exercisable and remain attached to the shares of common stock unless and until the occurrence of the earlier of the following (the Distribution Date): (i) the tenth day after the public announcement or disclosure by the Company or any person or group of affiliated or associated persons that any person or group of affiliated or associated persons has become an Acquiring Person by obtaining beneficial ownership of 10% (or 20% in the case of a passive institutional investor, which is defined generally as any person who has reported beneficial ownership of shares of common stock on Schedule 13G under the Securities Exchange Act of 1934 (the Exchange Act)) or more of the Company's outstanding common stock, subject to certain exceptions; or (ii) the tenth business day (or such later date as the Company's Board of Directors may designate before a person or group of affiliated or associated persons becomes an Acquiring Person) after the commencement of, or first public announcement of the intent of any person to commence, a tender or exchange offer by any person or group of affiliated or associated persons, which would, if consummated, result in such person or group becoming an Acquiring Person. The Board of Directors may redeem all of the Rights for \$0.001 per Right at any time before any person or group of affiliated or associated persons becomes an Acquiring Person. In addition, at any time on or after any person or group of affiliated or associated persons becomes an Acquiring Person (but before any person or group of affiliated or associated persons becomes the owner of 50% or more of the Company's outstanding common stock), the Board of Directors may exchange all or part of the Rights (other than the Rights beneficially owned by the Acquiring Person and certain affiliated persons) for shares of common stock at an exchange ratio of one share of common stock per Right. The Rights will expire at the close of business on March 5, 2016, unless redeemed or exchanged prior to that time.

If any person or group of affiliated or associated persons becomes an Acquiring Person, then, after the Distribution Date, each Right (other than Rights beneficially owned by the Acquiring Person and certain affiliated persons or transferees thereof) will entitle the holder to purchase, for the Purchase Price, a number of shares of common stock having a market value of twice the Purchase Price. Alternatively, if, after any person or group of affiliated or associated persons becomes an Acquiring Person, (i) the Company is involved in a merger or other business combination in which the Company is not the surviving corporation or its common stock is changed into or exchanged for other securities or assets; or (ii) the Company or one or more of its subsidiaries sells or otherwise transfers assets or earning power aggregating more than 50% of the assets or earning power of the Company and its subsidiaries, taken as a whole, then each Right will entitle the holder to purchase, for the Purchase Price, a number of shares of common stock of the other party to such business combination or sale (or in certain circumstances, an affiliate) having a market value of twice the Purchase Price.

**16. Commitments and Contingencies**

***Securities Class Action Complaints***

On March 12, 2014, a purported class action was filed against the Company and certain of the Company's now-former officers. On April 21, 2015, a related purported class action lawsuit was filed against the Company, certain of the Company's current directors and former and now-former officers, a shareholder of the Company, and certain financial firms that acted as underwriters of the Company's public stock offerings. On June 15, 2015, these two class action lawsuits were consolidated. On June 26, 2015, an amended complaint was filed in the consolidated action, against the Company, certain of the Company's current directors and former officers, a shareholder of the Company, and certain financial firms that acted as underwriters of the Company's public stock offerings on behalf of a putative class consisting of all persons other than the defendants who purchased or acquired the Company's securities between February 1, 2012 and February 12, 2015 and a putative subclass consisting of all purchasers of the Company's common stock pursuant to or traceable to a shelf registration statement and prospectus issued in connection with the Company's February 6, 2013 public stock offering. The consolidated amended complaint asserts claims on behalf of the putative class for (i) alleged violations of Section 10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder by the Company and certain of the Company's current directors and former officers, (ii) alleged violations of Section 20(a) of the Exchange Act by certain of the Company's current directors and former officers, and (iii) alleged violations of Sections 20(a) and 20(A) of the Exchange Act by a shareholder. The consolidated amended complaint also asserts claims on behalf the subclass for (i) alleged violations of Section 11 of the Securities Act of 1933 (the "Securities Act") by the Company, certain of the Company's current directors and former officers, and certain financial firms that acted as underwriters of the Company's public stock offerings, (ii) alleged violations of Section 12 of the Securities Act by the Company, certain of the Company's current directors and former officers, a shareholder of the Company, and certain financial firms that acted as underwriters of the Company's public stock offerings, (iii) alleged violations of Section 15 of the Securities Act by

**Table of Contents**

**MagnaChip Semiconductor Corporation and Subsidiaries**

**Notes to Consolidated Financial Statements (Continued)**

**(Unaudited; tabular dollars in thousands, except share data)**

the Company, certain of the Company's former officers, and a shareholder of the Company. The consolidated action, *Thomas et al., v. MagnaChip Semiconductor Corp., et al.*, No. 3:14-cv-1160, is pending in the Northern District of California. At this time, the Company is unable to estimate any reasonably possible loss, or range of reasonably possible losses, with respect to the matters described above.

***SEC Enforcement Staff Review***

In March 2014, the Company voluntarily reported to the SEC that the Company's Audit Committee (the "Audit Committee") had determined that the Company incorrectly recognized revenue on certain transactions and as a result would restate its financial statements, and that the Audit Committee had commenced the Independent Investigation. Over the course of 2014 and the first two quarters of 2015, the Company voluntarily produced documents to the SEC regarding the various accounting issues identified during the Independent Investigation, and whether the Company's hiring of an accountant from the Company's independent registered public accounting firm impacted that accounting firm's independence. On July 22, 2014, the Staff of the SEC's Division of Enforcement obtained a Formal Order of Investigation. On March 12, 2015, the SEC issued a subpoena for documents to the Company in connection with its investigation. The Company will continue to cooperate with the SEC in this investigation. At this time, the Company is unable to estimate any reasonably possible loss, or range of reasonably possible losses, with respect to the matters described above.

***Shareholder Derivative Complaints***

A shareholder derivative action, styled *Hemmingson et al. v. Elkins et al.*, Case No. 1-15-cv-278614, was filed in the Superior Court of the State of California in and for Santa Clara County on March 25, 2015, naming as defendants certain of the Company's current directors and former and now-former officers, as well as a shareholder of the Company, and naming the Company as a nominal defendant. The complaint in this action asserts claims for (i) alleged breaches of fiduciary duty by certain of the Company's current directors and former and now-former officers for purportedly knowingly failing to maintain adequate internal controls over its accounting and reporting functions and disseminating to stockholders certain alleged materially false and misleading statements, (ii) alleged breaches of fiduciary duty by certain of the Company's current directors and a current shareholder of the Company for purported insider trading, and (iii) alleged unjust enrichment by a shareholder of the Company for purported insider trading. On May 13, 2015, the court so ordered a stipulation entered into by certain of the parties, agreeing to stay the litigation until *Thomas et al., v. MagnaChip Semiconductor Corp., et al.*, No. 3:14-cv-1160 and *Okla. Police Pension & Retirement Sys. v. MagnaChip Semiconductor Corp., et al.*, No. 3:15-cv-01797 are resolved, unless the stay is lifted earlier.

On June 1, 2015, a shareholder derivative action as styled as *Bushansky v. Norby, et al.*, No. 1-15-cv-281289, was filed in the Superior Court of the State of California, Santa Clara County. The complaint names as defendants certain of the Company's current directors and former officers, and a shareholder of the Company, with the Company being named as a nominal defendant. The complaint asserts claims for (i) alleged breaches of fiduciary duties by certain of the Company's current directors and former officers for knowingly failing to maintain adequate internal controls over

the Company's accounting and reporting functions and disseminating to shareholders certain alleged materially false and misleading statements; and (ii) alleged aiding and abetting of such breaches of fiduciary duties by all defendants. At this time, the Company is unable to estimate any reasonably possible loss, or range of reasonably possible losses, with respect to the matters described above.

In addition, by letter dated May 28, 2015, a purported shareholder demanded to inspect certain of the Company's books and records, pursuant to Section 220 of the General Corporation Law of the State of Delaware (8 Del. C. § 220). The demand's stated purpose is to investigate alleged breaches of fiduciary duty by certain of the Company's current and former directors, officers, and senior management and otherwise evaluate whether to initiate a derivative action on the Company's behalf.

**Table of Contents**

**FORWARD LOOKING STATEMENTS**

The following Management's Discussion and Analysis of Financial Condition and Results of Operations contains forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended, and Section 27A of the Securities Act of 1933, as amended, that involve risks and uncertainties. Forward-looking statements give our current expectations and projections relating to our financial condition, results of operations, plans, objectives, future performance and business. You can identify these statements by the fact that they do not relate strictly to historical or current facts. These statements may include words such as anticipate, estimate, expect, project, intend, plan, believe and other words and terms of similar meaning in connection with any discussion of the timing or nature of future operating or financial performance or other events. All statements other than statements of historical facts included in this report that address activities, events or developments that we expect, believe or anticipate will or may occur in the future are forward-looking statements.

These forward-looking statements are largely based on our expectations and beliefs concerning future events, which reflect estimates and assumptions made by our management. These estimates and assumptions reflect our best judgment based on currently known market conditions and other factors relating to our operations and business environment, all of which are difficult to predict and many of which are beyond our control. Although we believe our estimates and assumptions to be reasonable, they are inherently uncertain and involve a number of risks and uncertainties that are beyond our control. In addition, management's assumptions about future events may prove to be inaccurate. Management cautions all readers that the forward-looking statements contained in this report are not guarantees of future performance, and we cannot assure any reader that those statements will be realized or the forward-looking events and circumstances will occur. Actual results may differ materially from those anticipated or implied in the forward-looking statements due to the factors listed in this section and in Part I: Item 1A. Risk Factors in our annual report on Form 10-K for the fiscal year ended December 31, 2014.

All forward-looking statements speak only as of the date of this report. We do not intend to publicly update or revise any forward-looking statements as a result of new information or future events or otherwise, except as required by law. These cautionary statements qualify all forward-looking statements attributable to us or persons acting on our behalf.

Statements made in this Quarterly Report on Form 10-Q (this Report), unless the context otherwise requires, that include the use of the terms we, us, our and MagnaChip refer to MagnaChip Semiconductor Corporation and its consolidated subsidiaries. The term Korea refers to the Republic of Korea or South Korea.

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**Table of Contents**

**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**

*The following discussion and analysis should be read in conjunction with the unaudited consolidated financial statements and the related notes included elsewhere in this Report. This discussion and analysis contains, in addition to historical information, forward-looking statements that include risks and uncertainties. Our actual results may differ materially from those anticipated in these forward-looking statements as a result of certain factors, including those set forth under the heading "Risk Factors" and elsewhere in this Report.*

**Overview**

We are a Korea-based designer and manufacturer of analog and mixed-signal semiconductor products for consumer, computing, communication, industrial, automotive and IoT applications. We provide technology platforms for analog, mixed-signal, power, high voltage, non-volatile memory, and RF applications. We have a proven record with a 30-year operating history, large portfolio of 2,669 registered novel patents and 159 pending novel patent applications and extensive engineering and manufacturing process expertise.

We previously reported our results of operations under one operating segment. During the second quarter of 2015, organizational changes were made to (i) realign our businesses and organizational structure and (ii) streamline and consolidate certain business processes to achieve greater operating efficiencies. In furtherance of these objectives, we combined our business lines of Display Solutions and Power Solutions into a new segment called Standard Products Group. Beginning in the second quarter of 2015, we report our financial results in two operating segments: Semiconductor Manufacturing Services and Standard Products Group. Our chief operating decision maker is our Chief Executive Officer who allocates resources and assesses performance of the business and other activities based on gross profit. The two newly established operating segments will be managed prospectively and have no effect on our historical consolidated results of operations. All prior period amounts related to the segment change have been retrospectively reclassified to conform to the new presentation.

Our Semiconductor Manufacturing Services segment provides specialty analog and mixed-signal foundry services mainly for fabless and IDM semiconductor companies that primarily serve consumer, computing, communication, industrial, automotive and IoT applications. Our Standard Products Group includes our Display Solutions and Power Solutions business lines. Our Display Solutions products provide flat panel display solutions to major suppliers of large and small flat panel displays and include our sensor products for mobile applications and industrial applications. Our Power Solutions products include discrete and integrated circuit solutions for power management in consumer, computing, communication and industrial applications.

Our wide variety of analog and mixed-signal semiconductor products and manufacturing services combined with our mature technology platform allow us to address multiple high-growth end markets and to rapidly develop and introduce new products and services in response to market demands. Our design center and substantial manufacturing operations in Korea place us at the core of the global electronics device supply chain. We believe this enables us to quickly and efficiently respond to our customers' needs and allows us to better serve and capture additional demand from existing and new customers.

To maintain and increase our profitability, we must accurately forecast trends in demand for electronics devices that incorporate semiconductor products we produce. We must understand our customers' needs as well as the likely end market trends and demand in the markets they serve. We must balance the likely manufacturing utilization demand of our product businesses and foundry business to optimize our capacity utilization. We must also invest in relevant research and development activities and manufacturing capacity and purchase necessary materials on a timely basis to meet our customers' demand while maintaining our target margins and cash flow.

The semiconductor markets in which we participate are highly competitive. The prices of our products tend to decrease regularly over their useful lives, and such price decreases can be significant as new generations of products are introduced by us or our competitors. We strive to offset the impact of declining selling prices for existing products through cost reductions and the introduction of new products that command selling prices above the average selling price of our existing products. In addition, we seek to manage our inventories and manufacturing capacity so as to mitigate the risk of losses from product obsolescence.

Demand for our products and services is driven by overall demand for consumer, communication and computing products and can be adversely affected by periods of weak consumer and enterprise spending or by market share losses by our customers. In order to mitigate the impact of market volatility on our business, we are diversifying our portfolio of products, customers, and target applications. We also expect that new competitors will emerge in these markets that may place increased pressure on the pricing for our products and services. While we believe we are well positioned competitively to compete in these markets and against these new competitors as a result of our long operating history, existing manufacturing capacity and our Korea-based operations, if we are not effective in competing in these markets our operating results may be adversely affected.

Within our Semiconductor Manufacturing Services, net sales are driven by customers' decisions on which manufacturing services provider to use for a particular product. Most of our Semiconductor Manufacturing Services customers are fabless, while some are IDM customers. A customer will often have more than one supplier of manufacturing services. In any given period, our net sales depend heavily upon the end-market demand for the goods in which the products we manufacture for customers are used, the inventory levels maintained by our customers and in some cases, allocation of demand for manufacturing services among selected qualified suppliers.

## **Table of Contents**

Within our Standard Products Group, net sales are driven by design wins in which we are selected by an electronics original equipment manufacturer (OEM) or other potential customer to supply its demand for a particular product. A customer will often have more than one supplier designed in to multi-source components for a particular product line. Once we have design wins and the products enter into mass production, we often specify the pricing of a particular product for a set period of time, with periodic discussions and renegotiations of pricing with our customers. In any given period, our net sales depend heavily upon the end-market demand for the goods in which our products are used, the inventory levels maintained by our customers and in some cases, allocation of demand for components for a particular product among selected qualified suppliers.

In contrast to fabless semiconductor companies, our internal manufacturing capacity provides us with greater control over manufacturing costs and the ability to implement process and production improvements which can favorably impact gross profit margins. Our internal manufacturing capacity also allows for better control over delivery schedules, improved consistency over product quality and reliability and improved ability to protect intellectual property from misappropriation. However, having internal manufacturing capacity exposes us to the risk of under-utilization of manufacturing capacity that results in lower gross profit margins, particularly during downturns in the semiconductor industry.

Our products and services require investments in capital equipment. Analog and mixed-signal manufacturing facilities and processes are typically distinguished by the design and process implementation expertise rather than the use of the most advanced equipment. These processes also tend to migrate more slowly to smaller geometries due to technological barriers and increased costs. For example, some of our products use high-voltage technology that requires larger geometries and that may not migrate to smaller geometries for several years, if at all. Additionally, the performance of many of our products is not necessarily dependent on geometry. As a result, our manufacturing base and strategy do not require substantial investment in leading edge process equipment, allowing us to utilize our facilities and equipment over an extended period of time with moderate required capital investments. Generally, incremental capacity expansions in our business of the market result in more moderate industry capacity expansion as compared to leading edge processes. As a result, this market, and we, specifically, are less likely to experience significant industry overcapacity, which can cause product prices to decline significantly. In general, we seek to invest in manufacturing capacity that can be used for multiple high-value applications over an extended period of time. We believe this capital investment strategy enables us to optimize our capital investments and facilitates deeper and more diversified product and service offerings.

Our success going forward will depend upon our ability to adapt to future challenges such as the emergence of new competitors for our products and services or the consolidation of current competitors. Additionally, we must innovate to remain ahead of, or at least rapidly adapt to, technological breakthroughs that may lead to a significant change in the technology necessary to deliver our products and services. We believe that our established relationships and close collaboration with leading customers enhance our awareness of new product opportunities, market and technology trends and improve our ability to adapt and grow successfully. In our Semiconductor Manufacturing Services, we strive to maintain competitiveness by offering high-value added processes, high-flexibility and excellent service by tailoring existing standard processes to meet customers' design needs and porting customers' own process technologies into our fabrication facilities.

## ***Restatement***

In January 2014, our Audit Committee commenced an internal investigation that resulted in the restatement of certain financial statements for prior periods (the *Restatement*). As a result of the Restatement, we have incurred substantial external accounting, legal and other related costs associated with the Restatement and certain litigation and other regulatory investigations and actions related thereto. We incurred Restatement related costs of \$12.0 million for the

six months ended June 30, 2015, compared to \$13.3 million in the six months ended June 30, 2014. We expect to continue to incur substantial Restatement related costs for the remainder of 2015 related to ongoing litigation and regulatory investigations, which could have a material adverse effect on our operating results and liquidity for the foreseeable future.

### ***Segments***

We previously reported our results of operations under one operating segment. During the second quarter of 2015, organizational changes were made to (i) realign our businesses and organizational structure and (ii) streamline and consolidate certain business processes to achieve greater operating efficiencies. Accordingly, we combined our business lines of Display Solutions and Power Solutions into a new segment called Standard Products Group. Beginning in the second quarter of 2015, we report our financial results in two operating segments: Semiconductor Manufacturing Services and Standard Products Group. We have identified these segments based on how we allocate resources and assess our performance.

***Semiconductor Manufacturing Services:*** Our Semiconductor Manufacturing Services segment provides specialty analog and mixed-signal foundry services to fabless semiconductor companies and IDMs that serve consumer, computing, communication, industrial, automotive and IoT applications. We manufacture wafers based on our customers' product designs. We do not market

## **Table of Contents**

these products directly to end customers but rather supply manufactured wafers and products to our customers to market to their end customers. We offer approximately 479 process flows to our manufacturing services customers. We also often partner with key customers to jointly develop or customize specialized processes that enable our customers to improve their products and allow us to develop unique manufacturing expertise. Our manufacturing services are targeted at customers who require differentiated, specialty analog and mixed-signal process technologies such as high voltage complementary metal-oxide-semiconductor (CMOS), embedded memory or bipolar-CMOS-DMOS (BCD). These customers typically serve the consumer, computing, communication, industrial, automotive and IoT applications. Our Semiconductor Manufacturing Services business represented 47.0% and 54.2% of our net sales for the six months ended June 30, 2015 and June 30, 2014, respectively. Gross profit from our Semiconductor Manufacturing Services business was \$32.6 million and \$40.7 million for the six months ended June 30, 2015 and June 30, 2014, respectively.

***Standard Products Group:*** Our Standard Products Group includes our Display Solutions and Power Solutions business lines. Our Display Solutions products include source and gate drivers and timing controllers that cover a wide range of flat panel displays used in ultra high definition (UHD), high definition (HD), light emitting diode (LED), 3D and OLED televisions and displays, notebooks and mobile communications and entertainment devices. Our Display Solutions support the industry's most advanced display technologies, such as active matrix organic light emitting diodes (AMOLEDs), and low temperature polysilicons (LTPS), as well as high-volume display technologies such as thin film transistors (TFT). We provide a full range of intelligent sensor product families featuring 0.18 micron analog and mixed-signal technology with low power consumption. Our sensor families target the growing market for applications ranging from smartphone, tablet PC and other consumer electronics to industrial devices. Our Power Solutions business line produces power management semiconductor products including discrete and integrated circuit solutions for power management in high-volume consumer applications. These products include MOSFETs, insulated-gate bipolar transistors (IGBTs), power modules, AC-DC converters, DC-DC converters, LED drivers, switching regulators and linear regulators for a range of devices, including televisions, smartphones, mobile phones, desktop PCs, notebooks, tablet PCs, other consumer electronics, and industrial applications such as power suppliers, LED lighting, motor control and home appliances. Our Standard Products Group, which includes our Display Solutions and Power Solutions business lines, represented 53.0% and 45.7% of our net sales for the six months ended June 30, 2015 and June 30, 2014, respectively. Gross profit from our Standard Products Group was \$37.4 million and \$34.8 million for the six months ended June 30, 2015 and June 30, 2014, respectively.

## **Explanation and Reconciliation of Non-US GAAP Measures**

### ***Adjusted EBITDA and Adjusted Net Income***

We use the terms Adjusted EBITDA and Adjusted Net Income throughout this Report. Adjusted EBITDA, as we define it, is a non-US GAAP measure. We define Adjusted EBITDA for the periods indicated as net income (loss), adjusted to exclude (i) depreciation and amortization, (ii) interest expense, net, (iii) income tax expenses (benefits), (iv) equity-based compensation expense, (v) foreign currency loss (gain), net, (vi) derivative valuation loss, net and (vii) restatement related expenses.

See the footnotes to the table below for further information regarding these items. We present Adjusted EBITDA as a supplemental measure of our performance because:

Adjusted EBITDA eliminates the impact of a number of items that may be either one time or recurring items that we do not consider to be indicative of our core ongoing operating performance;

we believe that Adjusted EBITDA is an enterprise level performance measure commonly reported and widely used by analysts and investors in our industry;

our investor and analyst presentations will include Adjusted EBITDA; and

we believe that Adjusted EBITDA provides investors with a more consistent measurement of period to period performance of our core operations, as well as a comparison of our operating performance to that of other companies in our industry.

We use Adjusted EBITDA in a number of ways, including:

for planning purposes, including the preparation of our annual operating budget;

to evaluate the effectiveness of our enterprise level business strategies;

in communications with our Board of Directors concerning our consolidated financial performance; and

in certain of our compensation plans as a performance measure for determining incentive compensation payments.

**Table of Contents**

We encourage you to evaluate each adjustment and the reasons we consider them appropriate. In evaluating Adjusted EBITDA, you should be aware that in the future we may incur expenses similar to the adjustments in this presentation. Adjusted EBITDA is not a measure defined in accordance with US GAAP and should not be construed as an alternative to income from continuing operations, cash flows from operating activities or net income (loss), as determined in accordance with US GAAP. A reconciliation of net income (loss) to Adjusted EBITDA is as follows:

|                                      | <b>Three Months Ended</b> |                      | <b>Six Months Ended</b>                 |                                       |
|--------------------------------------|---------------------------|----------------------|-----------------------------------------|---------------------------------------|
|                                      | <b>June 30, 2015</b>      | <b>June 30, 2015</b> | <b>Three Months Ended June 30, 2014</b> | <b>Six Months Ended June 30, 2014</b> |
|                                      | <b>(In millions)</b>      |                      |                                         |                                       |
| Net income (loss)                    | \$ (30.6)                 | \$ (50.7)            | \$ 15.0                                 | \$ (6.6)                              |
| Adjustments:                         |                           |                      |                                         |                                       |
| Depreciation and amortization        | 6.8                       | 13.7                 | 7.8                                     | 15.1                                  |
| Interest expense, net                | 3.9                       | 8.0                  | 4.0                                     | 8.1                                   |
| Income tax expenses (benefits)       | (0.6)                     | 0.5                  | 0.7                                     | 1.5                                   |
| Equity-based compensation expense(a) | 1.8                       | 2.0                  | 0.5                                     | 1.1                                   |
| Foreign currency loss (gain), net(b) | 12.3                      | 15.5                 | (38.4)                                  | (29.0)                                |
| Derivative valuation loss, net(c)    | 0.3                       | 0.3                  |                                         |                                       |
| Restatement related expenses(d)      | 5.2                       | 11.4                 | 8.5                                     | 13.3                                  |
| Adjusted EBITDA                      | \$ (0.9)                  | \$ 0.7               | \$ (2.0)                                | \$ 3.4                                |

- (a) This adjustment eliminates the impact of non-cash equity-based compensation expenses. Although we expect to incur non-cash equity-based compensation expenses in the future, we believe that analysts and investors will find it helpful to review our operating performance without the effects of these non-cash expenses, as supplemental information.
- (b) This adjustment eliminates the impact of non-cash foreign currency translation associated with intercompany debt obligations and foreign currency denominated receivables and payables, as well as the cash impact of foreign currency transaction gains or losses on collection of such receivables and payment of such payables. Although we expect to incur foreign currency translation gains or losses in the future, we believe that analysts and investors will find it helpful to review our operating performance without the effects of these primarily non-cash gains or losses, as supplemental information.
- (c) This adjustment eliminates the impact of gain or loss recognized in income on derivatives, which represents hedge ineffectiveness or derivatives value changes excluded from the risk being hedged. We enter into derivative transactions to mitigate foreign exchange risks. As our derivative transactions are limited to a certain portion of our expected cash flows denominated in U.S. dollars, and we do not enter into derivative transactions for trading or speculative purposes, we do not believe that these charges or gains are indicative of our core operating performance.
- (d) This adjustment eliminates expenses incurred in connection with the Audit Committee's independent investigation and related restatement and litigation, primarily comprised of legal and consulting fees. Partially offsetting the restatement related expenses was proceeds from an insurance claim for defense costs. This amount does not include any allocation of internal costs related to the restatement.

Adjusted EBITDA has limitations as an analytical tool, and you should not consider it in isolation, or as a substitute for analysis of our results as reported under US GAAP. Some of these limitations are:

Adjusted EBITDA does not reflect our cash expenditures, or future requirements, for capital expenditures or contractual commitments;

Adjusted EBITDA does not reflect changes in, or cash requirements for, our working capital needs;

Adjusted EBITDA does not reflect the interest expense, or the cash requirements necessary to service interest or principal payments, on our debt;

although depreciation and amortization are non-cash charges, the assets being depreciated and amortized will often have to be replaced in the future, and Adjusted EBITDA does not reflect any cash requirements for such replacements;

Adjusted EBITDA does not consider the potentially dilutive impact of issuing equity-based compensation to our management team and employees;

Adjusted EBITDA does not reflect the costs of holding certain assets and liabilities in foreign currencies; and

other companies in our industry may calculate Adjusted EBITDA differently than we do, limiting its usefulness as a comparative measure.

**Table of Contents**

Because of these limitations, Adjusted EBITDA should not be considered as a measure of discretionary cash available to us to invest in the growth of our business. We compensate for these limitations by relying primarily on our US GAAP results and using Adjusted EBITDA only supplementally.

We present Adjusted Net Income as a further supplemental measure of our performance. We prepare Adjusted Net Income by adjusting net income (loss) to eliminate the impact of a number of non-cash expenses and other items that may be either one time or recurring that we do not consider to be indicative of our core ongoing operating performance. We believe that Adjusted Net Income is particularly useful because it reflects the impact of our asset base and capital structure on our operating performance. We present Adjusted Net Income for a number of reasons, including:

we use Adjusted Net Income in communications with our Board of Directors concerning our consolidated financial performance;

we believe that Adjusted Net Income is an enterprise level performance measure commonly reported and widely used by analysts and investors in our industry; and

our investor and analyst presentations may include Adjusted Net Income.

Adjusted Net Income is not a measure defined in accordance with US GAAP and should not be construed as an alternative to income from continuing operations, cash flows from operating activities or net income (loss), as determined in accordance with US GAAP. We encourage you to evaluate each adjustment and the reasons we consider them appropriate. Other companies in our industry may calculate Adjusted Net Income differently than we do, limiting its usefulness as a comparative measure. In addition, in evaluating Adjusted Net Income, you should be aware that in the future we may incur expenses similar to the adjustments in this presentation. We define Adjusted Net Income for the periods indicated as net income (loss), adjusted to exclude (i) amortization of intangibles, (ii) equity-based compensation expense, (iii) foreign currency loss (gain), net, (iv) derivative valuation loss, net and (v) restatement related expenses.

The following table summarizes the adjustments to net loss that we make in order to calculate Adjusted Net Income (Loss) for the periods indicated:

|                                      | <b>Three Months Ended</b> |                      | <b>Six Months Ended</b>                 |                                       |
|--------------------------------------|---------------------------|----------------------|-----------------------------------------|---------------------------------------|
|                                      | <b>June 30, 2015</b>      | <b>June 30, 2015</b> | <b>Three Months Ended June 30, 2014</b> | <b>Six Months Ended June 30, 2014</b> |
|                                      | <b>(In millions)</b>      |                      |                                         |                                       |
| Net income (loss)                    | \$ (30.6)                 | \$ (50.7)            | \$ 15.0                                 | \$ (6.6)                              |
| Adjustments:                         |                           |                      |                                         |                                       |
| Amortization of intangibles(a)       |                           |                      | 0.4                                     | 0.7                                   |
| Equity-based compensation expense(b) | 1.8                       | 2.0                  | 0.5                                     | 1.1                                   |
| Foreign currency loss (gain), net(c) | 12.3                      | 15.5                 | (38.4)                                  | (29.0)                                |

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|                                   |           |           |           |           |
|-----------------------------------|-----------|-----------|-----------|-----------|
| Derivative valuation loss, net(d) | 0.3       | 0.3       |           |           |
| Restatement related expenses(e)   | 5.2       | 11.4      | 8.5       | 13.3      |
| Adjusted Net Loss                 | \$ (11.1) | \$ (21.5) | \$ (14.1) | \$ (20.5) |

- (a) This adjustment eliminates the non-cash impact of amortization expense for intangible assets created as a result from the application of fresh-start accounting in connection with the reorganization proceedings and the purchase accounting treatment of a subsequent acquisition. We do not believe these non-cash amortization expenses for intangibles are indicative of our core ongoing operating performance because the assets would not have been capitalized on our balance sheet but for the application of purchase accounting or fresh-start accounting, as applicable.
- (b) This adjustment eliminates the impact of non-cash equity-based compensation expenses. Although we expect to incur non-cash equity-based compensation expenses in the future, we believe that analysts and investors will find it helpful to review our operating performance without the effects of these non-cash expenses, as supplemental information.
- (c) This adjustment eliminates the impact of non-cash foreign currency translation associated with intercompany debt obligations and foreign currency denominated receivables and payables, as well as the cash impact of foreign currency transaction gains or losses on collection of such receivables and payment of such payables. Although we expect to incur foreign currency translation gains or losses in the future, we believe that analysts and investors will find it helpful to review our operating performance without the effects of these primarily non-cash gains or losses, as supplemental information.
- (d) This adjustment eliminates the impact of gain or loss recognized in income on derivatives, which represents hedge ineffectiveness or derivatives value changes excluded from the risk being hedged. We enter into derivative transactions to mitigate foreign exchange risks. As our derivative transactions are limited to a certain portion of our expected cash flows denominated in U.S. dollars, and we do not enter into derivative transactions for trading or speculative purposes, we do not believe that these charges or gains are indicative of our core operating performance.

## **Table of Contents**

- (e) This adjustment eliminates expenses incurred in connection with the Audit Committee's independent investigation and related restatement and litigation, primarily comprised of legal and consulting fees. Partially offsetting the restatement related expenses was proceeds from an insurance claim for defense costs. This amount does not include any allocation of internal costs related to the restatement.

Adjusted Net Income has limitations as an analytical tool, and you should not consider it in isolation, or as a substitute for analysis of our results as reported under US GAAP. Some of these limitations are:

Adjusted Net Income does not reflect our cash expenditures, or future requirements, for capital expenditures or contractual commitments;

Adjusted Net Income does not reflect changes in, or cash requirements for, our working capital needs;

Adjusted Net Income does not consider the potentially dilutive impact of issuing equity-based compensation to our management team and employees;

Adjusted Net Income does not reflect the costs of holding certain assets and liabilities in foreign currencies; and

other companies in our industry may calculate Adjusted Net Income differently than we do, limiting its usefulness as a comparative measure.

Because of these limitations, Adjusted Net Income should not be considered as a measure of discretionary cash available to us to invest in the growth of our business. We compensate for these limitations by relying primarily on our US GAAP results and using Adjusted Net Income only supplementally.

## **Factors Affecting Our Results of Operations**

**Net Sales.** We derive virtually all of our sales (net of sales returns and allowances) from two segments: Semiconductor Manufacturing Services and Standard Products Group. Our product inventory is primarily located in Korea and is available for drop shipment globally. Outside of Korea, we maintain limited product inventory, and our sales representatives generally relay orders to our factories in Korea for fulfillment. We have strategically located our sales and technical support offices near concentrations of major customers. Our sales offices are located in Korea, the United States, Japan and Greater China. Our network of authorized agents and distributors consists of agents in the United States and Europe and distributors and agents in the Asia Pacific region. Our net sales from All other consist principally of the disposal of waste materials.

We recognize revenue when risk and reward of ownership pass to the customer either upon shipment, upon product delivery at the customer's location or upon customer acceptance, depending on the terms of the arrangement. For the six months ended June 30, 2015 and 2014, we sold products to 268 and 258 customers, respectively, and our net sales to our ten largest customers represented 66% and 57% of our net sales, respectively. We have a combined production capacity of over 125,000 eight-inch equivalent semiconductor wafers per month. We believe our large-scale, cost-effective fabrication facilities enable us to rapidly adjust our production levels to meet shifts in demand by our end customers.

**Gross Profit.** Our overall gross profit generally fluctuates as a result of changes in overall sales volumes and in the average selling prices of our products and services. Other factors that influence our gross profit include changes in product mix, the introduction of new products and services and subsequent generations of existing products and services, shifts in the utilization of our manufacturing facilities and the yields achieved by our manufacturing operations, changes in material, labor and other manufacturing costs including outsourced manufacturing expenses, and variation in depreciation expense.

**Average Selling Prices.** Average selling prices for our products tend to be highest at the time of introduction of new products which utilize the latest technology and tend to decrease over time as such products mature in the market and are replaced by next generation products. We strive to offset the impact of declining selling prices for existing products through our product development activities and by introducing new products that command selling prices above the average selling price of our existing products. In addition, we seek to manage our inventories and manufacturing capacity so as to preclude losses from product and productive capacity obsolescence.

**Material Costs.** Our cost of material consists of costs of raw materials, such as silicon wafers, chemicals, gases and tape, packaging supplies, equipment maintenance and depreciation expenses. We use processes that require specialized raw materials, such as silicon wafers, that are generally available from a limited number of suppliers. If demand increases or supplies decrease, the costs of our raw materials could significantly increase.

**Labor Costs.** A significant portion of our employees are located in Korea. Under Korean labor laws, most employees and certain executive officers with one or more years of service are entitled to severance benefits upon the termination of their employment based on their length of service and rate of pay. As of June 30, 2015, approximately 98% of our employees were eligible for severance benefits.

## **Table of Contents**

***Depreciation Expense.*** We periodically evaluate the carrying values of long-lived assets, including property, plant and equipment and intangible assets, as well as the related depreciation periods. We depreciated our property, plant and equipment using the straight-line method over the estimated useful lives of our assets. Depreciation rates vary from 30-40 years on buildings to 5 to 12 years for certain equipment and assets. Our evaluation of carrying values is based on various analyses including cash flow and profitability projections. If our projections indicate that future undiscounted cash flows are not sufficient to recover the carrying values of the related long-lived assets, the carrying value of the assets is impaired and will be reduced, with the reduction charged to expense so that the carrying value is equal to fair value.

***Selling Expenses.*** We sell our products worldwide through a direct sales force as well as a network of sales agents and representatives to OEMs, including major branded customers and contract manufacturers, and indirectly through distributors. Selling expenses consist primarily of the personnel costs for the members of our direct sales force, a network of sales representatives and other costs of distribution. Personnel costs include base salary, benefits and incentive compensation.

***General and Administrative Expenses.*** General and administrative expenses consist of the costs of various corporate operations, including finance, legal, human resources and other administrative functions. These expenses primarily consist of payroll-related expenses, consulting and other professional fees and office facility-related expenses.

***Research and Development.*** The rapid technological change and product obsolescence that characterize our industry require us to make continuous investments in research and development. Product development time frames vary but, in general, we incur research and development costs one to two years before generating sales from the associated new products. These expenses include personnel costs for members of our engineering workforce, cost of photomasks, silicon wafers and other non-recurring engineering charges related to product design. Additionally, we develop base-line process technology through experimentation and through the design and use of characterization wafers that help achieve commercially feasible yields for new products. The majority of research and development expenses are for process development that serves as a common technology platform for all of our product lines.

***Interest Expense, Net.*** Our interest expense was incurred primarily under the 2021 Notes.

***Impact of Foreign Currency Exchange Rates on Reported Results of Operations.*** Historically, a portion of our revenues and greater than the majority of our operating expenses and costs of sales have been denominated in non-U.S. currencies, principally the Korean won, and we expect that this will remain true in the future. Because we report our results of operations in U.S. dollars converted from our non-U.S. revenues and expenses based on monthly average exchange rates, changes in the exchange rate between the Korean won and the U.S. dollar could materially impact our reported results of operations and distort period to period comparisons. In particular, because of the difference in the amount of our consolidated revenues and expenses that are in U.S. dollars relative to Korean won, depreciation in the U.S. dollar relative to the Korean won could result in a material increase in reported costs relative to revenues, and therefore could cause our profit margins and operating income (loss) to appear to decline materially, particularly relative to prior periods. The converse is true if the U.S. dollar were to appreciate relative to the Korean won. Moreover, our foreign currency gain or loss would be affected by changes in the exchange rate between the Korean won and the U.S. dollar as a substantial portion of non-cash translation gain or loss is associated with the intercompany long-term loans to our Korean subsidiary, which is denominated in U.S. dollars. As of June 30, 2015, the outstanding intercompany loan balance including accrued interest between the Korean subsidiary and the Dutch subsidiary was \$766 million. As a result of such foreign currency fluctuations, it could be more difficult to detect underlying trends in our business and results of operations. In addition, to the extent that fluctuations in currency exchange rates cause our results of operations to differ from our expectations or the expectations of our investors, the trading price of our stock could be adversely affected.

From time to time, we may engage in exchange rate hedging activities in an effort to mitigate the impact of exchange rate fluctuations. Our Korean subsidiary enters into foreign currency forward and zero cost collar contracts in order to mitigate a portion of the impact of U.S. dollar-Korean won exchange rate fluctuations on our operating results.

Obligations under these foreign currency forward and zero cost collar contracts must be cash collateralized if our exposure exceeds certain specified thresholds. These forward and zero cost collar contracts may be terminated by the counterparty in a number of circumstances, including if our total cash and cash equivalents is less than \$30.0 million at the end of a fiscal quarter unless a waiver is obtained from the counterparty. We cannot assure that any hedging technique we implement will be effective. If our hedging activities are not effective, changes in currency exchange rates may have a more significant impact on our results of operations.

**Foreign Currency Gain or Loss.** Foreign currency translation gains or losses on transactions by us or our subsidiaries in a currency other than our or our subsidiaries' functional currency are included in our statements of operations as a component of other income (expense). A substantial portion of this net foreign currency gain or loss relates to non-cash translation gain or loss related to the principal balance of intercompany balances at our Korean subsidiary that are denominated in U.S. dollars. This gain or loss results from fluctuations in the exchange rate between the Korean won and U.S. dollar.

**Income Taxes.** We record our income taxes in each of the tax jurisdictions in which we operate. This process involves using an asset and liability approach whereby deferred tax assets and liabilities are recorded for differences in the financial reporting bases and tax bases of our assets and liabilities. We exercise significant management judgment in determining our provision for income taxes,

## **Table of Contents**

deferred tax assets and liabilities. We assess whether it is more likely than not that the deferred tax assets existing at the period-end will be realized in future periods. In such assessment, we consider all available positive and negative evidence, including scheduled reversals of deferred tax liabilities, projected future taxable income, tax planning strategies and recent results of operations. In the event we were to determine that we would be able to realize the deferred income tax assets in the future in excess of their net recorded amount, we would adjust the valuation allowance, which would reduce the provision for income taxes.

Our operations are subject to income and transaction taxes in the United States and in multiple foreign jurisdictions, including Korea. Significant estimates and judgments are required in determining our worldwide provision for income taxes. Some of these estimates are based on interpretations of existing tax laws or regulations. The ultimate amount of tax liability may be uncertain as a result.

***Capital Expenditures.*** We invest in manufacturing equipment, software design tools and other tangible and intangible assets for capacity expansion and technology improvement. Capacity expansions and technology improvements typically occur in anticipation of increases in demand. We typically pay for capital expenditures in partial installments with portions due on order, delivery and final acceptance. Our capital expenditures include our payments for the purchase of property, plant and equipment as well as payments for the registration of intellectual property rights.

***Inventories.*** We monitor our inventory levels in light of product development changes and market expectations. We may be required to take additional charges for quantities in excess of demand, cost in excess of market value and product age. Our analysis may take into consideration historical usage, expected demand, anticipated sales price, new product development schedules, the effect new products might have on the sales of existing products, product age, customer design activity, customer concentration and other factors. These forecasts require us to estimate our ability to predict demand for current and future products and compare those estimates with our current inventory levels and inventory purchase commitments. Our forecasts for our inventory may differ from actual inventory use.

**Table of Contents****Results of Operations Comparison of Three Months Ended June 30, 2015 and 2014**

The following table sets forth consolidated results of operations for the three months ended June 30, 2015 and 2014:

|                                              | Three Months Ended<br>June 30, 2015 |                   | Three Months Ended<br>June 30, 2014 |                   | Change<br>Amount |
|----------------------------------------------|-------------------------------------|-------------------|-------------------------------------|-------------------|------------------|
|                                              | Amount                              | % of<br>Net Sales | Amount                              | % of<br>Net Sales |                  |
|                                              | (In millions)                       |                   |                                     |                   |                  |
| Net sales                                    | \$ 162.0                            | 100.0%            | \$ 172.1                            | 100.0%            | \$ (10.1)        |
| Cost of sales                                | 126.7                               | 78.2              | 136.6                               | 79.4              | (9.9)            |
| Gross profit                                 | 35.3                                | 21.8              | 35.5                                | 20.6              | (0.2)            |
| Selling, general and administrative expenses | 28.6                                | 17.6              | 30.7                                | 17.9              | (2.2)            |
| Research and development expenses            | 21.9                                | 13.5              | 24.1                                | 14.0              | (2.1)            |
| Operating loss                               | (15.2)                              | (9.4)             | (19.3)                              | (11.2)            | 4.1              |
| Interest expense, net                        | (3.9)                               | (2.4)             | (4.0)                               | (2.3)             | 0.1              |
| Foreign currency gain (loss), net            | (12.3)                              | (7.6)             | 38.4                                | 22.3              | (50.7)           |
| Others, net                                  | 0.2                                 | 0.1               | 0.6                                 | 0.3               | (0.4)            |
|                                              | (16.0)                              | (9.9)             | 35.0                                | 20.3              | (51.0)           |
| Income (loss) before income taxes            | (31.2)                              | (19.3)            | 15.7                                | 9.1               | (46.9)           |
| Income tax expenses (benefits)               | (0.6)                               | (0.4)             | 0.7                                 | 0.4               | (1.3)            |
| Net income (loss)                            | \$ (30.6)                           | (18.9)%           | \$ 15.0                             | 8.7%              | \$ (45.6)        |

**Results by segment**

|                                      | Three Months Ended<br>June 30, 2015 |                   | Three Months Ended<br>June 30, 2014 |                   | Change<br>Amount |
|--------------------------------------|-------------------------------------|-------------------|-------------------------------------|-------------------|------------------|
|                                      | Amount                              | % of<br>Net Sales | Amount                              | % of<br>Net Sales |                  |
|                                      | (In millions)                       |                   |                                     |                   |                  |
| <i>Net Sales</i>                     |                                     |                   |                                     |                   |                  |
| Semiconductor Manufacturing Services | \$ 79.0                             | 48.7%             | \$ 90.3                             | 52.5%             | \$ (11.4)        |
| Standard Products Group              |                                     |                   |                                     |                   |                  |
| Display Solutions                    | 48.9                                | 30.2              | 45.3                                | 26.3              | 3.6              |
| Power Solutions                      | 34.0                                | 21.0              | 36.3                                | 21.1              | (2.3)            |
| Total Standard Products Group        | 82.9                                | 51.2              | 81.6                                | 47.4              | 1.3              |

|                 |          |        |          |        |           |
|-----------------|----------|--------|----------|--------|-----------|
| All other       | 0.1      | 0.1    | 0.1      | 0.1    |           |
| Total net sales | \$ 162.0 | 100.0% | \$ 172.1 | 100.0% | \$ (10.1) |

|                                      | Three Months Ended<br>June 30, 2015 |                      | Three Months Ended<br>June 30, 2014 |                      | Change<br>Amount |
|--------------------------------------|-------------------------------------|----------------------|-------------------------------------|----------------------|------------------|
|                                      | Amount                              | % of<br>Gross Profit | Amount                              | % of<br>Gross Profit |                  |
|                                      | (In millions)                       |                      |                                     |                      |                  |
| <b>Gross Profit</b>                  |                                     |                      |                                     |                      |                  |
| Semiconductor Manufacturing Services | \$ 17.2                             | 48.7%                | \$ 18.6                             | 52.5%                | \$ (1.4)         |
| Standard Products Group              | 18.0                                | 50.9                 | 16.7                                | 47.2                 | 1.2              |
| All other                            | 0.1                                 | 0.4                  | 0.1                                 | 0.4                  |                  |
| Total gross profit                   | \$ 35.3                             | 100.0%               | \$ 35.5                             | 100.0%               | \$ (0.2)         |

## **Table of Contents**

### ***Net Sales***

Net sales were \$162.0 million for the three months ended June 30, 2015, a \$10.1 million, or 5.8%, decrease, compared to \$172.1 million for the three months ended June 30, 2014. This decrease was primarily due to decrease in revenue related to our Semiconductor Manufacturing Services segment as described below.

***Semiconductor Manufacturing Services.*** Net sales from our Semiconductor Manufacturing Services segment were \$79.0 million for the three months ended June 30, 2015, a \$11.4 million, or 12.6%, decrease compared to \$90.3 million for the three months ended June 30, 2014. The decrease was attributable to reduced levels of demand for our products by customers primarily serving the smartphone market.

***Standard Products Group.*** Net sales from our Standard Products Group segment were \$82.9 million for the three months ended June 30, 2015, a \$1.3 million, or 1.6%, increase compared to \$81.6 million for the three months ended June 30, 2014. This increase was primarily due to increase in revenue related to our Display Solution business line, partially offset by decrease in revenue related to our Power Solution business line as described below.

Net sales from our Display Solutions business line were \$48.9 million for the three months ended June 30, 2015, a \$3.6 million, or 7.9%, increase from \$45.3 million for the three months ended June 30, 2014. The increase in sales was attributable to higher sales of large display products, which was partially offset by reduced demand for mobile related products. Net sales from our Power Solutions business line were \$34.0 million for the three months ended June 30, 2015, a \$2.3 million, or 6.3%, decrease from \$36.3 million for the three months ended June 30, 2014. The decrease in sales of premium products such high-end MOSFETs and Power Modules impacted negatively our overall revenue, most of which was attributable to demand slowdown for our TV OEM customers. The decrease in sales was also resulted in part from reduced demand for MOSFET products driven by our existing customers due to significant competition in Asia.

***All Other.*** All other net sales were \$0.1 million for the three months ended June 30, 2015 and June 30, 2014, respectively.

### ***Gross Profit***

Total gross profit was \$35.3 million for the three months ended June 30, 2015 compared to \$35.5 million for the three months ended June 30, 2014, a \$0.2 million, or 0.5%, decrease. Gross profit as a percentage of net sales for the three months ended June 30, 2015 increased to 21.8% compared to 20.6% for the three months ended June 30, 2014. The slight increase in gross profit as a percentage of net sales was primarily due to increase in gross profit from our Standard Products Group segment, partially offset by decrease in gross profit from our Semiconductor Manufacturing Services segment as described below.

***Semiconductor Manufacturing Services.*** Gross profit from our Semiconductor Manufacturing Services segment was \$17.2 million for the three months ended June 30, 2015, a \$1.4 million, or 7.6%, decrease compared to \$18.6 million for the three months ended June 30, 2014. Gross profit as a percentage of net sales for the three months ended June 30, 2015 increased to 21.8% compared to 20.6% for the three months ended June 30, 2014. The increase in gross profit as a percentage of net sales was mainly attributable to better product mix and lower unit costs resulting from decrease in spending related to material and labor.

***Standard Products Group.*** Gross profit from our Standard Products Group segment was \$18.0 million for the three months ended June 30, 2015, a \$1.2 million, or 7.4%, increase from \$16.7 million for the three months ended June 30, 2014. Gross profit as a percentage of net sales for the three months ended June 30, 2015 increased to 21.7% compared

to 20.5% for the three months ended June 30, 2014. The improvement in gross profit as a percentage of net sales was primarily attributable to a decrease in warranty and inventory reserves and lower unit costs resulting from decrease in spending related to material and labor. This increase was partially offset by unfavorable mix mainly caused by higher sale of large display products and lower demand for mobile display products.

***All Other.*** All other gross profit was \$0.1 million for the three months ended June 30, 2015 and June 30, 2014, respectively.

**Table of Contents*****Net Sales by Geographic Region***

The following table sets forth our net sales by geographic region and the percentage of total net sales represented by each geographic region for the three months ended June 30, 2015 and 2014:

|                                 | Three Months Ended<br>June 30, 2015 |                   | Three Months Ended<br>June 30, 2014 |                   | Change<br>Amount |
|---------------------------------|-------------------------------------|-------------------|-------------------------------------|-------------------|------------------|
|                                 | Amount                              | % of<br>Net Sales | Amount                              | % of<br>Net Sales |                  |
|                                 | (In millions)                       |                   |                                     |                   |                  |
| Korea                           | \$ 61.7                             | 38.1%             | \$ 67.3                             | 39.1%             | \$ (5.6)         |
| Asia Pacific (other than Korea) | 75.6                                | 46.7              | 74.3                                | 43.2              | 1.2              |
| United States                   | 20.3                                | 12.5              | 24.6                                | 14.3              | (4.3)            |
| Europe                          | 3.7                                 | 2.3               | 5.6                                 | 3.3               | (1.9)            |
| Others                          | 0.7                                 | 0.4               | 0.2                                 | 0.1               | 0.4              |
|                                 | \$ 162.0                            | 100.0%            | \$ 172.1                            | 100.0%            | \$ (10.1)        |

Net sales in Korea for the three months ended June 30, 2015 decreased from \$67.3 million to \$61.7 million compared to the three months ended June 30, 2014, or by \$5.6 million, or 8.3%, primarily due to the discontinued use of a distributor in Korea and selling direct to OEM subsidiaries in Asia Pacific, which was partially offset by the increase in sales of large display applications.

Net sales in Asia Pacific (other than Korea) for the three months ended June 30, 2015 increased from \$74.3 million to \$75.6 million compared to the three months ended June 30, 2014, or by \$1.2 million, or 1.7%, primarily due to the discontinued use of a distributor in Korea and selling direct to OEM subsidiaries in Asia Pacific, which was partially offset by the reduced levels of demand for our products for mobile device and home appliances.

Net sales in the United States for the three months ended June 30, 2015 decreased from \$24.6 million to \$20.3 million compared to the three months ended June 30, 2014, or by \$4.3 million, or 17.4%, primarily due to the decrease in demand from our customers in the high end smartphone market.

Net sales in Europe for the three months ended June 30, 2015 decreased from \$5.6 million to \$3.7 million compared to the three months ended June 30, 2014, or by \$1.9 million, or 33.9%, primarily due to the decrease in revenues from our foundry service for automotive applications.

***Operating Expenses***

***Selling, General and Administrative Expenses.*** Selling, general and administrative expenses were \$28.6 million, or 17.6% of net sales, for the three months ended June 30, 2015, compared to \$30.7 million, or 17.9% of net sales, for the three months ended June 30, 2014. The decrease of \$2.2 million, or 7.0%, was primarily attributable to a \$0.9 million decrease in salaried compensation and a \$3.6 million decrease in bad debt expense. These decreases were partially offset by a \$1.6 million increase in separation cost and a \$1.2 million increase in equity-based compensation.

***Research and Development Expenses.*** Research and development expenses were \$21.9 million, or 13.5% of net sales, for the three months ended June 30, 2015, compared to \$24.1 million, or 14.0% of net sales, for the three

months ended June 30, 2014. The decrease of \$2.1 million, or 8.8%, was primarily due to a \$0.7 million decrease in direct material costs, a \$0.5 million decrease in outside service fees and reductions in various overhead expenses.

***Operating Loss***

As a result of the foregoing, operating loss decreased by \$4.1 million, or 21.3%, in the three months ended June 30, 2015 compared to the three months ended June 30, 2014. As discussed above, the decrease in operating loss resulted from a \$2.2 million decrease in selling, general and administrative expenses and a \$2.1 million decrease in research and development expenses, partially offset by a \$0.2 million decrease in gross profit.

***Other Income (Expense)***

***Interest Expense, Net.*** Net interest expense was \$3.9 million for the three months ended June 30, 2015 and \$4.0 million for the three months ended June 30, 2014.

***Foreign Currency Loss (Gain), Net.*** Net foreign currency loss for the three months ended June 30, 2015 was \$12.3 million compared to net foreign currency gain of \$38.4 million for the three months ended June 30, 2014. A substantial portion of our net foreign currency gain or loss is non-cash translation gain or loss associated with intercompany balances at our Korean subsidiary and is affected by changes in the exchange rate between the Korean won and the U.S. dollar. Foreign currency translation gain from intercompany balances was included in determining our consolidated net income since the intercompany balances were not considered long-term investments in nature because management intended to settle these intercompany balances at their respective maturity dates.

**Table of Contents**

***Others, Net.*** Others were comprised of gains and losses on valuation of derivatives which were designated as hedging instruments and rental incomes. Others for the three months ended June 30, 2015 and June 30, 2014 was \$0.2 million and \$0.6 million, respectively. The decrease of \$0.4 million was primarily attributable to net loss on valuation of derivatives due to hedge ineffectiveness.

***Income Tax Benefits (Expenses)***

Income tax benefits for the three months ended June 30, 2015 were \$0.6 million and income tax expenses for the three months ended June 30, 2014 were \$0.7 million. The decrease in income tax expenses of \$1.3 million was primarily attributable to benefits from the lapse of statute of limitations on unrecognized tax benefits related to withholding taxes on intercompany balances.

***Net Income***

As a result of the foregoing, net income decreased by \$45.6 million in the three months ended June 30, 2015 compared to the three months ended June 30, 2014. As discussed above, the decrease primarily resulted from a \$50.7 million unfavorable change in foreign currency translation, partially offset by a \$4.1 million decrease in operating loss.

**Table of Contents****Results of Operations Comparison of Six Months Ended June 30, 2015 and 2014**

The following table sets forth consolidated results of operations for the six months ended June 30, 2015 and 2014:

|                                              | Six Months Ended<br>June 30, 2015 |                   | Six Months Ended<br>June 30, 2014 |                   | Change<br>Amount |
|----------------------------------------------|-----------------------------------|-------------------|-----------------------------------|-------------------|------------------|
|                                              | Amount                            | % of<br>Net Sales | Amount                            | % of<br>Net Sales |                  |
|                                              | (In millions)                     |                   |                                   |                   |                  |
| Net sales                                    | \$ 326.9                          | 100.0%            | \$ 336.2                          | 100.0%            | \$ (9.3)         |
| Cost of sales                                | 256.6                             | 78.5              | 260.5                             | 77.5              | (3.9)            |
| Gross profit                                 | 70.3                              | 21.5              | 75.7                              | 22.5              | (5.5)            |
| Selling, general and administrative expenses | 53.6                              | 16.4              | 55.8                              | 16.6              | (2.2)            |
| Research and development expenses            | 44.1                              | 13.5              | 47.2                              | 14.0              | (3.1)            |
| Operating income (loss)                      | (27.4)                            | (8.4)             | (27.2)                            | (8.1)             | (0.2)            |
| Interest expense, net                        | (8.0)                             | (2.4)             | (8.1)                             | (2.4)             | 0.1              |
| Foreign currency gain (loss), net            | (15.5)                            | (4.7)             | 29.0                              | 8.6               | (44.5)           |
| Others, net                                  | 0.8                               | 0.2               | 1.2                               | 0.3               | (0.4)            |
|                                              | (22.7)                            | (6.9)             | 22.1                              | 6.6               | (44.8)           |
| Loss before income taxes                     | (50.1)                            | (15.3)            | (5.1)                             | (1.5)             | (45.0)           |
| Income tax expenses                          | 0.5                               | 0.2               | 1.5                               | 0.4               | (0.9)            |
| Net loss                                     | \$ (50.7)                         | (15.5)%           | \$ (6.6)                          | (2.0)%            | \$ (44.1)        |

**Results by segment**

|                                      | Six Months Ended<br>June 30, 2015 |                   | Six Months Ended<br>June 30, 2014 |                   | Change<br>Amount |
|--------------------------------------|-----------------------------------|-------------------|-----------------------------------|-------------------|------------------|
|                                      | Amount                            | % of<br>Net Sales | Amount                            | % of<br>Net Sales |                  |
|                                      | (In millions)                     |                   |                                   |                   |                  |
| <i>Net Sales</i>                     |                                   |                   |                                   |                   |                  |
| Semiconductor Manufacturing Services | \$ 153.5                          | 47.0%             | \$ 182.3                          | 54.2%             | \$ (28.8)        |
| Standard Products Group              |                                   |                   |                                   |                   |                  |
| Display Solutions                    | 105.3                             | 32.2              | 85.7                              | 25.5              | 19.6             |
| Power Solutions                      | 67.8                              | 20.8              | 68.1                              | 20.2              | (0.2)            |
| Total Standard Products Group        | 173.1                             | 53.0              | 153.8                             | 45.7              | 19.4             |

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|                 |          |        |          |        |          |
|-----------------|----------|--------|----------|--------|----------|
| All other       | 0.3      | 0.1    | 0.2      | 0.1    | 0.1      |
| Total net sales | \$ 326.9 | 100.0% | \$ 336.2 | 100.0% | \$ (9.3) |

|                                      | Six Months Ended<br>June 30, 2015 |                      | Six Months Ended<br>June 30, 2014 |                      | Change<br>Amount |
|--------------------------------------|-----------------------------------|----------------------|-----------------------------------|----------------------|------------------|
|                                      | Amount                            | % of<br>Gross Profit | Amount                            | % of<br>Gross Profit |                  |
|                                      | (In millions)                     |                      |                                   |                      |                  |
| <b>Gross Profit</b>                  |                                   |                      |                                   |                      |                  |
| Semiconductor Manufacturing Services | \$ 32.6                           | 46.3%                | \$ 40.7                           | 53.8%                | \$ (8.2)         |
| Standard Products Group              | 37.4                              | 53.2                 | 34.8                              | 46.0                 | 2.6              |
| All other                            | 0.3                               | 0.4                  | 0.2                               | 0.3                  | 0.1              |
| Total gross profit                   | \$ 70.3                           | 100.0%               | \$ 75.7                           | 100.0%               | \$ (5.5)         |

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**Table of Contents**

***Net Sales***

Net sales were \$326.9 million for the six months ended June 30, 2015, a \$9.3 million, or 2.8%, decrease, compared to \$336.2 million for the six months ended June 30, 2014. This decrease was primarily due to decrease in revenue related to our Semiconductor Manufacturing Services segment, which was offset in part by an increase in net sales from our Display Solutions business line as described below.

***Semiconductor Manufacturing Services.*** Net sales from our Semiconductor Manufacturing Services segment were \$153.5 million for the six months ended June 30, 2015, a \$28.8 million, or 15.8%, decrease compared to net sales of \$182.3 million for the six months ended June 30, 2014. The decrease was attributable to reduced levels of demand for our products by customers primarily serving the smartphone market.

***Standard Products Group.*** Net sales from our Standard Products Group segment were \$173.1 million for the six months ended June 30, 2015, a \$19.4 million, or 12.5%, increased compared to \$153.8 million for the six months ended June 30, 2014. This increase was primarily due to increase in revenue related to our Display Solution business line as described below.

Net sales from our Display Solutions business line were \$105.3 million for the six months ended June 30, 2015, a \$19.6 million, or 22.8%, increase from \$85.7 million for the six months ended June 30, 2014. The increase in sales was primarily attributable to higher sales of large display products. Net sales from our Power Solutions business line were \$67.8 million for the six months ended June 30, 2015, a \$0.2 million, or 0.3%, decrease from \$68.1 million for the six months ended June 30, 2014. The decrease in sales of products such as Power Modules negatively impacted our overall revenue, partially offset by increased demand for high-end MOSFETs primarily for TVs and mobile devices.

***All Other.*** All other net sales were \$0.3 million for the six months ended June 30, 2015 and \$0.2 million for the six months ended June 30, 2014.

***Gross Profit***

Total gross profit was \$70.3 million for the six months ended June 30, 2015 compared to \$75.7 million for the six months ended June 30, 2014, a \$5.5 million, or 7.2%, decrease. Gross profit as a percentage of net sales for the six months ended June 30, 2015 decreased to 21.5% compared to 22.5% for the six months ended June 30, 2014. The decrease in gross profit as a percentage of net sales was primarily due to decrease in gross profit from our Semiconductor Manufacturing Services segment, partially offset by increase in gross profit from our Standard Products Group segment as described below.

***Semiconductor Manufacturing Services.*** Gross profit from our Semiconductor Manufacturing Services segment was \$32.6 million for the six months ended June 30, 2015, a \$8.2 million, or 20.0%, decrease compared to \$40.7 million for the six months ended June 30, 2014. Gross profit as a percentage of net sales for the six months ended June 30, 2015 decreased to 21.2% compared to 22.3% for the six months ended June 30, 2014. The decrease in gross profit as a percentage of net sales was mainly attributable to a lower utilization rate and reduced levels of demand for our products by customers primarily serving the smartphone market, which negatively impacted our product mix compared to the six months ended June 30, 2014.

***Standard Products Group.*** Gross profit from our Standard Products Group segment was \$37.4 million for the six months ended June 30, 2015, a \$2.6 million, or 7.4%, increase from \$34.8 million for the six months ended June 30, 2014. Gross profit as a percentage of net sales for the six months ended June 30, 2015 decreased to 21.6% compared

to 22.6% for the six months ended June 30, 2014. The decrease in gross profit as a percentage of net sales was attributable to a lower utilization rate and unfavorable product mix mainly caused by higher sales of large display products while demand for mobile display products decreased.

**All Other.** All other gross profit was \$0.3 million for the six months ended June 30, 2015 and \$0.2 million for the six months ended June 30, 2014, respectively.

### ***Net Sales by Geographic Region***

The following table sets forth our net sales by geographic region and the percentage of total net sales represented by each geographic region for the six months ended June 30, 2015 and 2014:

|                                 | Six Months Ended<br>June 30, 2015 |                   | Six Months Ended<br>June 30, 2014 |                   | Change<br>Amount |
|---------------------------------|-----------------------------------|-------------------|-----------------------------------|-------------------|------------------|
|                                 | Amount                            | % of<br>Net Sales | Amount                            | % of<br>Net Sales |                  |
|                                 | (In millions)                     |                   |                                   |                   |                  |
| Korea                           | \$ 124.2                          | 38.0%             | \$ 134.3                          | 40.0%             | \$ (10.1)        |
| Asia Pacific (other than Korea) | 154.8                             | 47.3              | 144.6                             | 43.0              | 10.2             |
| United States                   | 39.7                              | 12.1              | 44.3                              | 13.2              | (4.7)            |
| Europe                          | 7.4                               | 2.3               | 12.5                              | 3.7               | (5.1)            |
| Others                          | 0.9                               | 0.3               | 0.5                               | 0.1               | 0.4              |
|                                 | \$ 326.9                          | 100.0%            | \$ 336.2                          | 100.0%            | \$ (9.3)         |

## **Table of Contents**

Net sales in Korea for the six months ended June 30, 2015 decreased from \$134.3 million to \$124.2 million compared to the six months ended June 30, 2014, or by \$10.1 million, or 7.5%, primarily due to the discontinued use of a distributor in Korea and selling direct to OEM subsidiaries in Asia Pacific, which was partially offset by the increase in sales of large display applications.

Net sales in Asia Pacific for the six months ended June 30, 2015 increased from \$144.6 million to \$154.8 million compared to the six months ended June 30, 2014, or by \$10.2 million, or 7.1%, primarily due to the discontinued use of a distributor in Korea and selling direct to OEM subsidiaries in Asia Pacific, which was partially offset by the reduced levels of demand for our products for mobile devices and home appliances.

Net sales in the United States for the six months ended June 30, 2015 decreased from \$44.3 million to \$39.7 million compared to the six months ended June 30, 2014, or by \$4.7 million, or 10.5%, primarily due to the decrease in demand from our existing customers in the high end smartphone market.

Net sales in Europe for the six months ended June 30, 2015 decreased from \$12.5 million to \$7.4 million compared to the six months ended June 30, 2014, or by \$5.1 million, or 41.1%, primarily due to the decrease in revenues from our foundry service for automotive and audio applications.

## ***Operating Expenses***

***Selling, General and Administrative Expenses.*** Selling, general, and administrative expenses were \$53.6 million, or 16.4% of net sales, for the six months ended June 30, 2015, compared to \$55.8 million, or 16.6% of net sales, for the six months ended June 30, 2014. The decrease of \$2.2 million, or 3.9%, was primarily attributable to a \$1.6 million decrease in salaried compensation and a \$3.7 million decrease in bad debt expense. These decreases were partially offset by a \$1.6 million increase in separation cost and a \$0.9 million increase in equity-based compensation. The remaining offset primarily related to increase in various outside service fees.

***Research and Development Expenses.*** Research and development expenses were \$44.1 million, or 13.5% of net sales, for the six months ended June 30, 2015, compared to \$47.2 million, or 14.0% of net sales, for the six months ended June 30, 2014. The decrease of \$3.1 million, or 6.6%, was due to a \$1.1 million decrease in personnel costs, a \$0.8 million decrease in outside service fees and reductions in various overhead expenses.

## ***Operating Loss***

As a result of the foregoing, operating loss increased by \$0.2 million in the six months ended June 30, 2015 compared to the six months ended June 30, 2014. As discussed above, the increase in operating loss resulted from a \$5.5 million decrease in gross profit, which was offset by a \$2.2 million decrease in selling, general and administrative expenses and a \$3.1 million decrease in research and development expenses.

## ***Other Income (Expense)***

***Interest Expense, Net.*** Net interest expense was \$8.0 million for the six months ended June 30, 2015 and \$8.1 million for the six months ended June 30, 2014.

***Foreign Currency Gain (Loss), Net.*** Net foreign currency loss for the six months ended June 30, 2015 was \$15.5 million compared to net foreign currency gain of \$29.0 million for the six months ended June 30, 2014. A substantial portion of our net foreign currency gain or loss is non-cash translation gain or loss associated with intercompany balances at our Korean subsidiary and is affected by changes in the exchange rate between the Korean

won and the U.S. dollar. Foreign currency translation gain from intercompany balances was included in determining our consolidated net income since the intercompany balances were not considered long-term investments in nature because management intended to settle these intercompany balances at their respective maturity dates.

***Others, Net.*** Others were comprised of gains and losses on valuation of derivatives which were designated as hedging instruments and rental incomes. Others for the six months ended June 30, 2015 and June 30, 2014 was \$0.8 million and \$1.2 million, respectively. The decrease of \$0.4 million was primarily attributable to net loss on valuation of derivatives due to hedge ineffectiveness.

**Table of Contents**

***Income Tax Expenses***

Income tax expenses for the six months ended June 30, 2015 and 2014 were \$0.5 million and \$1.5 million respectively. The decrease in income tax expenses of \$1.0 million was primarily attributable to benefits from the lapse of statute of limitations on unrecognized tax benefits related to withholding taxes on intercompany balances.

***Net Loss***

As a result of the foregoing, net loss increased by \$44.1 million in the six months ended June 30, 2015 compared to the six months ended June 30, 2014. As discussed above, the decrease primarily resulted from a \$44.5 million unfavorable change in foreign currency translation, partially offset by a \$0.9 million decrease in income tax expenses.

## **Table of Contents**

### **Liquidity and Capital Resources**

Our principal capital requirements are to fund sales and marketing, invest in research and development and capital equipment, to make debt service payments and to fund working capital needs. We calculate working capital as current assets less current liabilities.

Our principal sources of liquidity are our cash, cash equivalents, our cash flows from operations and our financing activities. Our ability to manage cash and cash equivalents may be limited as our primary cash flows are dictated by the terms of our sales and supply agreements, contractual obligations, debt instruments and legal and regulatory requirements. From time to time, we may sell accounts receivable to third parties under factoring agreements or engage in accounts receivable discounting to facilitate the collection of cash. In addition, from time to time, we may make payments to our vendors on extended terms with their consent.

#### ***Cash Flows from Operating Activities***

Cash outflow used in operating activities totaled \$27.5 million for the six months ended June 30, 2015, compared to \$5.5 million of cash provided by operating activities in the six months ended June 30, 2014. The net operating cash outflow for the six months ended June 30, 2015 reflects our net loss of \$50.7 million and non-cash adjustments of \$46.5 million which mainly consisted of depreciation and amortization, provision for severance benefits and foreign currency loss, and a decrease in net operating liabilities of \$23.3 million.

Our working capital balance as of June 30, 2015 was \$90.0 million compared to \$106.8 million as of December 31, 2014. The \$16.8 million decrease was primarily attributable to a \$29.8 million decrease in cash and cash equivalents and a \$13.3 million decrease in accounts payable. The decrease in account payable is a result of decreased material purchases and increased payments of outstanding outside service fees related to the restatement and litigation.

#### ***Cash Flows from Investing Activities***

Cash outflow used in investing activities totaled \$9.2 million in the six months ended June 30, 2015, compared to \$10.8 million in the six months ended June 30, 2014. The decrease was primarily due to a decrease in capital expenditures of \$10.3 million, partially offset by a \$6.6 million increase in hedge collateral, which is comprised of \$5.0 million of cash deposits and \$1.4 million of cash collateral related to our derivative financial instruments.

#### ***Cash Flows from Financing Activities***

Cash inflows generated by financing activities totaled \$1.2 million for the six months ended June 30, 2015, compared to \$0.1 million of cash outflow used in financing activities in the six months ended June 30, 2014. The financing cash inflow for the six months ended June 30, 2015 consists of proceeds received from the issuance of common stock in connection with exercised options.

#### ***Capital Expenditures***

We routinely make capital expenditures to enhance our existing facilities and reinforce our global research and development capability. For the six months ended June 30, 2015, capital expenditures were \$2.2 million, a \$10.3 million, or 82.3%, decrease from \$12.5 million in the six months ended June 30, 2014 due to acquisition of a specialized Epi toll and maintenance of our fab in the first half of 2014.

### **Seasonality**

Our net sales and number of distinct products sold are affected by market variations from quarter to quarter due to business cycles, and resulting product demand, of our customers. In our Display Solutions and Power Solutions business lines, consumer products manufacturers generally reduce orders in order to reduce excess inventory remaining from the holiday season. In our Semiconductor Manufacturing Services business, the supply-demand cycle is usually one quarter ahead of the broader semiconductor market due to lead time from wafer input to shipment to our customers.

**Table of Contents****Contractual Obligations**

The following summarizes our contractual obligations as of June 30, 2015:

|                                | Total    | Payments Due by Period  |         |         |         |         |            |
|--------------------------------|----------|-------------------------|---------|---------|---------|---------|------------|
|                                |          | Remainder<br>of<br>2015 | 2016    | 2017    | 2018    | 2019    | Thereafter |
|                                |          |                         |         |         |         |         |            |
| Senior notes <sup>(1)</sup>    | \$ 321.9 | \$ 7.5                  | \$ 14.9 | \$ 14.9 | \$ 14.9 | \$ 14.9 | \$ 254.8   |
| Operating lease <sup>(2)</sup> | 44.7     | 4.4                     | 4.9     | 2.2     | 2.1     | 2.0     | 29.2       |
| Others <sup>(3)</sup>          | 7.2      | 3.6                     | 3.6     |         |         |         |            |

- (1) Interest payments as well as \$225.0 million aggregate principal amount of the 2021 Notes outstanding as of June 30, 2015, which bear interest at a rate of 6.625% per annum and are scheduled to mature in 2021.
- (2) Assumes constant currency exchange rate for Korean won to U.S. dollars of 1,124.1:1, the exchange rate as of June 30, 2015.
- (3) Includes license agreements and other contractual obligations.

The Indenture relating to the 2021 Notes contains covenants that limit our ability and our restricted subsidiaries to: (i) declare or pay any dividend or make any payment or distribution on account of or purchase or redeem our capital stock or equity interests of the restricted subsidiaries; (ii) make any principal payment on, or redeem or repurchase, prior to any scheduled repayment or maturity, any subordinated indebtedness; (iii) make certain investments; (iv) incur additional indebtedness and issue certain types of capital stock; (v) create or incur any lien (except for permitted liens) that secures obligations under any indebtedness; (vi) merge with or into or sell all or substantially all of our assets to other companies; (vii) enter into certain types of transactions with affiliates; (viii) guarantee the payment of any indebtedness; (ix) enter into sale-leaseback transactions; (x) enter into agreements that would restrict the ability of the restricted subsidiaries to make distributions with respect to their equity to us or other restricted subsidiaries, to make loans to us or other restricted subsidiaries or to transfer assets to us or other restricted subsidiaries; and (xi) designate unrestricted subsidiaries.

We lease land, office space and equipment under various operating lease agreements that expire through 2034.

We follow ASC guidance on uncertain tax positions. Our unrecognized tax benefits totaled \$2.0 million as of June 30, 2015. These unrecognized tax benefits have been excluded from the above table because we cannot estimate the period of cash settlement with the respective taxing authorities.

Although we are obligated to pay severance benefits to eligible employees with one or more years of service upon the termination of their employment based on their length of service and pay rate, we have no obligation to fund the accrued severance benefits. Our accrued severance benefits totaled \$143.7 million as of June 30, 2015. Our obligations in connection with severance benefits have been excluded from the above table because we are unable to reasonably estimate the rate of termination and related cash payments for future periods.

**Critical Accounting Policies and Estimates**

Preparing financial statements in conformity with US GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the financial statements, the reported amounts of revenues and expenses during the reporting periods and the related disclosures in our consolidated financial statements and accompanying notes.

We believe that our significant accounting policies, which are described in Note 1 to the consolidated financial statements of MagnaChip Semiconductor Corporation of the 2014 Form 10-K, are critical due to the fact that they involve a high degree of judgment and estimates about the effects of matters that are inherently uncertain. We base these estimates and judgments on historical experience, knowledge of current conditions and other assumptions and information that we believe to be reasonable. Estimates and assumptions about future events and their effects cannot be determined with certainty. Accordingly, these estimates may change as new events occur, as more experience is acquired, as additional information is obtained and as the business environment in which we operate changes.

### ***Revenue Recognition***

Revenue is recognized when there is persuasive evidence of an arrangement, the price to the buyer is fixed or determinable, delivery has occurred and collectability of the sales price is reasonably assured. Revenue from the sale of products is recognized when title and risk of loss transfers to the customer, which is generally when the product is shipped to or accepted by the customer depending on the terms of the arrangement.

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**Table of Contents**

A portion of our sales are made through distributors for which revenue recognition criteria are usually met when the product is shipped to or accepted by the distributor, consistent with the principles described above. However, the risk of loss may not pass upon shipment of products to the distributor due to a variety of reasons, including the nature of the business arrangement with the distributor. For example, the financial condition of a distributor may indicate that payments by the distributor to us are contingent on resale of products to an end customer. In this situation, we defer recognition of revenue and cost of revenue on transactions with such distributor until the product has been resold to the end customer.

In accordance with revenue recognition guidance, any tax assessed by a governmental authority that is directly imposed on a revenue-producing transaction between a seller and a customer is presented in the statements of operations on a net basis (excluded from revenues).

We provide a warranty, under which customers can return defective products. We estimate the costs related to those defective product returns and record them as a component of cost of sales.

In addition, we offer sales returns (other than those that relate to defective products under warranty), yield provisions, cash discounts for early payments and certain allowances to our customers, including distributors. We record reserves for those returns, discounts and allowances as a deduction from sales, based on historical experience and other quantitative and qualitative factors.

All amounts billed to a customer related to shipping and handling are classified as sales while all costs incurred by us for shipping and handling are classified as selling, general and administrative expenses.

***Sales of Accounts Receivable***

We account for transfers of financial assets under ASC 860, Transfers and Servicing, as either sales or financings. Transfers of financial assets that result in sales accounting are those in which (1) the transfer legally isolates the transferred assets from the transferor, (2) the transferee has the right to pledge or exchange the transferred assets and no condition both constrains the transferee's right to pledge or exchange the assets and provides more than a trivial benefit to the transferor and (3) the transferor does not maintain effective control over the transferred assets. If the transfer does not meet these criteria, the transfer is accounted for as a financing. Financial assets that are treated as sales are removed from our accounts with any realized gain or loss reflected in earnings during the period of sale.

***Product Warranties***

We record, in other current liabilities, warranty liabilities for the estimated costs that may be incurred under our basic limited warranty. The standard limited warranty period is one year for the majority of products. This warranty covers defective products, and related liabilities are accrued when product revenues are recognized. Factors that affect our warranty liability include historical and anticipated rates of warranty claims and repair or replacement costs per claim to satisfy our warranty obligation. As these factors are impacted by actual experience and future expectations, we periodically assess the adequacy of our recorded warranty liabilities and adjust the amounts when necessary.

***Inventories***

Inventories are stated at the lower of cost or market, using the average cost method, which approximates the first in, first out method ( FIFO ). If net realizable value is less than cost at the balance sheet date, the carrying amount is reduced to the realizable value, and the difference is recognized as a loss on valuation of inventories within cost of sales. Inventory reserves are established when conditions indicate that the net realizable value is less than costs due to

physical deterioration, obsolescence, changes in price levels, or other causes based on individual facts and circumstances. Reserves are also established for excess inventory based on inventory levels in excess of six months of projected demand for each specific product.

In addition, as prescribed in ASC 330, Inventory, the cost of inventories is determined based on the normal capacity of each fabrication facility. In case the capacity utilization is lower than a certain level that management believes to be normal, the fixed overhead costs per production unit which exceed those under normal capacity are charged to cost of sales rather than capitalized as inventories.

#### ***Impairment of Long-Lived Assets***

We review property, plant and equipment and other long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable in accordance with ASC 360, Property, Plant and Equipment (ASC 360). Recoverability is measured by comparing its carrying amount with the future net undiscounted cash flows the assets are expected to generate. If such assets are considered to be impaired, the impairment is measured as the difference between the carrying amount of the assets and the fair value of assets using the present value of the future net cash flows generated by the respective long-lived assets.

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**Table of Contents**

***Intangible Assets***

Intangible assets other than intellectual property include technology and customer relationships which are amortized on a straight-line basis over periods ranging from one to five years. Intellectual property assets acquired represent rights under patents, trademarks and property use rights and are amortized over their respective periods of benefit, ranging up to ten years, on a straight-line basis.

***Income Taxes***

We account for income taxes in accordance with ASC 740, *Income Taxes* (ASC 740). ASC 740 requires recognition of deferred tax assets and liabilities for the expected future tax consequences of events that have been recognized in a company's financial statements or tax returns. Under this method, deferred tax assets and liabilities are determined based upon the difference between the financial statement carrying amounts and the tax bases of assets and liabilities using enacted tax rates in effect in the years in which the differences are expected to reverse. Valuation allowances are established when it is necessary to reduce deferred tax assets to the amount expected to be realized. Income tax expense is the tax payable for the period and the change during the period in deferred tax assets and liabilities.

We recognize and measure uncertain tax positions taken or expected to be taken in a tax return utilizing a two-step process. In the first step, recognition, we determine whether it is more-likely-than-not that a tax position will be sustained upon examination, including resolution of any related appeals or litigation processes, based on the technical merits of the position. The second step addresses measurement of a tax position that meets the more-likely-than-not criteria. The tax position is measured at the largest amount of benefit that has a likelihood of greater than 50 percent of being realized upon ultimate settlement.

***Derivative Financial Instruments***

We apply the provisions of ASC 815. This Statement requires the recognition of all derivative instruments as either assets or liabilities measured at fair value.

Under the provisions of ASC 815, we may designate a derivative instrument as hedging the exposure to variability in expected future cash flows that are attributable to a particular risk (a *cash flow hedge*) or hedging the exposure to changes in the fair value of an asset or a liability (a *fair value hedge*). Special accounting for qualifying hedges allows the effective portion of a derivative instrument's gains and losses to offset related results on the hedged item in the consolidated statements of operations and requires that a company formally document, designate and assess the effectiveness of the transactions that receive hedge accounting treatment. Both at the inception of a hedge and on an ongoing basis, a hedge must be expected to be highly effective in achieving offsetting changes in cash flows or fair value attributable to the underlying risk being hedged. If we determine that a derivative instrument is no longer highly effective as a hedge, it discontinues hedge accounting prospectively and future changes in the fair value of the derivative are recognized in current earnings. We assess hedge effectiveness at the end of each quarter.

In accordance with ASC 815, changes in the fair value of derivative instruments that are cash flow hedges are recognized in accumulated other comprehensive income (loss) and reclassified into earnings in the period in which the hedged item affects earnings. Ineffective portions of a derivative instrument's change in fair value are immediately recognized in earnings. Derivative instruments that do not qualify, or cease to qualify, as hedges must be adjusted to fair value and the adjustments are recorded through net income (loss).

The cash flows from derivative instruments receiving hedge accounting treatment are classified in the same categories as the hedged items in the consolidated statements of cash flows.

***Recent Accounting Pronouncements***

In April 2015, the FASB issued ASU 2015-03. ASU 2015-03 requires that debt issuance costs are presented in the balance sheet as a direct deduction from the carrying amount of debt liability, consistent with debt discounts or premiums. The recognition and measurement guidance for debt issuance costs would not be affected. ASU 2015-03 is effective for annual reporting periods beginning after December 15, 2015, including interim periods within that reporting period. We are currently evaluating the impact of the adoption of ASU 2015-03 on our consolidated financial statements.

In August 2014, the FASB issued ASU 2014-15, which provides guidance on determining when and how to disclose going-concern uncertainties in the financial statements. ASU 2014-15 requires management to perform interim and annual assessments of an entity's ability to continue as a going concern within one year of the date the financial statements are issued. An entity will be required to provide certain disclosures if conditions of events raise substantial doubt about the entity's ability to continue as a going concern. ASU 2014-15 is effective for annual periods ending after December 15, 2016, and interim periods thereafter, with early adoption permitted. We are currently evaluating the impact of the adoption of ASU 2014-15 on our consolidated financial statements.

**Table of Contents**

In May 2014, the FASB issued ASU 2014-09. ASU 2014-09 supersedes the revenue recognition requirements in Revenue Recognition (Topic 605) , and requires entities to recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled to in exchange for those goods or services. ASU 2014-09 is effective for annual reporting periods beginning after December 15, 2016 (the Original Effective Date ), including interim periods within that reporting period, and can be adopted either retrospectively to each prior period presented or as a cumulative-effect adjustment as of the date of adoption, with early application permitted as of the Original Effective Date. In July 2015, the FASB decided to delay the effective date of ASU 2014-09 by one year. We are currently evaluating the impact of the adoption of ASU 2014-09 on our consolidated financial statements.

**Table of Contents**

**Item 3. Quantitative and Qualitative Disclosures About Market Risk**

We are exposed to the market risk that the value of a financial instrument will fluctuate due to changes in market conditions, primarily from changes in foreign currency exchange rates and interest rates. In the normal course of our business, we are subject to market risks associated with interest rate movements and currency movements on our assets and liabilities.

***Foreign Currency Exposures***

We have exposure to foreign currency exchange rate fluctuations on net income from our subsidiaries denominated in currencies other than U.S. dollars, as our foreign subsidiaries in Korea, Taiwan, China, Japan and Hong Kong use local currency as their functional currency. From time to time these subsidiaries have cash and financial instruments in local currency. The amounts held in Japan, Taiwan, Hong Kong and China are not material in regards to foreign currency movements. However, based on the cash and financial instruments balance at June 30, 2015 for our Korean subsidiary, a 10% devaluation of the Korean won against the U.S. dollar would have resulted in a decrease of \$2.2 million in our U.S. dollar financial instruments and cash balances.

See Note 7. Derivative Financial Instruments to our consolidated financial statements under Part I: Item 1. Interim Consolidated Financial Statements (Unaudited) and Part I: Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations Factors Affecting Our Results of Operations Impact of Foreign Currency Exchange Rates on Reported Results of Operations of this Report for additional information regarding our foreign exchange hedging activities.

***Interest Rate Exposures***

As of June 30, 2015, \$225.0 million aggregate principal amount of our 2021 Notes were outstanding. Interest on the 2021 Notes accrues at a fixed rate of 6.625% per annum and is paid semi-annually every January 15 and July 15 of each year until the 2021 Notes mature on July 15, 2021. Since the interest rate is fixed, we have no market risk related to the 2021 Notes.

## **Table of Contents**

### **Item 4. Controls and Procedures**

#### ***Evaluation of Disclosure Controls and Procedures***

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in the reports we file or submit under the Securities Exchange Act of 1934, as amended (the Exchange Act), is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosure.

In connection with the preparation of this Quarterly Report on Form 10-Q, we carried out an evaluation under the supervision of and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, as of June 30, 2015, of the effectiveness of the design and operation of our disclosure controls and procedures, as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act. Based upon this evaluation, our Chief Executive Officer and Chief Financial Officer, concluded that our disclosure controls and procedures were not effective as of June 30, 2015, as we cannot conclude that the material weaknesses in internal control over financial reporting described in Part II, Item 9A of the 2014 Form 10-K have been remediated as of the date of this Quarterly Report.

#### ***Previously Identified Material Weaknesses***

As previously disclosed in the 2014 Form 10-K, management concluded that, based on the criteria set forth in Internal Control Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), our internal control over financial reporting was not effective as of December 31, 2014 to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements in accordance with US GAAP. For more information on the material weaknesses in internal control over financial reporting, see Part II, Item 9A of the 2014 Form 10-K.

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

In evaluating whether there were any reportable changes in our internal controls over financial reporting during the quarter ended June 30, 2015, we determined that there were enhancements to our internal control over financial reporting during this quarter as described below. Other than these changes, there were no changes in internal control over financial reporting during the quarter ended June 30, 2015 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

#### ***Control Environment:***

During the second quarter of 2015, the Company appointed YJ Kim as Chief Executive Officer and a member of the Company's Board of Directors, and Jonathan Kim as Chief Financial Officer. Messrs. YJ Kim and Jonathan Kim previously served as Chief Executive Officer and Chief Financial Officer, respectively, on an interim basis since the second quarter of 2014.

Commencing in the second quarter of 2014, the Principal Executive Officer and Principal Financial Officer/Chief Accounting Officer (new management team) took steps to communicate their expectation of

the enhanced compliance with high ethical standards by providing ethical guidelines and other forms of internal communications to all employees.

During the fourth quarter of 2014 and second quarter of 2015, the new management team provided mandatory ethics compliance trainings for all employees, which included a pledge to comply with the Company's Code of Business Conduct and Ethics. Through such employee training sessions, the new management team specifically emphasized the importance of our whistleblower hotline, through which employees at all levels can anonymously submit information or express concerns regarding accounting, financial reporting, and violations of our Code of Business Conduct and Ethics or other topics.

During 2014 and 2015, the new management team (i) strengthened the Company's accounting and finance teams by hiring full-time employees with extensive U.S. GAAP experience, (ii) established a detailed revenue recognition policy including logical criteria to decide whether necessary conditions for revenue recognition were fully met in accordance with U.S. GAAP, and (iii) facilitated U.S. GAAP training programs for relevant employees.

During the fourth quarter of 2014 and through the date of the filing of this Report, the new management team has been implementing a sub-certification process, which requires that certain employees certify on a quarterly basis that they have no knowledge of (i) any transaction of which terms deviate from the terms of written sales or purchasing contracts, (ii) any undisclosed or unauthorized transaction that should be communicated to the authorized personnel in the accounting team, and (iii) any irregular activities that were not conducted in the ordinary course of business, including inappropriate decision-making and non-compliance with applicable regulations, policies and procedures.

## **Table of Contents**

### ***Monitoring Activities:***

The new management team has been building an environment that prioritizes compliance across the enterprise, placing special efforts on improving internal audits and compliance with the Sarbanes-Oxley Act. In December 2014, the new management team hired a new Director of Compliance and Internal Audit, whose primary duties are to design, implement, and operate our internal control over financial reporting.

During the fourth quarter of 2014 and through the date of the filing of this Report, the Compliance and Internal Audit Team (i) has conducted a risk assessment that considers specific risk scenarios in which misstatement of financial reporting might occur and (ii) has executed monitoring of a sample of transactions for high risk areas. Specifically, the Compliance and Internal Audit Team has implemented an order deviation monitoring process whereby deviations from established customer sales terms were reviewed in order to ensure that such deviations are accurately reflected in our financial statements.

In May 2015, the Company named its General Counsel, Theodore Kim, as Executive Vice President and Chief Compliance Officer, a newly created position, reporting directly to the Board of Directors. He continues to serve as General Counsel. In addition, the Compliance and Internal Audit Team was reorganized under the Chief Compliance Officer, to whom the Director of Compliance and Internal Audit reports, as a part of the Company's continuing effort to reinforce the independence and objectivity of our internal audit activities from management.

As a result, we continue to effectively provide the Audit Committee with the information concerning internal audit activities, internal control deficiencies and remediation plans, investigation results of any whistle blowers' complaints, and any irregular activities that are non-compliant with applicable regulations, policies and procedures.

### ***Period End Closing and Financial Reporting:***

We have implemented our internal controls in the period-end closing and financial reporting process to: (i) require appropriate internal and external evidences to be prepared for certain type of journal entries; (ii) improve the methods of reconciliation, confirmation, verification, observation, period end cut-off test, and analysis of each accounts in a timely manner; and (iii) assign appropriate roles and responsibilities for more comprehensive review procedures, including the involvement of finance and operational managers, in order to strengthen controls over the completeness and accuracy of both recurring and non-recurring journal entries.

### ***Remediation Plans***

We are in the process of developing and implementing remediation plans to address our material weaknesses. Our remediation plans include many actions that are in various stages prior to completion and designed to strengthen our internal controls over financial reporting. They include the following:

### ***Control Environment:***

The new management team plans to hire a senior level employee or contract an outside advisor, with expertise in the area of tax accounting and reporting, to (i) manage and oversee income tax matters comprehensively, (ii) consult with the management team, and (iii) train accounting employees with regard to tax accounting, disclosure practices and rules and regulations.

***Income Tax Accounting and Disclosures:***

We have been improving our procedures and controls over tax accounting and reporting by ensuring that we, on a timely basis: (i) review rules and regulations of tax jurisdictions relevant to each of our consolidated entities; (ii) review related accounting implications; and (iii) improve the competency of our accounting employees through ongoing training on income tax accounting, disclosure practices, and rules and regulations.

As we continue to work to improve our internal controls over financial reporting, management may determine to take additional measures to address the material weaknesses or determine to modify the remediation plan described above. Until the remediation plans set forth above are fully completed and sufficiently operated, the material weaknesses in internal controls over financial reporting described in Part II, Item 9A of the 2014 Form 10-K will continue to exist.

**Table of Contents**

**PART II. OTHER INFORMATION**

**Item 1. Legal Proceedings**

For a discussion of legal proceedings, see Part I: Item 3. Legal Proceedings of our 2014 Form 10-K.

See also Part I: Item 1A. Risk Factors of our 2014 Form 10-K and Note 16 to our consolidated financial statements in this Report for additional information.

**Item 1A. Risk Factors**

The Company is subject to risks and uncertainties, any of which could have a significant or material adverse effect on our business, financial condition, liquidity or consolidated financial statements. You should carefully consider the risk factors disclosed in Part I, Item 1A of our 2014 Form 10-K. The risks described herein and therein are not the only ones we face. This information should be considered carefully together with the other information contained in this Report and the other reports and materials the Company files with the SEC.

There are no material changes to the Company's risk factors disclosed in Part I: Item 1A. Risk Factors of our 2014 Form 10-K.

**Table of Contents**

**Item 6. Exhibits.**

**Exhibit**

| <b>Number</b> | <b>Description</b>                                                                                                                                                                                                                                 |
|---------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 10.1#*        | Separation Agreement, effective June 30, 2015, by and between MagnaChip Semiconductor, Ltd. (Korea) and Heung Kyu Kim.                                                                                                                             |
| 10.2*         | Advisory Services and Separation Agreement, effective May 28, 2015, by and between MagnaChip Semiconductor, Inc. and Brent Rowe (incorporated by reference to Exhibit 10.29-1 to our Annual Report on Form 10-K filed on May 28, 2015).            |
| 10.3*         | Advisory Services and Separation Agreement, dated April 30, 2015, by and between MagnaChip Semiconductor, Ltd. (Korea) and Tae Young Hwang (incorporated by reference to Exhibit 10.28-1 to our Annual Report on Form 10-K filed on May 28, 2015). |
| 31.1#         | Certification pursuant to Rule 13a-14(a) or Rule 15d-14(a) of the Securities Exchange Act of 1934 of the Chief Executive Officer.                                                                                                                  |
| 31.2#         | Certification pursuant to Rule 13a-14(a) or Rule 15d-14(a) of the Securities Exchange Act of 1934 of the Chief Financial Officer.                                                                                                                  |
| 32.1          | Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, of the Chief Executive Officer.                                                                                            |
| 32.2          | Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, of the Chief Financial Officer.                                                                                            |
| 101.INS#      | XBRL Instance Document.                                                                                                                                                                                                                            |
| 101.SCH#      | XBRL Taxonomy Extension Schema Document.                                                                                                                                                                                                           |
| 101.CAL#      | XBRL Taxonomy Extension Calculation Linkbase Document.                                                                                                                                                                                             |
| 101.DEF#      | XBRL Taxonomy Extension Definition Linkbase Document.                                                                                                                                                                                              |
| 101.LAB#      | XBRL Taxonomy Extension Label Linkbase Document.                                                                                                                                                                                                   |
| 101.PRE#      | XBRL Taxonomy Extension Presentation Linkbase Document.                                                                                                                                                                                            |
| Footnotes:    |                                                                                                                                                                                                                                                    |

# Filed herewith

Furnished herewith

\* Management contract, compensatory plan or arrangement

**Table of Contents**

**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

MAGNACHIP SEMICONDUCTOR CORPORATION

(Registrant)

Dated: August 7, 2015

By: /s/ Young-Joon Kim  
Young-Joon Kim  
Chief Executive Officer

(Principal Executive Officer)

Dated: August 7, 2015

By: /s/ Jonathan W. Kim  
Jonathan W. Kim  
Chief Financial Officer, Executive Vice President and  
Chief Accounting Officer

(Principal Financial and Accounting Officer)

**Table of Contents**

**INDEX TO EXHIBITS**

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