

MAGNACHIP SEMICONDUCTOR Corp
Form 10-Q
August 05, 2013
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended June 30, 2013

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)

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Delaware
(State or other jurisdiction of
incorporation or organization)

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

c/o MagnaChip Semiconductor S.A.

74, rue de Merl, L-2146

Luxembourg, Grand Duchy of Luxembourg

(352) 45-62-62

(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

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Sections 12, 13 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court. Yes No

As of June 30, 2013, the registrant had 35,681,382 shares of common stock outstanding.

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MAGNACHIP SEMICONDUCTOR CORPORATION AND SUBSIDIARIES

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FORWARD LOOKING STATEMENTS

The following Management's Discussion and Analysis of Financial Condition and Results of Operations contain 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, 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 II: Item 1A. Risk Factors in this report.

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, 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.

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)**

	June 30, 2013	December 31, 2012
Assets		
Current assets		
Cash and cash equivalents	\$ 192,641	\$ 182,238
Restricted cash	6	133
Accounts receivable, net	165,181	143,331
Inventories, net	76,342	89,363
Other receivables	2,459	1,429
Prepaid expenses	9,366	7,884
Current deferred income tax assets	25,347	22,768
Other current assets	3,695	9,680
Total current assets	475,037	456,826
Property, plant and equipment, net	247,242	238,256
Intangible assets, net	10,068	15,260
Long-term prepaid expenses	17,962	18,048
Deferred income tax assets	42,631	46,710
Other non-current assets	15,422	14,866
Total assets	\$ 808,362	\$ 789,966
Liabilities and Stockholders' Equity		
Current liabilities		
Accounts payable	\$ 76,175	\$ 79,236
Other accounts payable	16,804	15,600
Accrued expenses	49,918	43,486
Derivative liabilities	10,247	
Other current liabilities	6,912	9,973
Total current liabilities	160,056	148,295
Long-term borrowings, net	201,801	201,653
Accrued severance benefits, net	112,198	112,446
Other non-current liabilities	17,880	17,263
Total liabilities	491,935	479,657
Stockholders' equity		
Common stock, \$0.01 par value, 150,000,000 shares authorized, 40,021,283 shares issued and 35,681,382 outstanding at June 30, 2013 and 39,599,374 shares issued and 35,635,357 outstanding at December 31, 2012	400	396

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Additional paid-in capital	107,375	101,885
Retained earnings	284,282	287,251
Treasury stock, 4,339,901 and 3,964,017 shares at June 30, 2013 and December 31, 2012, respectively	(45,918)	(39,918)
Accumulated other comprehensive loss	(29,712)	(39,305)
Total stockholders' equity	316,427	310,309
Total liabilities and stockholders' equity	\$ 808,362	\$ 789,966

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)**

	Three Months Ended		Six Months Ended	
	June 30, 2013	June 30, 2012	June 30, 2013	June 30, 2012
Net sales	\$ 215,289	\$ 202,634	\$ 420,587	\$ 379,636
Cost of sales	144,241	139,776	283,796	266,863
Gross profit	71,048	62,858	136,791	112,773
Selling, general and administrative expenses	19,709	20,093	39,500	38,302
Research and development expenses	21,131	19,762	41,713	39,593
Restructuring and impairment charges			2,446	
Operating income	30,208	23,003	53,132	34,878
Other income (expenses)				
Interest expense, net	(5,879)	(5,619)	(11,728)	(11,199)
Foreign currency gain (loss), net	(20,978)	(10,586)	(43,536)	523
Other	(230)	701	(490)	790
	(27,087)	(15,504)	(55,754)	(9,886)
Income (loss) before income taxes	3,121	7,499	(2,622)	24,992
Income tax expenses (benefits)	(1,315)	3,159	347	5,389
Net income (loss)	\$ 4,436	\$ 4,340	\$ (2,969)	\$ 19,603
Earnings (loss) per common share				
Basic	\$ 0.13	\$ 0.12	\$ (0.08)	\$ 0.53
Diluted	\$ 0.12	\$ 0.12	\$ (0.08)	\$ 0.52
Weighted average number of shares				
Basic	35,474,001	36,713,569	35,506,527	37,118,848
Diluted	37,125,005	37,566,699	35,506,527	37,916,149

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)**

	Three Months Ended		Six Months Ended	
	June 30,	June 30,	June 30,	June 30,
	2013	2012	2013	2012
Net income (loss)	\$ 4,436	\$ 4,340	\$ (2,969)	\$ 19,603
Other comprehensive income				
Unrealized gain (loss) on investments, net of tax	137	(106)	365	(27)
Derivative adjustments, net of tax	(5,068)	(690)	(9,579)	884
Foreign currency translation adjustments	9,674	7,566	18,807	(746)
Total comprehensive income	\$ 9,179	\$ 11,110	\$ 6,624	\$ 19,714

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

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MAGNACHIP SEMICONDUCTOR CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS EQUITY

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

	Common Stock		Additional Paid-In Capital	Retained Earnings (Accumulated deficit)	Common Stock Held in Treasury	Accumulated Other Comprehensive Income (loss)	Total
	Shares	Amount					
Three Months Ended June 30, 2013							
Balance at April 1, 2013	35,408,032	\$ 397	\$ 103,310	\$ 279,846	\$ (45,918)	\$ (34,455)	\$ 303,180
Stock-based compensation			493				493
Exercise of stock options	98,863	1	824				825
Exercise of warrants	174,487	2	2,748				2,750
Comprehensive income:							
Net income				4,436			4,436
Fair valuation of derivatives						(5,063)	(5,063)
Reclassification to net income from accumulated other comprehensive loss related to hedge derivatives						(5)	(5)
Foreign currency translation adjustments						9,674	9,674
Unrealized gains on investments						137	137
Total comprehensive income							9,179
Balance at June 30, 2013	35,681,382	\$ 400	\$ 107,375	\$ 284,282	\$ (45,918)	\$ (29,712)	\$ 316,427
Six Months Ended June 30, 2013							
Balance at January 1, 2013	35,635,357	\$ 396	\$ 101,885	\$ 287,251	\$ (39,918)	\$ (39,305)	\$ 310,309
Stock-based compensation			913				913
Exercise of stock options	246,673	2	1,817				1,819
Exercise of warrants	175,236	2	2,760				2,762
Acquisition of treasury stock	(375,884)				(6,000)		(6,000)
Comprehensive income:							
Net loss				(2,969)			(2,969)
Fair valuation of derivatives						(9,270)	(9,270)
Reclassification to net loss from accumulated other comprehensive loss related to hedge derivatives						(309)	(309)
Foreign currency translation adjustments						18,807	18,807
Unrealized gains on investments						365	365
Total comprehensive income							6,624
Balance at June 30, 2013	35,681,382	\$ 400	\$ 107,375	\$ 284,282	\$ (45,918)	\$ (29,712)	\$ 316,427

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

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MAGNACHIP SEMICONDUCTOR CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS EQUITY

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

	Common Stock		Additional Paid-In Capital	Retained Earnings (Accumulated deficit)	Common Stock Held in Treasury	Accumulated Other Comprehensive Income (loss)	Total
	Shares	Amount					
Three Months Ended June 30, 2012							
Balance at April 1, 2012	36,880,879	\$ 394	\$ 99,495	\$ 109,213	\$ (23,728)	\$ (21,469)	\$ 163,905
Stock-based compensation			457				457
Issuance of new stock	1,650		18				18
Exercise of stock options	9,625	1	57				58
Acquisitions of treasury stock	(538,609)				(5,000)		(5,000)
Comprehensive income:							
Net income				4,340			4,340
Fair valuation of derivatives						(2,187)	(2,187)
Reclassification to net income from accumulated other comprehensive loss related to hedge derivatives						1,497	1,497
Foreign currency translation adjustments						7,566	7,566
Unrealized losses on investments						(106)	(106)
Total comprehensive income							11,110
Balance at June 30, 2012	36,353,545	\$ 395	\$ 100,027	\$ 113,553	\$ (28,728)	\$ (14,699)	\$ 170,548
Six Months Ended June 30, 2012							
Balance at January 1, 2012	37,907,575	\$ 394	\$ 98,929	\$ 93,950	\$ (11,793)	\$ (14,810)	\$ 166,670
Stock-based compensation			915				915
Issuance of new stock	2,468		26				26
Exercise of stock options	26,755	1	157				158
Acquisition of treasury stock	(1,583,253)				(16,935)		(16,935)
Comprehensive income:							
Net income				19,603			19,603
Fair valuation of derivatives						(645)	(645)
Reclassification to net income from accumulated other comprehensive loss related to hedge derivatives						1,529	1,529
Foreign currency translation adjustments						(746)	(746)
Unrealized losses on investments						(27)	(27)
Total comprehensive income							19,714
Balance at June 30, 2012	36,353,545	\$ 395	\$ 100,027	\$ 113,553	\$ (28,728)	\$ (14,699)	\$ 170,548

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)**

	Six Months Ended	
	June 30,	June 30,
	2013	2012
Cash flows from operating activities		
Net income (loss)	\$ (2,969)	\$ 19,603
Adjustments to reconcile net income to net cash provided by operating activities		
Depreciation and amortization	16,881	15,397
Provision for severance benefits	10,686	10,975
Amortization of debt issuance costs and original issue discount	568	497
Loss on foreign currency translation, net	55,008	55
Gain on disposal of property, plant and equipment, net	(26)	(190)
Loss on disposal of intangible assets, net	1	15
Restructuring and impairment charges	618	
Stock-based compensation	913	915
Other	1,411	(348)
Changes in operating assets and liabilities		
Accounts receivable	(29,486)	(8,296)
Inventories	6,760	(11,498)
Other receivables	600	(2,580)
Other current assets	7,425	8,851
Deferred tax assets	(995)	1,146
Accounts payable	853	14,654
Other accounts payable	(7,522)	9,677
Accrued expenses	(7,003)	7,890
Other current liabilities	(1,097)	6,611
Payment of severance benefits	(2,939)	(4,816)
Other	(1,107)	(1,996)
Net cash provided by operating activities	48,580	66,562
Cash flows from investing activities		
Decrease in restricted cash	122	1,634
Proceeds from disposal of plant, property and equipment	27	891
Purchase of plant, property and equipment	(39,890)	(46,728)
Payment for intellectual property registration	(243)	(565)
Payment for purchase of Dawin, net of cash acquired		(8,642)
Decrease in short-term financial instruments		173
Collection of guarantee deposits	117	70
Payment of guarantee deposits	(939)	(176)
Other	11	(53)
Net cash used in investing activities	(40,795)	(53,396)
Cash flows from financing activities		
Proceeds from issuance of common stock	4,581	183
Repayment of obligations under capital lease		(2,968)
Acquisition of treasury stock	(6,000)	(16,935)

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Net cash used in financing activities	(1,419)	(19,720)
Effect of exchange rates on cash and cash equivalents	4,037	207
Net increase (decrease) in cash and cash equivalents	10,403	(6,347)
Cash and cash equivalents		
Beginning of the period	182,238	162,111
End of the period	\$ 192,641	\$ 155,764
Supplemental cash flow information		
Cash paid for interest	\$ 10,694	\$ 10,737
Cash paid (refunded) for income taxes	\$ 6,345	\$ (684)

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

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MagnaChip Semiconductor Corporation and Subsidiaries

Notes to Consolidated Financial Statements

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

1. General

The Company

MagnaChip Semiconductor Corporation (together with its subsidiaries, the Company) is a Korea-based designer and manufacturer of analog and mixed-signal semiconductor products for high-volume consumer applications. The Company's business is comprised of three key segments: Display Solutions, Power Solutions and Semiconductor Manufacturing Services. The Company's Display Solutions products include display drivers for use in a wide range of flat panel displays and mobile multimedia devices. The Company's Power Solutions products include discrete and integrated circuit solutions for power management in high-volume consumer applications. The Company's Semiconductor Manufacturing Services segment provides specialty analog and mixed-signal foundry services for fabless semiconductor companies that serve the consumer, computing and wireless end markets.

2. Significant Accounting Policies

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 presentation 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, 2013 are not necessarily indicative of the results to be expected for a full year or for any other periods.

The December 31, 2012 balance sheet data was derived from audited financial statements, but does not include all disclosures required by US GAAP.

Recent Accounting Pronouncements

In July 2013, the FASB issued ASU No. 2013-11, *Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists* (ASU 2013-11). The adoption of ASU 2013-11 will require an unrecognized tax benefit, or a portion of an unrecognized tax benefit to be presented in the financial statements as a reduction to a deferred tax asset for a net operating loss carryforward, a similar tax loss, or a tax credit carryforward, unless an exception applies. The amendments in this update are effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2013. The Company is currently evaluating the effect that the provisions of ASU 2013-11 will have on its financial statements.

In February 2013, the FASB issued ASU No. 2013-02, *Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income*, (ASU 2013-02) which requires an entity to provide information about the amounts reclassified out of accumulated other comprehensive income by component. In addition, ASU 2013-02 requires an entity to present, either on the face of the income statement or in the notes to financial statements, significant amounts reclassified out of accumulated other comprehensive income by the respective line items of net income but only if the amount reclassified is required under GAAP to be reclassified to net income in its entirety in the same reporting period. For other amounts, an entity is required to cross-reference to other disclosures required under GAAP that provide additional detail about those amounts. The update does not change the current requirements for reporting net income or other comprehensive income in financial statements and is effective prospectively for reporting periods beginning after December 15, 2012. The Company adopted ASU 2013-02 from the quarter ended March 31, 2013.

In December 2011, the FASB issued ASU No. 2011-11, *Disclosures about Offsetting Assets and Liabilities*, (ASU 2011-11) which is effective for annual reporting periods beginning on or after January 1, 2013, and interim periods within those annual periods. This authoritative guidance was issued to enhance disclosure requirements on offsetting financial assets and liabilities. The new rules require the Company to disclose both gross and net information about instruments and transactions eligible for offset in the statement of financial position, as well as instruments and

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transactions subject to a netting arrangement. In January 2013, the FASB further issued ASU No. 2013-01, Clarifying the Scope of Disclosures about Offsetting Assets and Liabilities (ASU 2013-01) to address implementation issues surrounding the scope of ASU 2011-11 and to clarify the scope of the offsetting disclosures and address any unintended consequences. The Company adopted ASU 2013-01 from the quarter ended March 31, 2013.

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

In July 2012, the FASB issued ASU No.2012-02, Testing Indefinite-Lived Intangible Assets for Impairment (ASU 2012-02). Under ASU 2012-02, testing the decline in the realizable value (impairment) of indefinite-lived intangible assets other than goodwill has been simplified. ASU 2012-02 provides the Company the option to first assess qualitative factors to determine whether it is necessary to perform the quantitative impairment test. The Company electing to perform a qualitative assessment is no longer required to calculate the fair value of an indefinite-lived intangible asset unless the Company determines, based on a qualitative assessment, that it is more likely than not that the asset is impaired. ASU 2012-02 is effective for impairment tests for fiscal years beginning after September 15, 2012. The Company adopted ASU 2012-02 from the year ended December 31, 2012.

In September 2011, the FASB issued ASU No. 2011-08, Intangibles-Goodwill and Other (Topic 350)-Testing Goodwill for Impairment (ASU 2011-08). ASU 2011-08 gives the option to first assess qualitative factors to determine if it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If, after assessing the totality of events or circumstances, an entity determines it is not more likely than not that the fair value of a reporting unit is less than its carrying amount, then performing the two-step impairment test is unnecessary. However, if an entity concludes otherwise, then it is required to perform the first step of the two-step impairment test by calculating the fair value of the reporting unit. Under the amendments in ASU 2011-08, an entity has the option to bypass the qualitative assessment for any reporting unit in any period and proceed directly to performing the first step of the two-step goodwill impairment test. An entity may resume performing the qualitative assessment in any subsequent period. The amendments in ASU 2011-08 are effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2011. Early adoption is permitted. The Company adopted the applicable requirements of ASU 2011-08 from the year ended 2012.

3. Sales of Accounts Receivable

The Company has entered into an agreement to sell selected trade accounts receivable to a financial institution. 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 \$20,121 thousand and \$8,412 thousand for the six month period ended June 30, 2013 and 2012, respectively and these sales resulted in a pre-tax loss of \$42 thousand and \$4 thousand for the six month period ended June 30, 2013 and 2012, respectively which is 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.

4. Inventories

Inventories as of June 30, 2013 and December 31, 2012 consist of the following:

	June 30, 2013	December 31, 2012
Merchandise	\$ 6	\$ 7
Finished goods	12,935	14,551
Semi-finished goods and work-in-process	52,739	61,202
Raw materials	9,277	11,426
Materials in-transit	1,385	2,177
Inventories, net	\$ 76,342	\$ 89,363

Table of Contents**MagnaChip Semiconductor Corporation and Subsidiaries****Notes to Consolidated Financial Statements (Continued)****(Unaudited; tabular dollars in thousands, except share data)****5. Property, Plant and Equipment**

Property, plant and equipment as of June 30, 2013 and December 31, 2012 comprise the following:

	June 30, 2013	December 31, 2012
Buildings and related structures	\$ 74,685	\$ 79,822
Machinery and equipment	252,686	221,927
Vehicles and others	18,588	17,143
Equipment under capital lease		12,181
	345,959	331,073
Less: accumulated depreciation	(114,695)	(106,271)
accumulated depreciation on equipment under capital lease		(3,697)
Land	15,978	17,151
Property, plant and equipment, net	\$ 247,242	\$ 238,256

6. Intangible Assets

Intangible assets as of June 30, 2013 and December 31, 2012 are as follows:

	June 30, 2013	December 31, 2012
Technology	\$ 20,540	\$ 25,011
Customer relationships	27,027	29,010
Intellectual property assets	6,925	7,145
Less: accumulated amortization	(47,555)	(49,266)
Goodwill	3,131	3,360
Intangible assets, net	\$ 10,068	\$ 15,260

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, MagnaChip Semiconductor, Ltd., entered into option, forward and 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, 2013 are as follows:

Date of transaction	Type of derivative	Total notional amount	Month of settlement
December 14, 2012	Zero cost collar	\$ 54,000	July to September 2013
December 27, 2012	Zero cost collar	\$ 54,000	October to December 2013
January 25, 2013	Zero cost collar	\$ 54,000	January to March 2014
March 8, 2013	Zero cost collar	\$ 54,000	April to June 2014
April 5, 2013	Zero cost collar	\$ 54,000	July to September 2014
May 29, 2013	Forward	\$ 30,000	July to September 2013
May 29, 2013	Zero cost collar	\$ 54,000	October to December 2014
June 21, 2013	Forward	\$ 30,000	October to December 2013

The option, forward and 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 forward and zero cost collar contracts recorded as assets and liabilities as of June 30, 2013 and December 31, 2012 are as follows:

		June 30, 2013	December 31, 2012
Derivatives designated as hedging instruments:			
Asset Derivatives:			
Forward	Other current assets	\$ 117	\$ 514
Liability Derivatives:			
Forward	Derivative liabilities	\$ 502	\$
Zero cost collars	Derivative liabilities	9,745	
Zero cost collars	Other non-current liabilities	1,604	

Offsetting of derivative assets and derivative liabilities as of June 30, 2013 and December 31, 2012 is as follows:

As of June 30, 2013	Gross amounts of recognized assets/liabilities	Gross amounts offset in the balance sheets	Net amounts of assets/liabilities presented in the balance sheets	Gross amounts not offset in the balance sheets Financial instruments received/pledged	Cash collateral received/pledged	Net amount
Asset Derivatives:						
Forward	\$ 117	\$	\$ 117	\$ (117)	\$	\$

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Liability Derivatives:					
Forward	\$	502	\$	\$	502
Zero cost collars		11,349	\$	11,349	(117)
					\$ 502
					11,232

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

As of December 31, 2012	Gross amounts of recognized assets/liabilities	Gross amounts offset in the balance sheets	Net amounts of assets/liabilities presented in the balance sheets	Financial instruments	Gross amounts not offset in the balance sheets	Cash collateral received/pledged	Net amount
Asset Derivatives:							
Zero cost collars	\$ 514	\$	\$ 514	\$	\$		\$ 514
Liability Derivatives:							
Zero cost collars	\$	\$	\$	\$	\$		\$

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 either hedge ineffectiveness or hedge components excluded from the assessment of effectiveness, are recognized in current earnings.

The following table summarizes the impact of derivative instruments on the consolidated statement of operations for the three months ended June 30, 2013 and 2012:

Derivatives in ASC 815	Amount of Gain (Loss) Recognized in AOCI on Derivatives (Effective Portion)		Location of Gain (Loss) Reclassified from AOCI into Statement of Income (Effective Portion)	Amount of Gain (Loss) Reclassified from AOCI into Statement of Income (Effective Portion)		Location of Gain (Loss) Recognized in Statement of Income on Derivative (Ineffective Portion and Amount Excluded from Effectiveness Testing)	Amount of Gain (Loss) Recognized in Statement of Income on Derivatives (Ineffective Portion and Amount Excluded from Effectiveness Testing)	
	2Q, 2013	2Q, 2012		2Q, 2013	2Q, 2012		2Q, 2013	2Q, 2012
Cash Flow Hedging Relationships								
Forward	\$ (214)	\$ (1,552)	Net sales	\$	\$	Other income (expenses) Others	\$ (107)	\$ 529
Zero cost collars	(4,849)	(635)	Net sales	5	(1,497)	Other income (expenses) Others	(124)	172
Total	\$ (5,063)	\$ (2,187)		\$ 5	\$ (1,497)		\$ (231)	\$ 701

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 six months ended June 30, 2013 and 2012:

Derivatives in ASC 815	Amount of Gain (Loss)		Location of Gain (Loss)	Amount of Gain (Loss)		Location of Gain (Loss)	Amount of Gain (Loss)	
	Recognized in AOCI on Derivatives (Effective Portion)		Reclassified from AOCI into Statement of Income (Effective Portion)	Reclassified from AOCI into Statement of Income (Effective Portion)		Recognized in Statement of Income on Derivative (Ineffective Portion and Amount Excluded from Effectiveness Testing)	Recognized in Statement of Income on Derivatives (Ineffective Portion and Amount Excluded from Effectiveness Testing)	
	1H, 2013	1H, 2012		1H, 2013	1H, 2012		1H, 2013	1H, 2012
Cash Flow Hedging Relationships								
Forward	\$ (214)	\$ (385)	Net sales	\$	\$	Other income (expenses) Others	\$ (107)	\$ 513
Zero cost collars	(9,056)	(260)	Net sales	309	(1,529)	Other income (expenses) Others	(391)	273
Total	\$ (9,270)	\$ (645)		\$ 309	\$ (1,529)		\$ (498)	\$ 786

The estimated net loss as of June 30, 2013 that is expected to be reclassified from accumulated other comprehensive income (loss) into earnings within the next twelve months is \$7,661 thousand.

The Company's option, forward and zero cost collar contracts are subject to termination upon the occurrence of the following events:

- (i) On the last day of a fiscal quarter, the sum of qualified and unrestricted cash and cash equivalents held by the Company is less than \$30 million.
- (ii) The rating of the Company's debt is B- or lower by Standard & Poor's Ratings Group or any successor rating agency thereof (S&P) or B3 or lower by Moody's Investor Services, Inc. or any successor rating agency thereof (Moody's) or the Company's debt ceases to be assigned a rating by either S&P or Moody's.

In addition, the Company is required to deposit cash collateral with two financial institutions, the counterparties to the option, forward and zero cost collar contracts, for any exposure in excess of \$5 million for each financial institution. No cash collateral was required as of June 30, 2013.

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 assets and liabilities measured at fair value on a recurring basis as of June 30, 2013, 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)
Assets:					
Available-for-sale securities	\$ 1,027	\$ 1,027	\$ 1,027	\$	\$
Other current assets	117	117		117	
Liabilities:					
Derivative liabilities	10,247	10,247		10,247	
Other non-current liabilities	1,604	1,604		1,604	

As of June 30, 2013, the total carrying value and estimated fair value of the Company's subsidiaries' 10.500% Senior Notes due 2018 (the 2018 Notes) which are not measured at fair value on a recurring basis were \$201,801 thousand and \$222,532 thousand, respectively. The estimated fair value is based on Level 2 inputs.

9. Accrued Severance Benefits

The majority of accrued severance benefits is for employees in the Company's Korean subsidiary, MagnaChip Semiconductor Ltd. Pursuant to the Employee Retirement Benefit Security Act of Korea, most 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, 2013, 98.3 % of employees of the Company were eligible for severance benefits.

Changes in accrued severance benefits for each period are as follows:

	Three Months Ended June 30, 2013	Six Months Ended June 30, 2013	Three Months Ended June 30, 2012	Six Months Ended June 30, 2012
Beginning balance	\$ 112,940	\$ 113,624	\$ 95,472	\$ 91,882
Provisions	6,458	10,687	6,272	10,975
Severance payments	(2,312)	(2,939)	(2,493)	(4,816)
Translation adjustments	(3,800)	(8,086)	(1,284)	(74)
	113,286	113,286	97,967	97,967
Less: Cumulative contributions to the National Pension Fund	(361)	(361)	(372)	(372)
Group Severance insurance plan	(727)	(727)	(712)	(712)
Accrued severance benefits, net	\$ 112,198	\$ 112,198	\$ 96,883	\$ 96,883

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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.

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

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

	Severance benefit
Remainder of 2013	\$
2014	337
2015	343
2016	1,236
2017	1,554
2018	2,788
2019 - 2023	19,396

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.

10. Foreign Currency Gain (Loss), Net

Net foreign currency gain or loss includes non-cash translation gain or loss associated with intercompany balances.

11. Restructuring and Impairment Charges

The Company recognized \$1,829 thousand of restructuring charges for the six months ended June 30, 2013 from restructuring one of the Company's fabrication facilities and \$617 thousand of impairment charges from certain existing technology.

12. Income Taxes

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

MagnaChip Semiconductor Ltd. (Korea) is the principal operating entity within the consolidated Company. For the three and six months ended June 30, 2013, income tax benefit for MagnaChip Semiconductor, Ltd. (Korea) was recorded due to the adjustment of deferred tax assets. The Company assesses 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, the Company considers 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.

Income tax benefit and income tax expense recorded for the three month period ended June 30, 2013 and 2012 was \$1,315 thousand and \$3,159 thousand, respectively, and income tax expense for the six month period ended June 30, 2013 and 2012 was \$347 thousand and \$5,389 thousand, respectively.

Table of Contents**MagnaChip Semiconductor Corporation and Subsidiaries****Notes to Consolidated Financial Statements (Continued)****(Unaudited; tabular dollars in thousands, except share data)****13. Geographic and Division Information**

The following is a summary of net sales by product division:

	Three Months Ended	
	June 30,	June 30,
	2013	2012
Net Sales		
Display Solutions	\$ 68,867	\$ 76,784
Semiconductor Manufacturing Services	109,751	91,318
Power Solutions	35,959	33,699
All other	712	833
 Total net sales	 \$ 215,289	 \$ 202,634

	Six Months Ended	
	June 30,	June 30,
	2013	2012
Net Sales		
Display Solutions	\$ 139,190	\$ 160,009
Semiconductor Manufacturing Services	213,890	159,180
Power Solutions	66,142	58,952
All other	1,365	1,495
 Total net sales	 \$ 420,587	 \$ 379,636

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

	Three Months Ended	
	June 30,	June 30,
	2013	2012
Korea	\$ 101,525	\$ 94,385
Asia Pacific	73,135	73,215
U.S.A.	26,943	25,714
Europe	12,866	8,385
Other	820	935
 Total	 \$ 215,289	 \$ 202,634

	Six Months Ended	
	June 30, 2013	June 30, 2012
Korea	\$ 196,027	\$ 192,336
Asia Pacific	142,872	132,450
U.S.A.	55,327	39,067
Europe	24,595	13,950
Other	1,766	1,833
 Total	 \$ 420,587	 \$ 379,636

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MagnaChip Semiconductor Corporation and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

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

Net sales from the Company's top ten largest customers accounted for 65.5 % and 64.0% for the three months ended June 30, 2013 and 2012, respectively, and 67.0% and 62.6% for the six months ended June 30, 2013 and 2012, respectively.

For the three months ended June 30, 2013, we had one customer which represented 15.2% of the Company's net sales, and for the six months ended June 30, 2013, we had two customers which represented 13.9% and 10.0%, respectively.

For the three months ended June 30, 2012, we had one customer which represented 12.3% of the Company's net sales, and for the six months ended June 30, 2012, we had two customers which represented 13.0% and 11.3%, respectively.

Over 99% of the Company's property, plant and equipment are located in Korea as of June 30, 2013.

14. Accumulated Other Comprehensive Loss

Accumulated other comprehensive loss consists of the following as of June 30, 2013 and December 31, 2012, respectively:

June&nbs