

MAGNACHIP SEMICONDUCTOR LLC

Form 10-K

March 30, 2007

Table of Contents

---

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

---

**FORM 10-K**

---

(Mark one)

**Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**  
For the fiscal year ended December 31, 2006

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 333-126019-09

---

**MAGNACHIP SEMICONDUCTOR LLC**

(Exact name of Registrant as specified in its charter)

---

**Delaware**  
(State or other jurisdiction of

incorporation or organization)

c/o MagnaChip Semiconductor S.A.

74, rue de Merl, B.P. 709, L-2017

Luxembourg, Grand Duchy of Luxembourg

**83-0406195**  
(I.R.S. Employer

Identification No.)

Not Applicable

Edgar Filing: MAGNACHIP SEMICONDUCTOR LLC - Form 10-K

(Address of principal executive offices)

(Zip Code)

Registrant's telephone number, including area code: (352) 45-62-62

---

Securities registered pursuant to Section 12(b) of the Act: None.

Securities registered pursuant to Section 12(g) of the Act: None.

---

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes  No

**Note** Checking the box above will not relieve any registrant required to file reports pursuant to Section 13 or 15(d) of the Exchange Act from their obligations under those Sections.

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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer  Accelerated filer  Non-accelerated filer   
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes  No

State the aggregate market value of the voting and non-voting common equity held by non-affiliates computed by reference to the price at which the common equity was last sold, or the average bid and asked price of such common equity, as of the last business day of the registrant's most recently completed second fiscal quarter. **Not applicable.**

As of March 1, 2007, the registrant had 52,720,784.047 of the registrant's common units outstanding.

---

**Table of Contents**

**Supplemental Information to be Furnished With Reports Filed Pursuant to Section 15(d) of the Act by Registrants Which Have Not Registered Securities Pursuant to Section 12 of the Act.**

No annual report or proxy statement, form of proxy or other proxy soliciting material with respect to any annual or other meeting of security holders has been sent to security holders.

**Table of Contents**

**MAGNACHIP SEMICONDUCTOR LLC**

**2006 FORM 10-K ANNUAL REPORT**

**TABLE OF CONTENTS**

**PART I**

Item 1	<u>Business</u>	2
Item 1A	<u>Risk Factors</u>	10
Item 1B	<u>Unresolved Staff Comments</u>	16
Item 2	<u>Properties</u>	16
Item 3	<u>Legal Proceedings</u>	17
Item 4	<u>Submission of Matters to a Vote of Security Holders</u>	17

**PART II**

Item 5	<u>Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities</u>	18
Item 6	<u>Selected Financial Data</u>	19
Item 7	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	21
Item 7A	<u>Quantitative and Qualitative Disclosures About Market Risk</u>	34
Item 8	<u>Financial Statements and Supplementary Data</u>	35
Item 9	<u>Changes in and Disagreements With Accountants on Accounting and Financial Disclosure</u>	76
Item 9A	<u>Controls and Procedures</u>	76
Item 9B	<u>Other Information</u>	77

**PART III**

Item 10	<u>Directors, Executive Officers and Corporate Governance</u>	78
Item 11	<u>Executive Compensation</u>	81
Item 12	<u>Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters</u>	92
Item 13	<u>Certain Relationships and Related Transactions, and Director Independence</u>	96
Item 14	<u>Principal Accounting Fees and Services</u>	97

**PART IV**

Item 15	<u>Exhibits and Financial Statement Schedules</u>	98
	<u>SIGNATURES</u>	104

**Table of Contents**

**PART I**

**INDUSTRY AND MARKET DATA**

In this report, we rely on and refer to information regarding the semiconductor market from iSuppli, DisplaySearch, and other third-party sources. Market data attributed to iSuppli are from CCD and CMOS Image Sensors: Handset Market Driving the Industry, Consumer Platforms Topical Report Q4 2006 dated October 2005, Pure Play Foundry Market Tracker H2 2006, and Much Room for Growth Before Display Driver Market Matures: Display Driver ICs Market Tracker Q4 2006. Market data attributed to DisplaySearch are from Quarterly Global TV Shipment & Forecast Data Tables Q4 2006, Quarterly Desktop MNT Shipment & Forecast Data Tables Q4 2006, and Quarterly NBPC Shipment & Forecast Data Table Q4 2006. Although we believe that this information is reliable, we cannot guarantee the accuracy and completeness of the information and have not independently verified it. As a result, you should be aware that market and other similar data set forth herein, and estimates and beliefs based on such data, may not be reliable. We do not have any obligation to announce or otherwise make publicly available updates or revisions to these forecasts. In many cases, we have made statements in this report regarding our industry and our position in the industry based on our experience in the industry and our own investigation of market conditions. We cannot assure you that any of these assumptions are accurate or that our assumptions correctly reflect our position in our industry.

**SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS**

This report includes forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. These forward-looking statements represent expectations or beliefs of ours concerning future events, and no assurance can be given that the results described in this report will be achieved. These forward-looking statements can generally be identified by the use of statements that include words such as estimate, project, believe, expect, anticipate, intend, plan, likely, may, will, should or other similar words or phrases. All forward-looking statements are based upon information available to us on the date of this report.

These forward-looking statements are subject to risks, uncertainties and other factors, many of which are outside of our control, that could cause actual results to differ materially from the results discussed in the forward-looking statements, including, among other things, the matters discussed in this report in the sections captioned: Business, Risk factors and Management's discussion and analysis of financial condition and results of operations. There may be other factors that could cause our actual results to differ materially from the results referred to in the forward-looking statements. All forward-looking statements attributable to us or persons acting on our behalf apply only as of the date of this report and are expressly qualified in their entirety by the cautionary statements included in this report. We undertake no obligation to publicly update or revise forward-looking statements to reflect events or circumstances after the date made or to reflect the occurrence of unanticipated events. Readers are urged to carefully review and consider the various disclosures made in this report which attempt to advise interested parties of the risks and factors that may affect our business, financial condition, results of operations and prospects.

---

MagnaChip and IC Media are our trademarks and trade names. All other trademarks, trade names, and service marks appearing in this report are the property of their respective owners.

---

---

**Table of Contents**

**Item 1. Business.**

**BUSINESS**

**Overview**

MagnaChip Semiconductor LLC (MagnaChip or the Company) is a leading designer, developer and manufacturer of mixed-signal and digital multimedia semiconductors addressing the convergence of consumer electronics and communications devices. We focus on Complementary Metal-Oxide Semiconductor (CMOS) image sensors and flat panel display drivers, which are complex, high-performance mixed-signal semiconductors that capture and display images and enable and enhance the features and capabilities of both small and large flat panel displays. Our solutions are used in a wide variety of consumer and commercial mass market applications, such as mobile handsets, including camera-equipped mobile handsets, flat panel monitors and televisions, consumer home and mobile displays, portable and desktop computer displays, handheld gaming devices, PDAs and audio-visual equipment such as DVD players. We serve consumer markets that we believe will have higher growth rates than those of the overall semiconductor industry.

We manufacture our products using our proprietary process technology, which we believe provides our products with cost advantages over those of our competitors. We have approximately 8,500 registered and pending patents. We believe that our proprietary in-house CMOS image sensor technology allows us to tailor our process to create brighter, sharper, more colorful picture quality in image-capture applications such as camera-equipped mobile handsets. Our flat panel display drivers enable our customers to deliver higher image quality, thinner and more power-efficient small panel displays for use in mobile handsets, handheld gaming devices and PDAs and large panel displays for use in portable and desktop computer monitors and digital televisions. We are also a leading provider of wafer foundry services whereby we leverage our specialized process technologies and low cost manufacturing facilities to produce semiconductors for third parties using their product designs.

We own and operate five wafer fabrication facilities, or fabs, which have a combined production capacity of over 119,000 eight-inch equivalent wafers per month. Our fabs provide us with large-scale, cost-effective and flexible capacity, enabling us to rapidly scale to high volume to meet shifts in demand by our end customers. Our fabs also provide us with the ability to further develop our differentiated process technologies for our own product development and manufacturing. The location of our manufacturing sites in Korea and research and development resources in Korea, Japan, and the United States provide close geographical proximity to many of our largest customers and to the core of the worldwide consumer electronics supply chain.

We sell our solutions to leading original equipment manufacturers, or OEMs, which include major branded customers as well as contract manufacturers. Our CMOS image sensors are currently designed into products offered by leading global mobile handset manufacturers. Our flat panel display drivers are currently incorporated into products offered by top flat panel display manufacturers. During the year ended December 31, 2006, we sold over 2,200 products to more than 240 customers.

In the three-month period ended December 31, 2004, and the fiscal years ended December 31, 2005, and December 31, 2006, we derived respectively 23.9%, 17.4%, and 8.1% of our consolidated revenue from CMOS image sensors, 24.8%, 34.8%, and 36.8% from flat panel display drivers, and 36.2%, 36.8%, and 46.0% from semiconductor manufacturing services.

**The Original Acquisition**

Our business was named MagnaChip Semiconductor when it was acquired from Hynix Semiconductor Inc. on October 6, 2004, by Citigroup Venture Capital Equity Partners, L.P. (now known as Court Square Capital Partners, but referred to herein as CVC), Francisco Partners L.P., or Francisco Partners, CVC Asia Pacific Limited, or CVC Asia Pacific, certain members of management and other investors, following discussions with

## **Table of Contents**

Hynix that began in late 2001 and the execution of a definitive agreement in June 2004. Previously, we were the System IC division within Hynix which, in 1999, had been formed from the Hyundai Electronics and LG Semiconductor System IC businesses and can trace its history back to the late 1970s. We refer to the acquisition transaction, including the related definitive agreements with Hynix, as the Original Acquisition.

### **Divestment of Application Processor Business**

On January 31, 2006, we completed the sale of our application processor business to ABOV Semiconductor Co., Ltd., a new independent entity formed by the investors in GreenChips Co., Ltd., a Korean semiconductor solution provider. The application processor business primarily included assets, staff, and intellectual property related to MagnaChip's 8-bit and 32-bit microcontroller, SmartCard controller, microperipheral IC, and linear IC product lines. MagnaChip retained a 2.3% equity stake in the new entity, and our semiconductor manufacturing services business continues to provide wafer foundry services for ABOV Semiconductor.

### **Competitive Strengths**

We believe that our competitive strengths include:

*Leading Technology and Intellectual Property.* We believe our advanced process technology and portfolio of approximately 8,500 registered and pending patents provide us with key competitive advantages in the following areas:

*CMOS image sensors:* Our CMOS image sensors feature low power consumption and currently up to 3.2 megapixel resolution with auto-focus and auto-zoom options; features which provide important benefits to products incorporating our solutions, including increased battery life, enhanced image quality and ease of use.

*Flat panel display drivers:* We believe that our flat panel display drivers offer superior performance in shaping image signals and transmitting those signals to flat panel displays. These technical features result in sharper, brighter and higher-quality colored images in our customers' end products. Furthermore, we believe that our flat panel display drivers enable thinner and more power-efficient flat panels that are easily integrated by our customers into their products.

*Semiconductor manufacturing services:* We have developed high-voltage, analog power and embedded memory specialty manufacturing process technologies that enable us to manufacture differentiated, high performance integrated semiconductor devices. For example, we developed the first high-voltage, high-performance CMOS 0.18  $\mu\text{m}$  process, which enables us to manufacture more integrated, and thus smaller and more cost-efficient, semiconductor products. We believe that our proprietary process technology allows us to meet a wide variety of the specialty semiconductor manufacturing needs of our customers.

*Flexible In-House Manufacturing.* Our in-house wafer manufacturing capacity allows us to provide dependable delivery and quality of integrated semiconductor products to our customers. We have the ability to ramp quickly to high volumes to meet the variable needs of our customers. We have significant wafer manufacturing capacity as a result of our former parent's investments in our wafer fabrication facilities. Because we offer specialty process technologies that do not require expensive investment in leading edge smaller geometry process equipment, we are able to keep our capital expenditures relatively low.

*Significant Cost Advantages.* We maintain price competitiveness on our products through our low cost operating structure. The Asian location of our primary manufacturing and research and development facilities provides us with a number of cost advantages relative to operating in other regions in the world. Additionally, we believe that our history of competing in the highly cost-sensitive markets in which we operated when we were a unit of Hynix required us to refine our manufacturing processes for optimal cost efficiency.

*Established Relationships With Key Consumer Electronics OEMs.* Our long history of operating in Asia and our proximity to leading communications and consumer OEMs facilitate our close customer relationships with

## **Table of Contents**

leading innovators in the consumer electronics market. We have active local applications and engineering work support programs for our customers and collaborate closely with our customers in the design and manufacturing of their products.

*Significant Management and Board Expertise.* Our management and Board of Directors have significant previous experience with advanced semiconductor companies both in Asia and worldwide. Our executives have many years of experience at such leading companies as Hynix, Samsung, Fairchild Semiconductor, and ChipPAC. In addition, two of our equity sponsors, CVC and Francisco Partners, have a long history of investments in semiconductor companies. We believe that their understanding of semiconductor system solutions, relationships, and credibility with key customers provides us with a key competitive advantage.

### **Business Strategy**

Our goal is to build upon our position as a leading provider of mixed-signal and digital multimedia semiconductors addressing the convergence of consumer electronics and communications devices. Our business strategy emphasizes the following key elements:

*Leverage Our Substantial Intellectual Property.* We intend to use our broad patent portfolio and specific end market expertise to deliver system-level products with higher levels of integration and performance to customers in our existing and new markets. In CMOS image sensors, we intend to leverage our strong pixel design and manufacturing expertise to introduce higher resolution, more integrated and cost-effective solutions for camera-equipped mobile handsets and to penetrate emerging applications for image sensors in the automotive, medical and industrial markets over time. In flat panel display drivers, we intend to leverage our broad library of circuit building blocks, our embedded memory capabilities, our understanding of the major flat panel display types and our process technology to continue to reduce time to market and introduce new products that enhance image quality and operate with greater power efficiency. Our manufacturing process expertise and related intellectual property underlies and supports many of the advances in our technology.

*Strengthen Collaboration With Key Customers.* We intend to continue strengthening and deepening relationships with our key customers by collaborating on critical design and product development roadmaps. We believe such collaborative relationships will solidify our position with our customers, further our competitive differentiation and accelerate our drive for deeper customer and new market penetration. For example, close collaboration with our mobile handset customers has allowed us to deliver improved interfaces between baseband and image processors, which have resulted in solutions with smaller form factors and improved image quality.

*Increase Large Account Penetration.* We have a global customer base consisting of leading consumer electronics OEMs and contract manufacturers. Many of our customers have multiple product variations that use image-capture and processing. We will seek to increase our customer penetration by taking advantage of our broad product portfolio and existing relationships to cross-sell existing products to our customers and to penetrate product variations where our solutions are currently not used.

*Broaden Our Customer Base.* We intend to expand our customer base across various applications and geographic locations by leveraging our position as a supplier to many of the largest global consumer electronics companies and delivering to potential customers proven, innovative solutions. We also believe that as consumer electronics and communications applications converge and proliferate, we will increasingly have opportunities to sell our products into new markets such as the automotive, medical and industrial markets. We also intend to expand our global sales presence to penetrate new accounts worldwide and grow existing account relationships. We will leverage our sales representatives and distributors located throughout Asia, the United States, and Europe to further these goals.

*Leverage Our Capital Light Business Model.* We acquired significant proprietary process technologies and wafer manufacturing capacity from our former parent, Hynix. We intend to leverage these investments made by



## **Table of Contents**

Hynix to drive our growth and margin improvement. Furthermore, we plan to continue to keep our capital expenditures relatively low by maintaining our focus on specialty process technologies that do not require expensive investment in leading edge technologies. If needed, we will access other foundries that provide such technology in the future. We believe this approach will lead to a higher return on invested capital.

### **Products and Services**

We have a balanced portfolio of products that address many of the most rapidly growing consumer electronics markets. We have determined, based on the nature of our operations and products offered to customers, that our reportable segments are Imaging Solutions, Display Solutions, and Semiconductor Manufacturing Services. The Imaging Solutions segment's primary products are CMOS image sensors, and the Display Solutions segment's primary products are flat panel display drivers. The Semiconductor Manufacturing Service segment provides wafer foundry services to clients.

*Imaging Solutions.* Our highly integrated image sensors are designed to be cost effective and to provide brighter, sharper, more colorful and, thus enhanced, image quality for use primarily in applications that require small form factors, low power consumption, effective heat dissipation and high reliability. Our image sensors fully satisfy these key criteria and are used in image capture applications such as camera-equipped mobile handsets and personal computer cameras. Our in-house manufacturing capabilities enable us to continuously fine tune our CMOS process technology to deliver improved image-capture sensitivity and accuracy.

CMOS image sensors are typically less expensive to produce and consume less power than other types of image sensors. Historically, CMOS image sensors were primarily used for low-cost applications for which high-image quality was not a priority. Recently, advances in semiconductor manufacturing processes and design techniques have led to improvements in CMOS image sensor performance and quality. As a result, CMOS image sensors have become useful, relatively low-cost solutions for use in applications such as camera-equipped mobile handsets and PDAs, where high-image quality, low power consumption, small size and low-cost are important considerations.

According to iSuppli, total worldwide image sensor revenue is expected to grow from \$6.56 billion to \$9.146 billion from 2006 to 2010, while unit shipments for area sensors such as our products will grow from 919 million units in 2006 to 1.538 billion units in 2010. Image sensor revenues for wireless electronics are forecasted by iSuppli to grow from 29% of the total revenue in 2006 to 64% by 2010. Conversely, revenues for consumer electronics will drop from 45% to 18% of the total market. Handsets accounted for 70% of all image sensor unit shipments in 2005 and will increase at a compound annual growth rate of 20% to account for 77% of all sensor shipments by 2010. Importantly, sensors for digital still cameras will only increase at a 5.8% compound annual growth rate from 98 million units in 2005, or 14.5% of the total, to 130 million units in 2010, or 8.4% of the total.

Our CMOS image sensors are characterized by a high level of integration. Many CMOS image sensors systems are made up of at least two integrated circuits: the CMOS image sensor itself and a separate image signal processor, or ISP. With the continuing demand for ever smaller camera-enabled devices, small size has become an increasingly important consideration for manufacturers of camera phones and similar products. Our products meet this demand for smaller form factors by integrating both our proprietary image sensor and image signal processor onto a single chip, thus occupying approximately half of the space required by multiple chip solutions, while providing equivalent or even superior image quality with lower power consumption and a lower overall cost.

We offer CMOS image sensors with resolutions of VGA, 1.0MP (megapixels), 1.3MP, 2.1MP and 3.2MP. Our solutions enable small form factor camera module implementations which are required for today's demanding industrial designs, such as very thin mobile phones. All of our solutions support both video and still capture modes, and provide sub-sampling modes to enable preview modes of operation with reduced power

## Table of Contents

consumption. The choice of resolution by an OEM customer may involve many factors such as size, power and cost target. By offering a full line of solutions, we can service our customer's requirements across the multiple end products they may offer.

Our imaging solutions segment received revenues of \$60.5 million and had a gross loss of \$4.0 million during the year ended December 31, 2006, revenues and gross profit of \$163.3 million and \$25.4 million during the year ended December 31, 2005, and revenues and gross profit of \$58.1 million and \$12.7 million during the three-month period ended December 31, 2004.

*Display Solutions.* Our flat panel display driver solutions are used in a wide variety of displays for mass market and commercial applications such as mobile handsets, handheld gaming devices, PDAs, displays for desktop and mobile computer monitors and flat panel televisions. We produce highly integrated flat panel display driver solutions and have pioneered developments in embedded memory and in the design and manufacturing of display drivers, enabling our customers to provide improved picture quality through thinner, smaller, more power-efficient displays.

Display drivers are the critical semiconductor components that enable the display's functionality. A display driver operates by interfacing with the host processor to generate the precise analog voltages and currents required to create images on the display. The performance characteristics of a display driver are critical to the quality and visual appeal of the images and text generated on the display and, in mobile devices, the power efficiency of the device. Our display drivers are highly integrated semiconductors that are customized for the particular needs of our customers. We believe that our design engineering expertise, technology leadership, manufacturing process expertise and library of functional building blocks produce display drivers that enable a wide variety of display types with high-impact visual performance.

The overall end market for flat panel display drivers is composed of a multitude of consumer electronics device markets such as television, laptop and desktop computers and portable consumer devices, including mobile handsets. This overall market can be broken down into several distinct sub-markets which we serve. These sub-markets include large panel TFTs, typically used in flat panel televisions and computer displays, small panel TFTs, typically used in mobile handsets, OLEDs and Color STNs. iSuppli forecasts in the Display Driver ICs Market Tracker that small and medium flat panel display producer shipments will increase from approximately 1.897 billion units in 2006 to 2.226 billion units by 2010, a compound annual growth rate of 4.1%. DisplaySearch forecasts the large TFT LCD market size to increase from 258 million units and \$96 billion revenue in 2006 to 462 million units and \$138 billion revenue in 2010, a compound annual growth rate of 16%.

We provide display drivers for use in several different types of display technologies and for a variety of end-market applications as discussed below.

*TFT-LCD.* TFT is an advanced active matrix LCD technology that uses a matrix of transistors embedded on a thin film of silicon to change the transparency of the LCD when voltage is applied. TFT-LCD technology is currently widely used for notebook computers and large scale flat panel monitors (Large TFT) as well as for displays for high-end mobile devices such as advanced mobile handsets (Small TFT). We currently provide Large TFT display drivers for use in mobile and desktop computer displays and in stand-alone flat panel television displays. We also provide Small TFT display drivers for use in mobile handsets, PDAs and in other consumer devices such as handheld gaming devices.

*Color STN.* Color STN is a low-power, low-cost solution based on passive matrix LCD technology and is widely used in color mobile displays available in the market today. Our Color STN display drivers are used in mobile applications such as mobile handsets, PDAs and handheld gaming devices.

*Organic Light Emitting Diode or OLED.* OLED is a relatively new display technology used in both mobile displays as well as in larger displays. OLED technology provides enhanced picture quality, low power consumption and long product life; it also has fast image response time, making it an ideal solution

## **Table of Contents**

for displaying motion pictures on mobile devices. We currently offer display drivers for OLED displays used in mobile handsets and other mobile devices.

Our display solutions segment received revenues of \$273.7 million and gross profit of \$35.6 million during the year ended December 31, 2006, \$326.1 million and \$66.6 million during the year ended December 31, 2005, and \$60.3 million and \$4.5 million during the three-month period ended December 31, 2004.

*Semiconductor Manufacturing Services.* We provide semiconductor manufacturing services primarily to semiconductor companies that do not have their own fabs. We target the market for diversified semiconductor products that require differentiated specialty process technologies for their manufacture, including high-voltage CMOS, non-volatile memory processes, power, analog and mixed-signal processes. We focus on specialty process technologies that do not require significant recurring capital investment, and we are able to better differentiate ourselves through the depth of our intellectual property portfolio and process technology skills.

The increasing trend toward the outsourcing of semiconductor manufacturing has resulted in a rapid increase in the size of this market. According to iSuppli, the worldwide foundry service market is projected to grow from in excess of \$26.6 billion in 2006 to \$44.3 billion in 2010, a compound annual growth rate of 13.6%.

Typical applications serviced by our semiconductor manufacturing services business are high-voltage, analog and mixed-signal, power, and non-volatile memory products for consumer, data processing, mobile, game and data communication end-markets. We have developed specialty manufacturing process technologies that enable us to manufacture differentiated, high-performance integrated semiconductor devices. For example, we developed a distinctive high-voltage, high-performance CMOS 0.18  $\mu\text{m}$  process that enables us to manufacture more integrated, and thus smaller and more cost efficient, semiconductor products. We believe that our proprietary process technology allows us to meet a wide variety of the specialty semiconductor manufacturing needs of our customers.

Our internal wafer fab facilities serve both our in-house product design groups and external foundry customers, allowing for both specialty process technology expertise and flexible manufacturing capacity. We target to be the primary-source provider of semiconductor manufacturing services for specialty process technologies for our foundry customers.

Our semiconductor manufacturing services segment received revenues of \$342.4 million and gross profit of \$45.7 million during the year ended December 31, 2006, \$345.4 million and \$110.4 million during the year ended December 31, 2005, and \$88.3 million and \$19.1 million during the three-month period ended December 31, 2004.

## **Customers**

During the year ended December 31, 2006, we sold over 2,200 products to more than 240 customers. In the year ended December 31, 2006, our 10 largest customers accounted for approximately 65.6% of our net sales, and we had one customer, a group of LG affiliates including LG.Philips LCD, representing greater than 10% of our net sales. See Risk Factors A significant portion of our sales comes from a relatively limited number of customers.

Revenue classified by geography is determined by the headquarters locations of our customers. During the year ended December 31, 2006, we received revenues of \$62.3 million from external customers in the United States and \$682.0 million from all foreign countries, of which 60.7% was from Korea, 11.5% from Japan, 17.4% from Taiwan, and 7.5% from China, Hong Kong, and Macau. During the year ended December 31, 2005, we received revenues of \$45.5 million from external customers in the United States and \$892.2 million from all foreign countries, of which 57.4% was from Korea, 11.0% from Japan, 16.0% from Taiwan, and 11.8% from China, Hong Kong, and Macau. During the three-month period ended December 31, 2004, we received revenues of \$9.3 million from external customers in the United States and \$234.3 million from all foreign countries, of

## **Table of Contents**

which 54.3% was from Korea, 16.2% from Japan, 12.8% from Taiwan, and 13.5% from China, Hong Kong, and Macau.

### **Sales, Marketing and Distribution**

We sell our products through a direct sales force and a network of authorized agents and distributors. We have strategically located our sales and technical support offices near concentrations of major customers. Our direct sales force consists primarily of representatives located in our headquarters in Korea, as well as representatives located elsewhere throughout Asia, the United States, and Europe. 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. During the year ended December 31, 2006, we derived approximately 74% of net sales through our direct sales force and 26% of net sales through our network of authorized agents and distributors.

Our product inventory is primarily located in Korea and is available for drop shipment globally. Outside of Korea, we maintain limited amounts of product inventory, and our sales representatives generally relay orders to our headquarters for fulfillment. Our agreements with our authorized agents and distributors are usually terminable by either party on relatively short notice.

### **Research and Development**

Our expenditures for research and development were \$131.2 million, representing 17.6% of net sales for the year ended December 31, 2006, \$107.6 million, representing 11.5% of net sales for the year ended December 31, 2005, and \$97.8 million, representing 9.0% of net sales for the year ended December 31, 2004. Our research and development efforts focus on process technology, design methodology and intellectual property for our semiconductor products and foundry services. As a result, we have implemented improvements to our manufacturing processes, design software and design libraries, including our 0.15  $\mu\text{m}$  high-voltage process and our 0.13  $\mu\text{m}$  CIS process and library. We also work closely with our major customers in many research and development activities, including joint intellectual property development, to increase the likelihood that our products will be more easily designed into the customers' products and consequently achieve rapid and lasting market acceptance. In CMOS image sensors, we are focusing on pixel size reduction, thereby enabling smaller form factors and higher resolution sensors. In flat panel display drivers, we are focusing on further integration. In semiconductor manufacturing services, our research and development work allows us to add features such as mixed-signal, high voltage, embedded memory and power devices.

### **Raw Materials**

We use processes that require specialized raw materials that are generally available from a limited number of suppliers. In 2006, we diversified suppliers for many of our raw materials, including chemicals, gases, and tape, which is one of the process materials for our display drivers. We continue to attempt to qualify additional suppliers for these materials. Although we have not experienced any significant raw material shortages in the past, it is possible that going forward our business and results of operations could be adversely affected due to supply shortages or price increases for raw materials.

Worldwide supplies of silicon wafers, an important raw material for the semiconductors we manufacture, have been decreasing due to a worldwide shortage of polysilicon, the raw material of wafers, and are not expected to increase until late 2008. Polysilicon is also a key raw material for solar cells, the demand for which has steadily increased over the last two years.

### **Intellectual Property**

As of March 1, 2007, our portfolio of intellectual property assets included approximately 8,500 registered and pending patents. Our patents expire at various times over the next 18 years. While these patents are in the aggregate important to our competitive position, no single registered or pending patent is material to us.

## **Table of Contents**

Pursuant to the intellectual property license agreement that we entered into with Hynix in connection with the Original Acquisition, we obtained from Hynix a non-exclusive license to certain intellectual property of Hynix that is mostly patent-related, and we granted to Hynix a non-exclusive license to certain of our intellectual property. Additionally, we have entered into exclusive and non-exclusive licenses and development agreements with third parties relating to the use of intellectual property of the third parties in our products and our design processes, including licenses related to embedded memory technology, design tools, process simulation tools, circuit designs, and ARM's ARM7 and ARM9 core-based System-on-Chip.

In addition, we rely on proprietary know-how, continuing technological innovation and other trade secrets to develop products and maintain our competitive position. We attempt to protect our proprietary know-how and our other trade secrets by executing, when appropriate, confidentiality agreements with our customers and employees. We cannot assure you that our competitors will not discover comparable or the same knowledge and techniques through independent development or other means.

## **Competition**

We operate in highly competitive markets. Although no one company competes with us in all of our product lines, we face significant competition in each of our market segments.

Our competitors include other manufacturers and designers of system semiconductors, standard products, and semi-standard programmable digital logic semiconductor products, as well as customers who design their own semiconductors that are manufactured at third party foundries.

We compete with other semiconductor providers based on design experience, the ability to service customer needs from the design phase to the shipping of a completed product, length of design cycle, longevity of technology support and sales and technical support personnel. Our ability to successfully compete depends on internal and external variables, both within and outside of our control. These variables include, but are not limited to, the timeliness with which we can develop new products and technologies, product performance and quality, manufacturing yields and availability, customer service, pricing, industry trends and general economic trends.

## **Employees**

Our worldwide workforce consisted of 3,504 employees (full- and part-time) as of March 1, 2007, of which 455 were involved in sales, general and administrative, 485 were in research and development, 92 were in quality, reliability and assurance and 2,472 were in manufacturing (comprised of 401 in engineering and 2,071 in operations). As of March 1, 2007, 2,149 employees, or approximately 61% of our workforce, were represented by the MagnaChip Semiconductor Labor Union, which is a member of the Federation of Korean Metal Workers Trade Unions.

Currently, members of the Korean Confederation of Trade Unions (KCTU), representing the former employees of two subcontractors that we retained for only three months in 2004, have demonstrated and may continue to demonstrate at our campus in Cheongju, Korea. The KCTU is demanding that we pressure other subcontractors to hire the employees and that we pay monetary compensation to the employees. These demonstrations have required additional interim expenses and may have a continuing negative impact on our operations in the future.

## **Environmental Matters**

Our operations are subject to a variety of environmental, health and safety laws and regulations in each of the jurisdictions in which we operate, governing, among other things, air emissions, wastewater discharges, the generation, use, handling, storage and disposal of, and exposure to, hazardous substances (including asbestos)

## **Table of Contents**

and wastes, soil and groundwater contamination and employee health and safety. These laws and regulations are complex, constantly changing and have tended to become more stringent over time. We cannot assure you that we have been, or will be at all times, in complete compliance with all these laws and regulations or that we will not incur material costs or liabilities in connection with these laws and regulations in the future. The adoption of new environmental, health and safety laws, the failure to comply with new or existing laws, or issues relating to hazardous substances could subject us to material liability (including substantial fines or penalties), impose the need for additional capital equipment or other process requirements upon us, curtail our operations, or restrict our ability to expand operations.

### **For More Information**

We file periodic reports with the Securities and Exchange Commission. Copies of our Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, and Current Reports on Form 8-K, including any amendments to these reports, are available on our website at [www.magnachip.com](http://www.magnachip.com). The public may also read and copy any materials we file with the SEC at the SEC's Public Reference Room at 100 F Street, NE, Washington, D.C. 20549, or on the SEC's website at [www.sec.gov](http://www.sec.gov). For information on the operation of the Public Reference Room, please call the SEC at 1-800-SEC-0330.

### **Item 1A. Risk Factors.**

#### **The cyclical nature of the semiconductor industry may limit our ability to maintain or increase net sales and profit levels during industry downturns.**

The semiconductor industry is highly cyclical and periodically experiences significant economic downturns characterized by diminished product demand, resulting in production overcapacity and excess inventory in the markets we serve, which can result in rapid erosion of average selling prices. The industry has experienced significant downturns, often in connection with, or in anticipation of, maturing product cycles of both semiconductor companies and their customers' products and the decline in general economic conditions.

We have experienced these conditions in our business in the past and may experience renewed, and possibly more severe and prolonged, downturns in the future as a result of such cyclical changes. This may reduce our profitability and the value of our business.

#### **Customer demand is difficult to accurately forecast.**

We make significant decisions, including determining the levels of business that we will seek and accept, production schedules, component procurement commitments, personnel needs and other resource requirements, based on our estimates of customer requirements. The short-term nature of commitments by many of our customers and the possibility of rapid changes in demand for their products reduces our ability to accurately estimate future customer demand. On occasion, customers may require rapid increases in production, which can challenge our resources and reduce margins. We may not have sufficient capacity at any given time to meet our customers' increased demand for our product. Conversely, downturns in the semiconductor industry may cause and have caused our customers to significantly reduce the amount of products ordered from us. Because many of our costs and operating expenses are relatively fixed, a reduction in customer demand may decrease our gross margins and operating income.

#### **Our customers may cancel their orders, change production quantities or delay production.**

We generally do not obtain firm, long-term purchase commitments from our customers. Customers may cancel their orders, change production quantities or delay production for a number of reasons. Cancellations, reductions or delays by a significant customer or by a group of customers, which we have experienced as a result of the recent downturn in the semiconductor industry, have adversely affected and may continue to adversely

## **Table of Contents**

affect our results of operations. In addition, while we do not obtain long-term purchase commitments, we generally agree to the pricing of a particular product for the entire lifecycle of the product, which can extend over a number of years. If we underestimate our costs when determining the pricing, our margins and results of operations would be adversely affected.

### **A significant portion of our sales comes from a relatively limited number of customers.**

If we were to lose key customers or if customers cease to place orders for our high volume devices, our financial results will be adversely affected. While we served more than 240 customers in the twelve-month period ended December 31, 2006, net sales to our 10 largest customers represented approximately 65.6% of our net sales for the period. We had one individual customer and one group of affiliated customers that each represented greater than 10% of our net sales during the year ended December 31, 2006. Significant reductions in sales to any of these customers, the loss of major customers or the curtailment of orders for our high-volume devices within a short period of time would adversely affect our business.

### **Our industry is highly competitive.**

The semiconductor industry is highly competitive and includes hundreds of companies, a number of which have achieved substantial market share. Current and prospective customers for our products evaluate our capabilities against the merits of our direct competitors. Some of our competitors are well-established as independent companies and have substantially greater market share and manufacturing, financial, research and development and marketing resources than we do. We also compete with emerging companies that are attempting to sell their products in specialized markets, and with the internal capabilities of many of our significant customers. We expect to experience continuing competitive pressures in our markets from existing competitors and new entrants. Any consolidation among our competitors could enhance their product offerings and financial resources, further enhancing their competitive position. Our ability to compete successfully depends on a number of factors, including the following: our ability to offer cost effective products on a timely basis using our technologies; our ability to accurately identify and respond to emerging technological trends and demand for product features and performance characteristics; product introductions by our competitors; our ability to adopt or adapt to emerging industry standards; and the number and nature of our competitors in a given market. Many of these factors are outside of our control. In the future, our competitors may capture our existing or potential customers and our customers may satisfy more of their requirements internally. As a result, we may experience declining revenues and profits.

### **A decline in average selling prices could decrease our profits.**

In the past, our industry has experienced a decline in average selling prices. A decline in average selling prices for our products, if not offset by reductions in the costs of producing such products, would decrease our gross profits and could have a material adverse effect on our business, financial condition and results of operations.

### **Growth in the consumer electronics and other end markets for our products is an important component in our success.**

Our continued success will depend in part on the growth of various consumer electronics markets and other end markets that use our semiconductors and on general economic growth. To the extent that we cannot offset recessionary periods or periods of reduced growth that may occur in these markets through greater penetration of these markets, our sales may decline and our business, financial condition and results of operations may suffer as a result.

### **We depend on successful technological advances for growth.**

Our industry is subject to rapid technological change and product obsolescence as customers and competitors create new and innovative products and technologies. Products or technologies developed by other

## **Table of Contents**

companies may render our products or technologies obsolete or noncompetitive and we may not be able to access leading edge process technologies or to license or otherwise obtain essential intellectual property required by our customers. Our inability to continue identifying new product opportunities, or manufacturing technologically advanced products on a cost-effective basis, may result in decreased revenues and a loss of market share to our competitors.

### **We may not be able to attract or retain the technical or management employees necessary to remain competitive in our industry.**

We depend on our ability to attract and retain skilled technical and managerial personnel. We could lose the services of, or fail to recruit, skilled personnel, which could hinder our research and product development programs or otherwise have a material adverse effect on our business.

### **If we encounter future labor problems, we may fail to deliver our products in a timely manner which could adversely affect our revenues and profitability.**

As of March 1, 2007, approximately 61% of our employees were represented by the MagnaChip Semiconductor Labor Union, which is a member of the Federation of Korean Metal Workers Trade Unions. We cannot assure you that issues with the labor union and other employees will be resolved favorably for us in the future, that we will not experience significant work stoppages in future years or that we will not record significant charges related to those work stoppages.

### **We may incur costs to engage in future business combinations or strategic investments and the anticipated benefits of those transactions may not be realized.**

As part of our business strategy, we may seek to enter into business combinations, investments, joint ventures and other strategic alliances with other companies in order to maintain and grow revenue and market presence as well as to provide us with access to technology, products and services. Those transactions would be accompanied by risks that may harm our business, such as difficulties in assimilating the operations, personnel and products of an acquired business or in realizing the projected benefits; disruption of our ongoing business; potential increases in our indebtedness and contingent liabilities; and charges if the acquired company or assets are later worth less than the amount paid for them in the Original Acquisition. In addition, our senior secured credit facility and the indentures governing our notes may prohibit us from making acquisitions that we may otherwise wish to pursue.

### **We depend on high utilization of our manufacturing capacity.**

As many of our costs are fixed, a reduction in capacity utilization, together with other factors such as yield and product mix, could reduce our profit margins and adversely affect our operating results. A number of factors and circumstances may reduce utilization rates, including periods of industry overcapacity, low levels of customer orders, operating inefficiencies, mechanical failures and disruption of operations due to expansion or relocation of operations, power interruptions, fire, flood or other natural disasters or calamities.

### **The failure to achieve acceptable manufacturing yields could adversely affect our business.**

The manufacture of semiconductors requires precision, a highly-regulated and sterile environment and expensive equipment. We may have difficulty achieving acceptable yields in the manufacture of our products. Slight impurities or defects in the masks used to print circuits on a wafer or other factors can cause significant difficulties, particularly in connection with the production of a new product, the adoption of a new manufacturing process or any expansion of our manufacturing capacity and related transitions.



## **Table of Contents**

### **We rely on certain subcontractors.**

The majority of our net sales are derived from semiconductor devices assembled in advanced packages. The packaging of semiconductors is a complex process requiring, among other things, a high degree of technical skill and advanced equipment. We outsource our semiconductor packaging to subcontractors, most of which are located in Korea and Southeast Asia. We rely on these subcontractors to package our devices with acceptable quality and yield levels. If our semiconductor packagers experience problems in packaging our semiconductor devices or experience prolonged quality or yield problems, our operating results could be adversely affected.

### **We depend on successful parts and materials procurement for our manufacturing processes.**

We use a wide range of parts and materials in the production of our semiconductors, including silicon, processing chemicals, processing gases, precious metals and electronic and mechanical components. We procure materials and electronic and mechanical components from domestic and foreign sources and original equipment manufacturers. If we cannot obtain adequate materials in a timely manner or on favorable terms for the manufacture of our products, either or both of our revenues or profits will decline.

### **We face product liability risks and the risk of negative publicity if our products fail.**

Our semiconductors are incorporated into a number of end products, and our business is exposed to product liability risk and the risk of negative publicity if our products fail. Although we maintain insurance for product liability claims, the amount and scope of our insurance may not be adequate to cover a product liability claim that is asserted against us. In addition, product liability insurance could become more expensive and difficult to maintain and, in the future, may not be available on commercially reasonable terms or at all.

In addition, we are exposed to the product liability risk and the risk of negative publicity affecting our customers and suppliers. Our sales may decline if any of our customers are sued on a product liability claim. We may also suffer a decline in sales from the negative publicity associated with such a lawsuit or with adverse public perceptions in general regarding our customers' products.

### **Our ability to compete successfully and achieve future growth will depend, in part, on our ability to protect our proprietary technology, as well as our ability to operate without infringing the proprietary rights of others.**

We seek to protect our proprietary technologies and know-how through the use of patents, trade secrets, confidentiality agreements and other security measures. The process of seeking patent protection takes a long time and is expensive. We cannot assure you that patents will issue from pending or future applications or that, if patents issue, they will not be challenged, invalidated or circumvented, or that the rights granted under the patents will provide us with meaningful protection or any commercial advantage. Some of our technologies are not covered by any patent or patent application. The confidentiality agreements on which we rely may be breached and may not be adequate to protect our proprietary technologies. We cannot assure you that other countries in which we market our services will protect our intellectual property rights to the same extent as the United States.

Our ability to compete successfully depends on our ability to operate without infringing the proprietary rights of others. We have no means of knowing what patent applications have been filed in the United States until they are published. In addition, the semiconductor industry is characterized by frequent litigation regarding patent and other intellectual property rights. Litigation, which could result in substantial costs to us and diversion of our resources, may also be necessary to enforce our patents or other intellectual property rights or to defend against claimed infringement of the rights of others. In the event of an adverse outcome in any such litigation, we may be required to pay substantial damages, indemnify customers or licensees for damages they may suffer if the products they purchase from us or the technology they license from us violate the intellectual property rights of

## **Table of Contents**

others; stop our manufacture, use, sale or importation of infringing products; expend significant resources to develop or acquire non-infringing technologies; discontinue processes; or obtain licenses to the intellectual property we are found to have infringed. We cannot assure you that we would be successful in such development or acquisition or that such licenses would be available under reasonable terms, or at all.

Our competitors may develop, patent or gain access to know-how and technology similar to our own. Failure to protect our existing intellectual property rights may result in the loss of valuable technologies or our having to pay other companies for infringing on their intellectual property rights.

### **We are subject to many environmental laws and regulations that could affect our operations or result in significant expenses.**

We are subject to requirements of environmental, health and safety laws and regulations in each of the jurisdictions in which we operate, governing, among other things, air emissions, wastewater discharges, the generation, use, handling, storage and disposal of, and exposure to, hazardous substances (including asbestos) and wastes, soil and groundwater contamination and employee health and safety. These laws and regulations are complex, constantly changing and have tended to become more stringent over time. We cannot assure you that we have been, or will be at all times, in complete compliance with all these laws and regulations or that we will not incur material costs or liabilities in connection with these laws and regulations in the future. The adoption of new environmental, health and safety laws, the failure to comply with new or existing laws, or issues relating to hazardous substances could subject us to material liability (including substantial fines or penalties), impose the need for additional capital equipment or other process requirements upon us, curtail our operations, or restrict our ability to expand operations.

### **We could suffer adverse tax and other financial consequences as a result of changes in, or differences in the interpretation of, applicable tax laws.**

Our company organizational structure is based, in part, on assumptions about the various tax laws, including withholding tax, and other laws of applicable non-U.S. jurisdictions. In addition, our Korean subsidiary ( MagnaChip Korea ) was granted a limited tax-holiday under Korean law in October 2004, which provides for certain tax exemptions for corporate taxes, withholding taxes, acquisition taxes, property and land taxes and other taxes for five years. Our interpretations and conclusions are not binding on any taxing authority, and, if our assumptions about tax and other laws are incorrect or if the authorities were to change or modify the relevant laws, we could suffer adverse tax and other financial consequences or have the anticipated benefits of our company organizational structure materially impaired.

### **A limited number of persons indirectly control us.**

CVC, Francisco Partners, and CVC Asia Pacific own approximately 34.1%, 34.1% and 18.3%, respectively, of the outstanding voting interests in MagnaChip. By virtue of their ownership of these voting interests, and the securityholders' agreement among MagnaChip and its unitholders, these entities have significant influence over our management and will be able to determine the outcome of all matters required to be submitted to the unitholders for approval, including the election of a majority of our directors and the approval of mergers, consolidations and the sale of all or substantially all of our assets.

### **We may need additional capital in the future and it may not be available on acceptable terms or at all.**

We may require more capital in the future to fund our operations, finance investments in equipment and infrastructure, and respond to competitive pressures and potential strategic opportunities. Additional capital may not be available when needed or, if available, may not be available on satisfactory terms. If we are unable to obtain capital on favorable terms, or if we are unable to obtain capital at all, we may have to reduce our operations or forego opportunities and it may have a material adverse effect on our business, financial condition and results of operations.

## **Table of Contents**

### **Our international operations are subject to various risks that may lead to decreases in financial results.**

We face risks inherent in international operations, such as unexpected changes in regulatory requirements, tariffs and other market barriers, political, social and economic instability, adverse tax consequences, war, civil disturbances and acts of terrorism, difficulties in accounts receivables collection, extended payment terms and differing labor standards, enforcement of contractual obligations and protection of intellectual property. These risks may lead to increased costs or decreased revenue growth, or both.

### **Any increase in tensions with North Korea could adversely affect our business, financial condition, and results of operations.**

Relations between Korea and North Korea have been tense throughout Korea's modern history. The level of tension between Korea and North Korea has fluctuated and may increase or change abruptly as a result of current and future events. Although we do not derive any revenue from, nor sell any products in, North Korea, any future increase in tensions which may occur, for example, the breakdown of high-level contacts between Korea and North Korea or the occurrence of military hostilities, could adversely affect our business, financial condition and results of operations.

### **We are subject to risks associated with currency fluctuations.**

Our revenues are denominated in various currencies, specifically, the Korean Won, Japanese Yen, Euro and U.S. dollar. As a result, changes in the exchange rates of these currencies or any other applicable currencies to the U.S. dollar will affect the translated price of products and therefore operating margins and could result in exchange losses.

The majority of our costs are denominated in Korean Won and to a lesser extent in Japanese Yen, U.S. dollar and Euro. Therefore, changes in the exchange rates of these currencies or any other applicable currencies to the U.S. dollar will affect cost of goods sold and operating margins and could result in exchange losses.

We cannot fully predict the impact of future exchange rate fluctuations on our profitability. From time to time, we may have engaged in, and may continue to engage in, exchange rate hedging activities in an effort to mitigate the impact of exchange rate fluctuations. However, we cannot assure you that any hedging technique we implement will be effective. If it is not effective, we may experience reduced operating margins.

### **Our historical financial information may not be representative of our results as a separate company.**

Prior to the Original Acquisition, we operated as a division of Hynix. Historical financial information for periods prior to September 30, 2004, was derived from Hynix's consolidated financial statements, has been presented on a carve-out basis and does not necessarily reflect what our financial position, results of operations or cash flows would have been had we been a separate, stand-alone company during the periods presented. As carve-out financial statements, the financial statements include allocations of the costs of shared activities and overhead of Hynix and of intangible assets and property, plant and equipment shared with Hynix. These allocations are based upon various assumptions and estimates, some of which are subjective. Actual results of our operations had we operated on a stand-alone basis, may differ from those allocations and estimates. Also, as part of the Original Acquisition we did not acquire certain assets that were included in the carve-out financial statements and we assumed certain additional costs and obligations that are not reflected in the carve-out financial statements. Accordingly, the carve-out financial statements should not be relied upon as being representative of our financial position or operating results had we operated on a stand-alone basis, nor may they be representative of our financial position or operating results following the Original Acquisition.

## **Table of Contents**

### **Our expenses could increase if Hynix were unwilling or unable to provide certain services related to our shared facilities with Hynix.**

Because we share certain facilities with Hynix, a few services that are essential to our business are provided to us by or through Hynix. These services include electricity, bulk gasses and de-ionized water, campus facilities, wastewater and sewage management, and environmental safety. If any of our agreements with Hynix were terminated or if Hynix were unwilling or unable to fulfill its obligations to us under the terms of these agreements, we would have to procure these services on our own and as a result may experience an increase in our expenses.

In addition, we lease building and warehouse space from Hynix in Cheongju, Korea, and lease to Hynix some of the space we own in Cheongju, Korea. If Hynix were to become insolvent, we could lose our leases on some of our building and warehouse space.

### **Research and development investments may not yield profitable and commercially viable products and thus will not necessarily result in increases in revenues for us.**

We invest significant resources in our research and development. However, research and development efforts may not yield commercially viable products. During each stage of research and development there is a substantial risk that we will have to abandon a potential product which is no longer marketable and in which we have invested significant resources. In the event we are able to develop viable new products, a significant amount of time will have elapsed between our investment in the necessary research and development effort and the receipt of any related revenues.

### **Investor confidence may be adversely impacted if we are unable to comply with Section 404 of the Sarbanes-Oxley Act of 2002.**

Beginning with our fiscal year ending December 31, 2007, we will be subject to rules adopted by the SEC pursuant to Section 404 of the Sarbanes-Oxley Act of 2002, which require us to include in our Annual Report on Form 10-K our management's report on, and assessment of the effectiveness of, our internal controls over financial reporting. Beginning with our fiscal year ending December 31, 2008, our independent auditors will be required to attest to and report on management's assessment of the effectiveness of our internal controls over financial reporting. If we fail to achieve and maintain the adequacy of our internal controls, there is a risk that we will not comply with all of the requirements imposed by Section 404. Moreover, effective internal controls, particularly those related to revenue recognition, are necessary for us to produce reliable financial reports and are important to helping prevent financial fraud. Any of these possible outcomes could result in an adverse reaction in the financial marketplace due to a loss of investor confidence in the reliability of our financial statements, which ultimately could harm our business and could negatively impact the market price of our securities.

### **Item 1B. Unresolved Staff Comments.**

Not Applicable.

### **Item 2. Properties.**

We own and operate five wafer fabrication facilities, or fabs, which have a combined production capacity of over 119,000 eight-inch equivalent wafers per month. We manufacture wafers at our two 8-inch fabs and our 6-inch fab located in Cheongju, Korea and our 8-inch fab and our 5-inch fab located in Gumi, Korea. The Cheongju facilities have three main buildings totaling 164,058 square meters. The Gumi facilities have two main buildings with 50,351 square meters devoted to manufacturing. We also lease from Hynix certain exclusive-use space plus certain common- and joint-use space in several buildings, primarily warehouses and utility facilities, in Cheongju, Korea.

**Table of Contents**

In addition to our fabs located in Cheongju and Gumi, Korea, we lease facilities in Seoul, Korea, Osaka, Japan, and Sunnyvale, California. Each of these facilities includes administration, sales and marketing, research and development, and operations functions. We also lease design facilities in Tokyo, Japan, which also has a sales and marketing office, and Lake Oswego, Oregon, and sales and marketing offices at our subsidiaries in several other countries.

The ownership of our wafer manufacturing assets is an important component of our business strategy that enables us to develop proprietary, differentiated products and maintain a high level of manufacturing control resulting in high production yields, shortened design and production cycles, adequate manufacturing capacity, and the capture of the wafer manufacturing profit margin.

The table below sets forth information with respect to our manufacturing facilities and technologies:

**Manufacturing**

<b>Facility</b>	<b>Location</b>	<b>Wafer Size</b>	<b>Technology</b>
F-5	Cheongju	8	0.18 / 0.15 / 0.13 $\mu$ m
F-4	Cheongju	8	0.35 / 0.25 / 0.22 $\mu$ m
F-3	Gumi	8	0.5 / 0.35 $\mu$ m
F-2	Cheongju	6	0.8 / 0.6 / 0.5 $\mu$ m
F-1	Gumi	5	1.2 $\mu$ m

We outsource most of our back-end manufacturing processes, including assembly, test and packaging to independent providers of these services.

**Item 3. Legal Proceedings.**

We are subject to lawsuits and claims that arise in the ordinary course of business and intellectual property litigation and infringement claims. Intellectual property litigation and infringement claims, in particular, could cause us to incur significant expenses or prevent us from selling our products. We are currently not involved in any legal proceedings, the outcome of which we believe would have a material adverse effect on our business, financial condition or results of operations.

**Item 4. Submission of Matters to a Vote of Security Holders.**

None.

**Table of Contents**

**PART II**

**Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.**

*Market Information*

There is currently no established public trading market for our outstanding common equity.

*Holdings*

The approximate number of record holders of our outstanding class of common equity as of March 1, 2007, was 206.

*Dividends*

We did not pay any dividends in fiscal year 2006. Our ability to pay dividends is restricted by certain covenants contained in our senior credit facilities, as well as certain restrictions contained in our indentures relating to our senior notes and our subordinated notes.

*Equity Compensation Plan Information*

The information required by this item is incorporated by reference to the information set forth in Item 12 of this Annual Report on Form 10-K.

*Recent Sales of Unregistered Securities*

None.

**Table of Contents****Item 6. Selected Financial Data**

The following table sets forth our selected financial and other data as of the dates and periods indicated. The information contained in this table should be read in conjunction with Item 7. Management's discussion and analysis of financial condition and results of operations and our historical financial statements and the accompanying notes thereto included elsewhere in this Form 10-K.

	Year ended December 31		Three months ended	Nine months ended	Year ended	
	2006	2005	December 31, 2004	September 30, 2004	2003	2002
	(Successor Company)(1)		(Predecessor Company)(1)			
	<i>(in millions of US dollars, except unit data)</i>					
<b>Statement of Operations Data</b>						
Net Sales						
Related party(2)	\$	\$	\$	\$	\$	\$
Other	744.3	937.7	243.6	677.8	570.1	393.5
	744.3	937.7	243.6	841.6	830.8	700.3
Cost of sales	644.9	729.0	204.5	654.6	752.5	691.0
Gross profit	99.4	208.7	39.1	187.0	78.3	9.3
Selling, general and administrative	87.7	123.3	29.8	54.0	68.7	61.9
Research and development	131.2	107.6	22.1	75.7	86.6	87.0
Restructuring and impairment charges	94.3	36.2				
Operating income (loss)	(213.8)	(58.4)	(12.8)	57.3	(77.0)	(139.6)
Interest expense, net	(57.2)	(57.2)	(16.7)	(17.7)	(37.8)	(46.8)
Foreign currency gain, net	50.9	16.5	30.4	5.3	1.4	8.6
Other				1.1	1.1	1.3
Other income (expenses)	(6.3)	(40.7)	13.7	(11.3)	(35.3)	(36.9)
Income (loss) before income taxes	(220.1)	(99.1)	0.9	46.0	(112.3)	(176.5)
Income tax expenses	9.2	1.8	6.7	2.8	1.4	1.8
Net income (loss)	\$ (229.3)	\$ (100.9)	\$ (5.8)	\$ 43.2	\$ (113.7)	\$ (178.3)
Dividends to preferred unitholders	10.9	9.9	13.4	N/A	N/A	N/A
Net loss attributable to common units	\$ (240.2)	\$ (110.8)	\$ (19.2)	N/A	N/A	N/A
Net loss per common unit basic and diluted	\$ (4.54)	\$ (2.10)	\$ (0.38)	N/A	N/A	N/A
Weighted average number of units basic and diluted	52,911,734	52,898,497	50,061,910	N/A	N/A	N/A
<b>Balance Sheet Data at period end</b>						
Cash and cash equivalents	\$ 89.2	\$ 86.6	\$ 58.4	\$	\$	\$
Working capital(3)	122.6	141.4	129.3	75.9	21.7	3.1
Total assets	770.1	1,040.6	1,154.5	653.8	790.0	1,077.8
Total indebtedness(4)	750.0	750.0	750.7	252.6	468.1	631.7
Preferred units	117.4	106.5	96.5			

Edgar Filing: MAGNACHIP SEMICONDUCTOR LLC - Form 10-K

Owners equity	N/A	N/A	N/A	206.7	155.3	268.3
Unitholders equity	(284.5)	(46.5)	55.9	N/A	N/A	N/A
<b>Foreign exchange rate (KRW/USD)(5)</b>						
Average exchange rate	954.3	1,023.8	1,090.8	1,163.3	1,191.8	1,250.3
End-of-period exchange rate	930.0	1,010.0	1,035.1	1,152.0	1,192.0	1,186.3



**Table of Contents**

- (1) On October 6, 2004, MagnaChip Semiconductor LLC completed the Original Acquisition. For accounting purposes and consistent with its reporting periods, the Company has used October 1, 2004 as the effective date of the Original Acquisition since the financial results from October 1, 2004 onwards accrued to the Company's benefit. As a result, the Company has reported its operating results and financial position for all periods from and after October 1, 2004, as those of the successor company. The predecessor company periods and the successor company periods have different bases of accounting and are therefore not comparable.
- (2) Primarily relates to wafer foundry contract manufacturing services to Hynix Semiconductor, Inc., Hynix Display Technology and other related parties during the predecessor company periods when the Company was the System IC division within Hynix.
- (3) Working capital is calculated as current assets less current liabilities.
- (4) Total indebtedness is calculated as long and short-term borrowings, including the current portion of long-term borrowings.
- (5) As a substantial portion of the Company's revenues and assets are recorded in KRW functional currency, conversion to US Dollar reporting currency is required at the end of each reporting period in order to follow the methodology prescribed in SFAS No. 52, *Foreign Currency Translation*.

## **Table of Contents**

### **Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations**

The following Management's Discussion and Analysis of Financial Condition and Results of Operations contain forward-looking statements within the meaning of the federal securities laws that involve risks and uncertainties. Our actual results may differ materially from those anticipated in these forward-looking statements as a result of certain factors set forth elsewhere in this Form 10-K and in the Company's prior public filings with the SEC. These forward looking statements are made based upon management's expectations and beliefs concerning future events impacting the Company and, therefore, involve a number of risks and uncertainties. The Company's management cautions that forward looking statements are not guarantees and that actual results could differ materially from those expressed or implied in the forward looking statements. The following discussion should be read in conjunction with the audited consolidated financial statements and related notes included elsewhere in this Form 10-K. While the Company periodically reassesses material trends and uncertainties affecting the Company's results of operations and financial condition in connection with the preparation of Management's Discussion and Analysis of Financial Condition and Results of Operations and certain other sections contained in the Company's quarterly, annual or other reports filed with the SEC, the Company does not intend to review or revise any particular forward looking statement in light of future events.

#### **Overview**

We are a leading designer, developer and manufacturer of mixed-signal and digital multimedia semiconductors addressing the convergence of consumer electronics and communication devices. We focus our core business on CMOS image sensors and flat panel display drivers, which are complex, high-performance mixed-signal semiconductors that capture images and enable and enhance the features and capabilities of both small and large flat panel displays. We also provide wafer foundry services whereby we leverage our specialized process technologies and low cost manufacturing facilities to produce semiconductors for third parties using their product designs. Our solutions are used in a wide variety of consumer and commercial mass market applications, such as mobile handsets, including camera-equipped mobile handsets, flat panel monitors and televisions, mobile displays, portable computer displays, handheld gaming devices, PDAs and audio-visual equipment such as DVD players.

We have three separate business segments: Display Solutions, Imaging Solutions and Semiconductor Manufacturing Services.

*Display Solutions:* Our Display Solutions segment offers flat panel display drivers for the entire product range of small to large panel displays, including mobile handsets, handheld gaming devices, PDAs, displays for desktop and mobile computer monitors and flat panel televisions. Our products also cover a broad range of technologies and interfaces including LTPS, TFT, CSTN, OLED technologies, RSDS and mini-LVDS interfaces.

*Imaging Solutions:* Our Imaging Solutions segment address a broad spectrum of consumer electronics products ranging from camera-equipped mobile handsets to personal computer webcams, offering VGA, 1.3, 2.1 and 3.2 megapixel CMOS image sensors. Our highly integrated image sensors are designed to be cost effective and to provide brighter, sharper and more colorful image quality for use primarily in applications that require small form factors, low power consumption, effective heat dissipation and high reliability.

*Semiconductor Manufacturing Services:* Our Semiconductor Manufacturing Services segment uses our process technology and manufacturing facilities to manufacture semiconductor wafers for third parties based on their designs. We provide our services to specialty markets that utilize high-voltage, embedded memory, analog and power processes. We offer customized services for clients globally at our state-of-the-art fabrication facilities located in Cheongju and Gumi, Korea. Our fabs provide us with large scale, cost-effective and flexible capacity enabling us to rapidly scale to high volume to meet shifts in demand by our end customers.

## **Table of Contents**

### **Basis of Presentation**

Prior to October 1, 2004, our consolidated financial statements were prepared on a carve-out basis from the consolidated financial statements and accounting records of Hynix using the actual results of operations and actual basis of assets and liabilities of our business. The consolidated statements of operations include allocations of certain raw materials, other assets and accounts payable which our business has historically shared with Hynix, and allocations of certain manufacturing costs, general and administrative, sales and marketing, and other miscellaneous expenses. These allocations were made on a specifically identifiable basis or using the relative percentages, as compared to Hynix's other businesses, of sales, headcount, raw material consumption or other reasonable methods. Hynix and MagnaChip considered these allocations to be a reasonable reflection of the utilization of services provided. We believe the assumptions underlying the consolidated financial statements are reasonable. However, the consolidated financial statements may not necessarily reflect our results of operations, financial position and cash flows in the future or what our results of operations, financial position and cash flows would have been, had we been a separate stand-alone company during the historical carve-out periods presented. As part of the Original Acquisition, we did not acquire certain assets that were included in the carve-out financial statements and we assumed certain additional obligations that are not reflected in the carve-out financial statements. Accordingly, the carve-out financial statements should not be relied upon as being representative of our financial position or operating results had we operated on a stand alone basis, nor may they be representative of our financial position or operating results following the Original Acquisition.

Prior to our fiscal year 2006, we operated in a single segment semiconductor manufacturing. In our fiscal year 2006, subsequent to the appointment of new chief operating decision maker (the CODM) as defined by Statements of Financial Accounting Standards (SFAS) No. 131, *Disclosure about Segments of an Enterprise and Related Information*, the manner in which the CODM reviewed the Company's operational results and made significant business decisions was changed to include disaggregated financial information with respect to our three primary business units. Segment information for the prior periods was prepared in conformity with the current segment structure.

**Table of Contents****Results of Operations Comparison of Years Ended December 31, 2006 and December 31, 2005**

	Year ended December 31,		Year ended December 31,		Change	
	2006		2005			
	Amount	% of net sales	Amount	% of net sales	Amount	%
	<i>(in millions of US dollars; %)</i>					
Net sales	\$ 744.3	100.0	\$ 937.7	100.0	\$ (193.4)	(20.6)
Cost of sales	644.9	86.6	729.0	77.7	(84.1)	(11.5)
Gross profit	99.4	13.4	208.7	22.3	(109.3)	(52.4)
Selling, general and administrative expenses	87.7	11.8	123.3	13.1	(35.6)	(28.9)
Research and development expenses	131.2	17.6	107.6	11.5	23.6	21.9
Restructuring and impairment charges	94.3	12.7	36.2	3.9	58.1	160.5
Operating income (loss)	(213.8)	(28.7)	(58.4)	(6.2)	(155.4)	266.1
Interest expense, net	(57.2)	(7.7)	(57.2)	(6.1)	0.0	0.0
Foreign currency gain, net	50.9	6.8	16.5	1.8	34.4	208.5
Income (loss) before income taxes	(220.1)	(29.6)	(99.1)	(10.5)	(121.0)	122.1
Income tax expenses	9.2	1.2	1.8	0.2	7.4	411.1
Net income (loss)	\$ (229.3)	(30.8)	\$ (100.9)	(10.7)	\$ (128.4)	127.3

**Net Sales**

	Year ended December 31,		Year ended December 31,		Change	
	2006		2005			
	Amount	% of total	Amount	% of total	Amount	%
	<i>(in millions of US dollars; %)</i>					
Display solutions	\$ 273.7	36.8	\$ 326.1	34.8	\$ (52.4)	(16.1)
Imaging solutions	60.5	8.1	163.3	17.4	(102.8)	(63.0)
Semiconductor Manufacturing Services	342.4	46.0	345.4	36.8	(3.0)	(0.9)
All other	67.7	9.1	102.9	11.0	(35.2)	(34.2)
	\$ 744.3	100.0	\$ 937.7	100.0	\$ (193.4)	(20.6)

We derive a majority of our net sales from three operating segments: Display Solutions, Imaging Solutions and Semiconductor Manufacturing Services. The All other category for 2006 represents certain business activities other than these business segments, principally composed of rental and unit processing. All other for the prior period also included certain business activities exited in late 2005 or early 2006, such as our application processor and DRAM foundry business.

Total net sales for 2006 decreased \$193.4 million, or 20.6% compared to 2005. Net sales generated from the three operating segments in 2006 were \$676.6 million, a decrease of \$158.2 million or 18.9% from net sales from the three operating segments in 2005.

*Display Solutions.* Net sales from Display Solutions for the year ended December 31, 2006 were \$273.7 million, a \$52.4 million or 16.1% decrease from \$326.1 million for the year ended December 31, 2005. This decrease was primarily attributable to sales volume decrease in large

## Edgar Filing: MAGNACHIP SEMICONDUCTOR LLC - Form 10-K

display driver products as a result of our customer's inventory correction, build-up of inventory in the prior year and subsequent reductions of inventory in 2006 due to less-than-expected market demand from our major customers. In addition, average selling price erosion during 2006 also had a negative impact on net sales.





## **Table of Contents**

attributable to a reduction in professional service fees driven by our cost containment efforts and a decrease in amortization expense of intangible assets as a result of an impairment taken during the year.

*Research and Development Expenses.* Research and development expenses for the year ended December 31, 2006 were \$131.2 million, a \$23.6 million or 21.9% increase from \$107.6 million for the year ended December 21, 2005. This increase in research and development expenses during the year primarily represents our focus on the introduction of new products, especially in the Imaging Solutions and Display Solutions segments. As a percentage of net sales, research and development expense increased to 17.6% in current period compared to 11.5% in the prior period.

*Restructuring and Impairment Charges.* During the year ended December 31, 2006, we recorded restructuring and impairment charges totaling \$94.3 million, which included \$92.9 million of impairment charges under SFAS No. 144, *Accounting for the Impairment or Disposal of Long-lived Assets* and \$1.4 million of restructuring charges under SFAS No. 146, *Accounting for Costs Associated with Exit or Disposal Activities*.

The impairment charges of \$92.5 million recorded during 2006 related to certain fixed assets and technology and customer-based intangible assets (the asset group) comprising our Imaging Solution business. At the end of 2005, the capacity utilization of the Fab was under the level that we believe to be normal. This was primarily due to a transition in product mix, coupled with a seasonal decrease in market demand, which was deemed to be temporary and recoverable. However, in 2006, our management determined, based on revised forecasting, that the projected demand for certain of its products in our Imaging Solutions business was significantly less than previously forecasted and that this decline was not temporary or seasonal. Therefore, we assessed whether there had been an impairment of the asset group pursuant to SFAS No. 144 and, based on the assessment, recorded the impairment charge. We also recorded \$0.4 million of impairment charges in association with the disposition of certain held-for-sale assets.

The \$1.4 million of restructuring charges for 2006 were incurred in connection with the termination of certain of our management and employees.

During the year ended December 31, 2005, the Company recorded a one-time charge of \$36.2 million of restructuring and impairment charges which included \$33.5 million for asset impairment and \$2.7 million for restructuring.

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

*Net Interest Expense.* Net interest expense was \$57.2 million for the year ended December 31, 2006, consistent with \$57.2 million for the year ended December 31, 2005. Substantially all of our interest expense is to serve our long-term borrowings of \$750.0 million at a weighted-average interest rate of 7.4%.

*Net Foreign Currency Gain.* Net foreign currency gain for the year ended December 31, 2006 was \$50.9 million, compared to \$16.5 for the year ended December 31, 2005. A substantial portion of our net foreign currency gain was non-cash translation gain recorded for intercompany borrowings at one of our subsidiaries.

### ***Income Tax Expenses***

Income tax expenses for the year ended December 31, 2006 were \$9.2 million while income tax expenses were \$1.8 million for the year ended December 31, 2005. The lower income tax expenses in the prior period were primarily attributable to the income tax benefit recognized for a temporary difference related to revenue recognition at our Japanese subsidiaries, which became recognizable as a result of change in business model. Income tax expense for 2006 was comprised of \$5.2 million of withholding taxes on the interest paid by one of our subsidiaries to its parent company, a \$2.0 million income tax effect from the decrease of deferred tax assets and an aggregate \$2.0 million of current income taxes incurred at various jurisdictions where we had our operations.





Edgar Filing: MAGNACHIP SEMICONDUCTOR LLC - Form 10-K

Display solutions	\$ 326.1	34.8	\$ 60.3	\$	198.8	\$ 259.1	23.9	67.0	25.9
Imaging solutions	163.3	17.4	58.1		142.1	200.2	18.5	(36.9)	(18.4)
Semiconductor Manufacturing Services	345.4	36.8	88.3		270.2	358.5	33.0	(13.1)	(3.7)
All other	102.9	11.0	36.9		230.5	267.4	24.6	(164.5)	(61.5)
	\$ 937.7	100.0	\$ 243.6	\$	841.6	\$ 1,085.2	100.0	(147.5)	(13.6)





## **Table of Contents**

*Imaging Solutions.* Gross margin percentage for Imaging Solutions for 2005 was 15.6% compared with 34.7% for 2004. The gross margin decrease from 2004 was primarily attributable to decrease in average selling prices.

*Semiconductor Manufacturing Services.* Gross margin for Semiconductor Manufacturing Services increased to 32.0% in 2005 from 29.4% in 2004. This increase in gross margin percentage in 2005 resulted from higher average selling price and lower depreciation expenses during the period.

*All other.* Gross margin percentage for All other for 2005 was 6.1%, relatively consistent with 6.2% for 2004.

### ***Operating Expenses***

*Selling, General and Administrative Expenses.* Selling, general and administrative expenses were \$123.3 million or 13.1% of net sales in 2005. This represents a \$39.5 million or 47.1% increase from a total of \$83.8 million or 7.7% of net sales in 2004, which consisted of \$54.0 million for the nine months ended September 30, 2004 and \$29.8 million for the three months ended December 31, 2004. The increase in selling, general and administrative expenses was primarily attributable to amortization of intangible assets recorded upon the application of purchase accounting as a result of the Original Acquisition. We also recognized increased professional fees related to consulting and infrastructure build-out as well as additional warranty reserves to cover possible exposures to future claims from customers.

*Research and Development Expenses.* Research and development expenses in 2005 were \$107.6 million, a \$9.8 million or 10.0% increase from \$97.8 million in 2004, which consisted of \$75.7 million for the nine months ended September 30, 2004 and \$22.1 million for the three months ended December 31, 2004. The increase in research and development expenses was mainly due to our reinforcement of research and development centers worldwide through our mergers and acquisitions and process development to support next generation products. As a percentage of net sales, research and development expense increased to 11.5% in 2005 from 9.0% in 2004.

*Restructuring and Impairment Charges.* During the year ended December 31, 2005, the Company recorded a one-time charge of \$36.2 million of restructuring and impairment charges associated with the Company's initiative to focus on its core businesses and streamline the organization. The amount included \$33.5 million for asset impairment and \$2.7 million for restructuring.

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

*Net Interest Expense.* Net interest expense was \$57.2 million in 2005, a \$22.8 million or 66.3% increase from aggregated interest expense of \$34.4 million in 2004, which consisted of \$17.7 million for the nine months ended September 30, 2004 and \$16.7 million for the three months ended December 31, 2004. The increase in net interest expense was primarily due to interest expenses incurred on the long-term debt of \$750.0 million, which was issued in December 2004 and outstanding throughout the year 2005.

*Net Foreign Currency Gain.* Net foreign currency gain for the year ended December 31, 2005 was \$16.5 million, compared to \$35.7 for the year ended December 31, 2004. A substantial portion of our net foreign currency gain for 2005 was non-cash translation gain recorded for intercompany borrowings at one of our subsidiaries.

### ***Income Tax Expenses***

*Income Tax Expense.* Income tax expense was \$1.8 million in 2005, compared to \$6.7 million for the three months ended December 31, 2004 and \$2.8 million for the nine months ended September 30, 2004, which on an aggregate basis totaled \$9.5 million for the year ended December 31, 2004. Income tax expense for the year ended December 31, 2005 was primarily attributable to \$5.2 million of Korean withholding tax on the interest

---

## **Table of Contents**

income paid to our Korean subsidiary's parent company. Income tax expense including this withholding tax was partially offset by the recognition of a deferred tax asset at our Japanese subsidiaries based on temporary difference related to revenue recognition.

### **Liquidity and Capital Resources**

Our principal capital requirements are to fund working capital needs, to meet required debt payments, including debt service payments on the notes and, if drawn upon, the senior credit facility, and to invest in research and development and capital equipment. We anticipate that operating cash flow, together with available borrowing capacity under our senior credit facility, will be sufficient to meet our working capital needs, our research and development and capital expenditures needs and service requirements on our debt obligations for the foreseeable future. As of December 31, 2006 we had total long-term debt outstanding of \$750.0 million.

Our principle sources of liquidity are our cash, cash equivalents and available borrowings under our senior credit facility of \$100 million. As of December 31, 2006 our cash and cash equivalents balance was \$89.2 million or 11.6% of our total assets, a \$2.6 million increase from \$86.6 million or 8.3% of total assets as of December 31, 2005. The increase in cash and cash equivalents was due to cash inflow from operating activities coupled with an increase from foreign currency translation gains, mostly offset by cash outflows for capital expenditures and other investing activities.

We generated cash from operating activities of \$30.5 million during the year 2006, which principally reflects the Company's net loss of \$229.3 million adjusted by \$247.2 million of total non-cash items composed mainly of depreciation and amortization expenses and impairment charges. Cash from operating activities for 2006 decreased \$73.1 million from \$103.6 million for 2005. This decrease in cash from operating activities between the two periods was primarily due to 52.4% lower gross profits mitigated by a decrease in working capital during the year 2006.

Our working capital balance as of December 31, 2006 was \$122.6 million compared to \$141.4 million as of December 31, 2005. The decrease of \$18.8 million in our working capital balance consisted primarily of a \$35.4 million decrease in accounts receivable and \$30.8 million decrease in inventories, partially offset by a \$34.5 million decrease in accounts and other accounts payable and \$5.3 million decrease in accrued expenses. This decrease in working capital is mainly attributable to a 20.6% decline in total net sales.

For investing activities, we used cash of approximately \$33.4 million in 2006 compared to \$64.1 million in 2005. The decrease in cash used for investing activities during the year 2006 was primarily attributable to lower capital equipment expenditures during the year. Cash outflows for acquisitions of subsidiaries in 2005 in an effort to reinforce global R&D capability also led to a higher investing cash outlay in 2005. We did not consummate any business acquisitions during the year 2006. Capital expenditures for the year ended December 31, 2006 were \$41.4 million, a decrease of \$23.1 million or 35.8% compared to \$64.5 million for the year ended December 31, 2005. This year over year decrease was a result of managing capital expenditure timing in order to better support the growth of our business from new customers and to optimize returns on investment.

For financing activities, we used \$0.3 million for the year ended December 31, 2006, compared to \$12.8 million for the year ended December 31, 2005. As we had sufficient capital resources available to serve our capital requirements we did not have significant financing activities during the year 2006. The cash outlay in 2006 was mainly due to our repurchase of common units upon termination of certain of our management and employees. Cash outflow in 2005 was mainly for the repayment of short-term borrowings at one of our subsidiaries that we acquired during the year.

*Future Financing Activities.* Our primary future capital requirements on a recurring basis will be funding working capital needs, meeting required debt payments, funding research and development, and capital expenditures. We anticipate that operating cash flows, together with available borrowings under our senior credit

**Table of Contents**

facility, will be sufficient to meet these capital requirements for the foreseeable future. We may from time to time incur additional debt.

We may need to incur additional debt or issue equity to make strategic acquisitions of investments. However, we cannot assure you that such financing will be available to us on acceptable terms or that such financing will be available at all.

**Contractual Obligations**

Summarized in the table below are our obligations and commitments to make future payments under debt obligations and minimum lease payment obligations as of December 31, 2006.

	Payments Due by Period						Interest expense
	Total	2007	2008	2009	2010	2011	
	<i>(in millions of US dollars)</i>						
Revolving credit facility							
Secured notes and subordinated notes(*)	750.0					500.0	250.0
Operating lease	59.5	11.9	11.9	11.9	11.9	11.9	
Others	8.5	7.7	1.1				(0.3)

(\*) Excludes interest obligations on revolving credit facility and notes.

The Floating Rate Second Priority Senior Secured Notes of \$300 million and Second Priority Senior Secured Notes of \$200 million mature in 2011, while the Senior Subordinated Notes of \$250 million mature in 2014. Interest rates are 3 month LIBOR + 3.25%, 6<sup>7</sup>/<sub>8</sub>% and 8%, respectively. These notes will be paid in full upon maturity.

Each indenture governing the notes contains covenants that limit the ability of the Company and its subsidiaries to (i) incur additional indebtedness, (ii) pay dividends or make other distributions on its capital stock or repurchase, repay or redeem its capital stock, (iii) make certain investments, (iv) incur liens, (v) enter into certain types of transactions with affiliates, (vi) create restrictions on the payment of dividends or other amounts to the Company by its subsidiaries, and (vii) sell all or substantially all of its assets or merge with or into other companies.

**Off-Balance Sheet Arrangements**

On December 23, 2004, two of the Company's subsidiaries, MagnaChip Semiconductor S.A. and MagnaChip Semiconductor Finance Company entered into a senior credit agreement with a syndicate of banks, financial institutions and other entities providing for a \$100 million senior secured revolving credit facility. The undrawn portion of such senior secured credit line as of December 31, 2006 and December 31, 2005 were \$93.8 million and \$83 million, respectively. The utilized portions of the credit line are related to the issuance of letters of credit rather than cash drawdowns.

Other than the senior credit facility, there are no material off-balance sheet arrangements that have or are reasonably likely to have a current or future effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources that is material to investors.

**Recent Accounting Pronouncements**

In September 2006, FASB issued SFAS No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plan* an amendment of SFAS No. 87, 88, 106 and 132(R). This Statement requires an employer to recognize the over funded or under funded status of a defined benefit post retirement plan (other than a multiemployer plan) as an asset or liability in its statement of financial position, and to recognize changes in that funded status in the year in which the changes occur through comprehensive income. SFAS No. 158 is effective for fiscal years ending after June 15, 2007.

## **Table of Contents**

We do not expect that the implementation of SFAS No. 158 will have a material impact on our financial position and results of operations.

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements*. This Statement defines fair value, establishes a framework for measuring fair value and requires enhanced disclosures about fair value measurements. SFAS No. 157 requires companies to disclose the fair value of its financial instruments according to a fair value hierarchy, as defined and may be required to provide additional disclosures based on that hierarchy. SFAS No. 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007. We are currently evaluating the impact that the adoption may have on our consolidated financial statements.

In September 2006, the SEC issued SAB No. 108 which provides interpretive guidance on how the effects of the carryover or reversal of prior year misstatements should be considered in quantifying a current year misstatement. The guidance is applicable for fiscal years ending after November 15, 2006. We do not expect that adoption of SAB 108 will have a material impact on our consolidated financial statements.

In June 2006, the FASB issued FIN No. 48, *Accounting for Uncertainty in Income Taxes* an interpretation of SFAS No. 109. FIN 48 clarifies the accounting for uncertain income tax positions accounted for in accordance with SFAS No. 109. The Interpretation stipulates recognition and measurement criteria in addition to classification, interim period accounting and significantly expanded disclosure provisions for uncertain tax positions that are expected to be taken in a company's tax return. FIN 48 is effective for fiscal years beginning after December 15, 2006. We are currently evaluating the impact that the adoption may have on our consolidated financial statements.

In March 2006, the FASB issued SFAS No. 156, *Accounting for Servicing of Financial Assets* an amendment of FASB Statement No. 140. This Statement addresses the accounting for recognized servicing assets and liabilities related to certain transfers of the servicer's financial assets and for acquisitions or assumptions of obligations to service financial assets that do not relate to the financial assets of the servicer and its related parties. SFAS No. 156 requires that all recognized servicing assets and liabilities are initially measured at fair value, and subsequently measured at either fair value or by applying an amortization method for each class of recognized servicing assets and liabilities. SFAS No. 156 is effective in fiscal years beginning after September 15, 2006. The adoption of SFAS No. 156 is not expected to have a material impact on our consolidated financial statements.

In February 2006, the FASB issued SFAS No. 155, *Accounting for Certain Hybrid Financial Instruments* an amendment of FASB Statements No. 133 and 140. This Statement amends SFAS No. 133 and SFAS No. 140, and improves the financial reporting of certain hybrid financial instruments by requiring more consistent accounting. Specifically, this Statement allows fair value re-measurement for any hybrid financial instrument that contains an embedded derivative that otherwise would require bifurcation. This Statement is effective for all financial instruments acquired or issued after the beginning of an entity's first fiscal year that begins after September 15, 2006. The adoption of this Statement is not expected to have a material impact on our consolidated financial statements.

## **Critical Accounting Policies and Estimates**

The preparation of financial statements and related disclosures in conformity with U.S. GAAP requires our management to make significant judgments and estimates that affect our financial position and results of operations. For a summary of our significant accounting policies, including the accounting policies discussed below, see Note 2 to the Consolidated Financial Statements.

### ***Revenue Recognition***

Our revenue is derived from the sale of semiconductor products we design and the manufacture of semiconductor wafers for third parties. We recognize revenue when persuasive evidence of an arrangement



## **Table of Contents**

exists, the product has been delivered and title and risk of loss have transferred, the price is fixed and determinable, and collection of resulting receivables is reasonably assured. For certain distributors, standard products are sold without rights to return products or stock rotation or price protection rights. Our policy is to recognize revenue upon delivery of products to customers, where shipment represents the point when the rights and risks of ownership have passed to the customer, when persuasive evidence of an arrangement exists, the product has been delivered, the price is fixed or determinable and collection of the resulting receivable is reasonably assured. Specialty foundry services are performed pursuant to manufacturing agreements and purchase orders. Standard products are shipped and sold based upon purchase orders from customers. 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 expenses.

We maintain allowances for doubtful accounts for estimated losses resulting from the inability of our customers to make payment. If the financial condition of our customers were to deteriorate, additional allowances may be required. We record warranty liabilities for the estimated costs that may be incurred under our limited warranty. This warranty covers product defects based on compliance to our specifications and is normally applicable for twelve months from the date of purchase. These liabilities are recorded when related revenue is recognized. Warranty costs include the costs to replace the defective product. Factors that affect our warranty liability include the historical and anticipated rate of warranty claims on those repairs and the cost per claim to satisfy our warranty obligations. 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 as necessary.

### ***Inventory Valuation***

Inventories are stated at the lower of cost or market, using the average cost method, which approximates the first in, first out method. 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 under cost of sales. We estimate the net realizable value for such finished goods and work-in-progress based on current invoice prices. Inventory reserves are established when conditions indicate that the net realizable value is less than cost due to physical deterioration, obsolescence, changes in price levels, or other causes. Reserves are also established for excess inventory based on inventory levels in excess of six months of projected demand, as judged by management, for each specific product.

In addition, as prescribed in SFAS No. 151, 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 the management believes to be normal, the fixed overhead costs per production unit which exceeds those under normal capacity, are charged to cost of sales rather than capitalized as inventories.

### ***Useful Lives of Tangible and Intangible Assets***

Property, plant and equipment are stated at cost, less accumulated depreciation. Depreciation is computed using the straight-line method over the estimated useful lives of the assets. Buildings and related structures are depreciated over the 10 to 40 year periods. Machinery, equipment and other assets including vehicles are depreciated over the estimated useful lives ranging 5 to 10 years.

Upon the Original Acquisition, machinery, equipment and other assets were assumed from Hynix, approximately 50% depreciated. Accordingly, remaining useful lives of these assets were determined at approximately 50% of initial useful lives.

Our intangible assets represent rights under patents, trademarks, property use rights, customer relationship and technology, and are amortized over the periods of benefit, ranging up to 10 years, on a straight-line basis.

## **Table of Contents**

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

We review the carrying value of fixed assets for impairment when events and circumstances indicate that the carrying value of an asset or group of assets may not be recoverable from the estimated future cash flows expected to result from its use and/or disposition. Factors which could trigger an impairment review include the following: (i) significant negative industry or economic trends, (ii) exiting an activity in conjunction with a restructuring of operations, (iii) current, historical or projected losses that demonstrate continuing losses associated with an asset, and (iv) management's assessment of future manufacturing capacity requirements. In cases where undiscounted expected future cash flows are less than the carrying value, an impairment charge is recognized equal to the amount by which the carrying value exceeds the estimated fair value of the assets. The estimation of future cash flows involves numerous assumptions, which require our judgment, including, but not limited to, future use of the assets for our operations versus sale or disposal of the assets, future-selling prices for our products and future production and sales volumes. In addition, we must use our judgment in determining the groups of assets for which impairment tests are separately performed.

### ***Restructuring Charges***

We recognize restructuring charges in accordance with SFAS No. 146, *Accounting for Costs Associated with Exit or Disposal Activities*. Certain costs and expenses related to exit or disposal activities are recorded as restructuring charges when liabilities for those costs and expenses are incurred.

### ***Income taxes***

We account for income taxes in accordance with SFAS No. 109, *Accounting for Income Taxes*. SFAS No. 109 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 on 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 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 established valuation allowances for deferred tax assets at most of our subsidiaries since, other than with respect to one particular subsidiary, it is not probable that a majority of the deferred tax assets will be realizable. The valuation allowance at this particular subsidiary was not set up since it is expected that the deferred tax assets at this subsidiary will be deemed realizable based on the current prospects for its future taxable income.

### ***Unit-based Compensation***

In 2006, we adopted SFAS No. 123(R) using the modified prospective application method and began to account for unit-based compensation based on a fair value method. Under the provision of SFAS No. 123(R), unit-based compensation cost is estimated at the grant date based on the fair-value of the award and is recognized as expense over the requisite service period of the award. Consistent with prior-period pro forma presentation under SFAS No. 123, we use the Black-Scholes option pricing model to value options. In developing assumptions for fair value calculation under SFAS No. 123(R), we use estimates based on historical data and market information. A small change in the assumptions used in the estimate can cause a relatively significant change in the fair value calculation.

The valuation of our common unit is based on an independent appraisal from a third party and is updated reflecting the changes in our financial results and prospects. Determination of the fair value of our common units involves complex and subjective judgments. If we make different judgments or adopt different assumptions, material differences could result in the timing and amount of the unit-based compensation expenses recorded because the estimated fair value of the underlying units for the options granted would be different.

## **Table of Contents**

### ***Segment Information***

We have determined, based on the nature of our operations and products offered to customers, that our reportable segments are Display Solutions, Imaging Solutions, and Semiconductor Manufacturing Services. Our chief operating decision maker ( CODM ) as defined by SFAS 131, *Disclosure about Segments of an Enterprise and Related Information*, allocates resources to and assesses the performance by these segments. Prior to 2006, we had a single reportable segment semiconductor manufacturing.

### **Item 7A. Quantitative and Qualitative Disclosures About Market Risk**

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

*Foreign Currency Risk.* 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 December 31, 2006 for our Korean subsidiary, a 10% devaluation of the Korean Won against the U.S. dollar would have resulted in a decrease of \$3.2 million in our U.S. dollar financial instruments balance and cash balance.

*Interest Rate Risk.* The \$200 million 6<sup>7</sup>/<sub>8</sub>% Second Priority Senior Secured Notes due 2011 and the \$250 million 8% Senior Subordinated Notes due 2014 are subject to changes in fair value due to interest rate changes. If the market interest rate had decreased by 10% and all other variables were held constant from their levels at December 31, 2006, we estimate that we would have additional interest expense costs over the market rate of \$2.8 million (360 days basis). The fair value of these fixed rate notes would have decreased by \$8.6 million or increased by \$8.9 million with a 10% increase or decrease in the interest rate, respectively.

*Cash Flow Interest Rate Risk.* In 2005, we entered into an interest rate swap agreement to convert the variable interest rate on our Floating Rate Second Priority Senior Secured Notes to a fixed interest rate for the periods to maturity date of June 2008. With this interest rate swap, cash flow interest rate risk was replaced with exposure to interest rate risk. For details, refer to Note 9. Long-term Borrowings.

**Table of Contents**

**Item 8. Financial Statements and Supplementary Data.**

**Index to Consolidated Financial Statements**

	<b>Page</b>
<b><u>Report of Independent Registered Public Accounting Firm</u></b>	36
<b>Consolidated Financial Statements</b>	
<u>Statements of Operations (for the years ended December 31, 2006 and 2005, the three months ended December 31, 2004 (successor company) and the nine months ended September 30, 2004 (predecessor company))</u>	38
<u>Balance Sheets (as of December 31, 2006 and 2005 (successor company))</u>	39
<u>Statements of Changes in Unitholders' Equity (for the years ended December 31, 2006 and 2005, the three months ended December 31, 2004 (successor company) and the nine months ended September 30, 2004 (predecessor company))</u>	40
<u>Statements of Cash Flows (for the years ended December 31, 2006 and 2005, the three months ended December 31, 2004 (successor company) and the nine months ended September 30, 2004 (predecessor company))</u>	41
<u>Notes to Consolidated Financial Statements</u>	42

**Table of Contents**

**Report of Independent Registered Public Accounting Firm**

To the Board of Directors and Unitholders of

MagnaChip Semiconductor LLC (Successor Company)

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of operations, of changes in unitholders equity and of cash flows present fairly, in all material respects, the financial position of MagnaChip Semiconductor LLC and its subsidiaries (the Company ) at December 31, 2006 and 2005, and the results of their operations and their cash flows for the years ended December 31, 2006 and 2005 and for the three-month period ended December 31, 2004 (successor basis), in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits of these statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

/s/ Samil PricewaterhouseCoopers

Seoul, Korea

March 26, 2007

**Table of Contents**

**Report of Independent Registered Public Accounting Firm**

To the Board of Directors and Unitholders of

MagnaChip Semiconductor LLC (Predecessor Company)

In our opinion, the accompanying consolidated (carve-out) statements of operations, of changes in owners' equity and of cash flows present fairly, in all material respects, the results of operations and cash flows of MagnaChip Semiconductor LLC and its subsidiaries (Predecessor Company) (the Company) for the nine-month period ended September 30, 2004 (predecessor basis), in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits of these statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

/s/ Samil PricewaterhouseCoopers

Seoul, Korea

June 15, 2005

**Table of Contents****MagnaChip Semiconductor LLC and Subsidiaries****Consolidated Statements of Operations****(In thousands of US dollars, except unit data)**

	Year Ended		Three months ended December 31, 2004	Nine months ended September 30, 2004 (Predecessor Company)
	December 31, 2006	December 31, 2005 (Successor Company)		
Net sales				
Related party	\$	\$	\$	\$ 163,760
Other	744,352	937,656	243,582	677,828
	744,352	937,656	243,582	841,588
Cost of sales	644,911	728,999	204,461	654,569
Gross profit	99,441	208,657	39,121	187,019
Selling, general and administrative expenses	87,677	123,211	29,784	53,982
Research and development expenses	131,252	107,590	22,058	75,657
Restructuring and impairment charges	94,266	36,234		
Operating income (loss)	(213,754)	(58,378)	(12,721)	57,380
Other income (expenses)				
Interest expense, net	(57,159)	(57,236)	(16,816)	(17,749)
Foreign currency gain, net	50,861	16,532	30,437	5,364
Other				1,070
	(6,298)	(40,704)	13,621	(11,315)
Income (loss) before income taxes	(220,052)	(99,082)	900	46,065
Income tax expenses	9,258	1,816	6,725	2,828
Net income (loss)	\$ (229,310)	\$ (100,898)	\$ (5,825)	\$ 43,237
Dividends accrued on preferred units	10,912	9,928	13,428	
Net loss attributable to common units	\$ (240,222)	\$ (110,826)	\$ (19,253)	
Net loss per common unit Basic and diluted	\$ (4.54)	\$ (2.10)	\$ (0.38)	
Weighted average number of units Basic and diluted	52,911,734	52,898,497	50,061,910	

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





**Table of Contents****MagnaChip Semiconductor LLC and Subsidiaries****Consolidated Balance Sheets****(In thousands of US dollars, except unit data)**

	December 31, 2006	December 31, 2005
<b>Assets</b>		
Current assets		
Cash and cash equivalents	\$ 89,173	\$ 86,574
Restricted cash		2,837
Accounts receivable, net	76,665	112,053
Inventories, net	57,846	88,677
Other receivables	6,754	9,501
Other current assets	13,626	10,148
<b>Total current assets</b>	<b>244,064</b>	<b>309,790</b>
Property, plant and equipment, net	336,279	485,077
Intangible assets, net	139,729	191,389
Other non-current assets	49,981	54,391
<b>Total assets</b>	<b>\$ 770,053</b>	<b>\$ 1,040,647</b>
<b>Liabilities and Unitholders Equity</b>		
Current liabilities		
Accounts payable	\$ 62,399	\$ 93,911
Other accounts payable	32,423	35,368
Accrued expenses	23,647	28,968
Other current liabilities	2,980	10,102
<b>Total current liabilities</b>	<b>121,449</b>	<b>168,349</b>
Long-term borrowings	750,000	750,000
Accrued severance benefits, net	62,836	55,124
Other non-current liabilities	2,935	7,196
<b>Total liabilities</b>	<b>937,220</b>	<b>980,669</b>
<b>Commitments and contingencies</b>		
Series A redeemable convertible preferred units; 60,000 units authorized, 50,091 units issued and 0 unit outstanding at December 31, 2006 and 2005		
Series B redeemable convertible preferred units; 550,000 units authorized, 450,692 units issued and 93,997 units outstanding at December 31, 2006 and 2005	117,374	106,462
<b>Total redeemable convertible preferred units</b>	<b>117,374</b>	<b>106,462</b>
<b>Unitholders equity</b>		
Common units; 65,000,000 units authorized, 52,720,784 and 53,091,570 units issued and outstanding at December 31, 2006 and 2005, respectively	52,721	53,092
Additional paid-in capital	2,451	2,169
Accumulated deficit	(370,314)	(130,092)

Edgar Filing: MAGNACHIP SEMICONDUCTOR LLC - Form 10-K

Accumulated other comprehensive income	30,601	28,347
Total unitholders' equity	(284,541)	(46,484)
Total liabilities, redeemable convertible preferred units and unitholders' equity	\$ 770,053	\$ 1,040,647

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

**Table of Contents****MagnaChip Semiconductor LLC and Subsidiaries****Consolidated Statements of Changes in Unitholders' Equity and Owners' Equity**

(In thousands of US dollars, except unit data)

	Common Units			Owner Equity	Deferred Stock Compensation	Accumulated deficit	Accumulated Other Comprehensive Income (loss)	Total
	Units	Amount	Additional Paid-In Capital					
<b>(Predecessor Company)</b>								
<b>Balance at January 1, 2004</b>				\$ 135,781	\$ 2,350		\$ 17,183	\$ 155,314
Comprehensive income :								
Net income				43,237				43,237
Foreign currency translation adjustments							4,842	4,842
Total comprehensive income								48,079
Deferred stock compensation					3,324			3,324
<b>Balance at September 30, 2004</b>				\$ 179,018	\$ 5,674		\$ 22,025	\$ 206,717
<b>(Successor Company)</b>								
<b>Balance at October 1, 2004</b>	49,713,286	\$ 49,713	\$			\$ (13)	\$ (116)	\$ 49,584
Issuance of common units	363,627	364						364
Exercise of unit options	2,456,090	2,456						2,456
Issuance of warrants in connection with Original Acquisition			2,100					2,100
Payment of accumulated accrued dividends						(10,891)		(10,891)
Dividends accrued on preferred units						(2,537)		(2,537)
Comprehensive income (loss):								
Net loss						(5,825)		(5,825)
Foreign currency translation adjustments							20,621	20,621
Total comprehensive income								14,796
<b>Balance at December 31, 2004</b>	52,533,003	\$ 52,533	\$ 2,100			\$ (19,266)	\$ 20,505	\$ 55,872
Issuance of common units	504,317	504	10					514
Exercise of unit options	54,250	55	59					114
Dividends accrued on preferred units						(9,928)		(9,928)
Comprehensive income (loss):								
Net loss						(100,898)		(100,898)
Fair valuation of derivatives							4,534	4,534
Foreign currency translation adjustments							3,308	3,308
Total comprehensive loss								(93,056)
<b>Balance at December 31, 2005</b>	53,091,570	\$ 53,092	\$ 2,169			\$ (130,092)	\$ 28,347	\$ (46,484)
Exercise of unit options	46,062	46	42					88
Repurchase of common units	(416,848)	(417)	(3)					(420)
Unit-based compensation			243					243
Dividends accrued on preferred units						(10,912)		(10,912)
Comprehensive income (loss):								
Net loss						(229,310)		(229,310)
Fair valuation of derivatives							(193)	(193)
Foreign currency translation adjustments							2,447	2,447

Edgar Filing: MAGNACHIP SEMICONDUCTOR LLC - Form 10-K

Total comprehensive loss (227,056)

<b>Balance at December 31, 2006</b>	52,720,784	\$ 52,721	\$ 2,451	\$ (370,314)	\$ 30,601	\$ (284,541)
-------------------------------------	------------	-----------	----------	--------------	-----------	--------------

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

**Table of Contents****MagnaChip Semiconductor LLC and Subsidiaries****Consolidated Statements of Cash Flows**

(In thousands of US dollars)

	Year Ended December 31		Three months ended December 31,	Nine months ended September 30,
	2006	2005 (Successor Company)	2004	2004 (Predecessor Company)
<b>Cash flows from operating activities</b>				
Net income (loss)	\$ (229,310)	\$ (100,898)	\$ (5,825)	\$ 43,237
Adjustments to reconcile net income (loss) to net cash provided by operating activities				
Depreciation and amortization	188,560	202,929	45,855	266,862
Provision for severance benefits	11,497	16,583	3,397	15,353
Amortization of debt issuance costs	3,701	3,432	4,411	
Gain on foreign currency translation, net	(54,188)	(15,880)	(33,263)	(3,811)
Loss (gain) on disposal of property, plant and equipment, net	1,490	(829)	(193)	(488)
Impairment charges	92,858	33,576		
Unit/stock-based compensation	243			3,324
Other	3,023	721	494	3,138
Changes in operating assets and liabilities				
Accounts receivable	44,091	(25,812)	(43,270)	(7,067)
Inventories	37,064	(806)	36,513	(18,070)
Other receivables	3,180	62,821	(56,917)	(548)
Deferred tax assets	1,954	(12,935)		
Accounts payable	(38,423)	24,928	(33,061)	(5,719)
Other accounts payable	(15,897)	(66,069)	81,509	18,329
Accrued expenses	(7,453)	(5,184)	17,711	584
Other current assets	5,063	2,713	(6,009)	(1,177)
Other current liabilities	(7,329)	200	9,842	1,450
Payment of severance benefits	(8,589)	(13,831)	(2,898)	(6,602)
Other	(1,065)	(2,012)	(1,011)	3,376
Net cash provided by operating activities	30,470	103,647	17,285	312,171
<b>Cash flows from investing activities</b>				
Proceeds from disposal of plant, property and equipment	3,651	673		
Proceeds from disposal of intangible assets	2,819			
Purchase of plant, property and equipment	(39,196)	(62,334)	(23,346)	(84,595)
Payment for intellectual property registration	(2,203)	(2,174)	(108)	(2,128)
Acquisition of business, net of cash acquired of \$4,620 and \$0 for the year ended December 31, 2005 and for three months ended December 31, 2004, respectively		(11,749)	(488,152)	
Decrease (increase) in restricted cash	3,002	10,307	(12,350)	
Other	(1,458)	1,205	(2,027)	1,392
Net cash used in investing activities	(33,385)	(64,072)	(525,983)	(85,331)
<b>Cash flows from financing activities</b>				
Proceeds from issuance of Senior Secured and Subordinated Notes			750,000	
Proceeds from long-term borrowings			45,867	
Proceeds from short-term borrowings			720	
Issuance of common units	88	628	2,820	
Issuance of redeemable convertible preferred units			3,636	
Repayment of short-term borrowings		(12,883)		(46,978)
Repayment of long-term borrowings			(347,718)	(179,862)

## Edgar Filing: MAGNACHIP SEMICONDUCTOR LLC - Form 10-K

Repurchase of common units	(420)			
Redemption of redeemable convertible preferred units			(406,786)	
Payment of preferred dividends			(10,891)	
Debt issuance costs paid	(594)		(27,635)	
Other			(16)	
Net cash provided by (used in) financing activities	(332)	(12,849)	9,997	(226,840)
Effect of exchange rates on cash and cash equivalents	5,846	1,452	10,217	
Net increase (decrease) in cash and cash equivalents	2,599	28,178	(488,484)	
<b>Cash and cash equivalents</b>				
Beginning of the period	86,574	58,396	546,880	
End of the period	\$ 89,173	\$ 86,574	\$ 58,396	\$
<b>Supplemental cash flow information</b>				
Cash paid for interest	\$ 56,025	\$ 53,373	\$ 11,862	\$ 17,791
Cash paid for income taxes	\$ 12,685	\$ 15,370	\$ 76	\$ 2,828

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

## **Table of Contents**

### **MagnaChip Semiconductor LLC and Subsidiaries**

#### **Notes to Consolidated Financial Statements**

**(Tabular dollars in thousands, except unit data)**

## **1. General**

### **The Company**

MagnaChip Semiconductor LLC and its subsidiaries (successor company) (the Company) is a leading designer, developer and manufacturer of mixed-signal and digital multimedia semiconductors addressing the convergence of consumer electronics and communication devices.

The Company operates in three segments Display Solutions, Imaging Solutions and Semiconductor Manufacturing Services. The Display Solutions segment offers flat panel display drivers for the entire product range of small to large panel displays, including mobile handsets, handheld gaming devices, PDAs, displays for desktop and mobile computer monitors and flat panel televisions. The Imaging Solutions segment addresses a broad spectrum of consumer electronics products ranging from camera-equipped mobile handsets to personal computer webcams, offering VGA, 1.3, 2.1 and 3.2 megapixel CMOS image sensors. The Semiconductor Manufacturing Services segment uses the Company's process technology and manufacturing facilities to manufacture semiconductor wafers for third parties based on their designs. The Company has five wafer fabrication facilities located in Cheongju and Gumi in the Republic of Korea.

MagnaChip Semiconductor LLC was created on November 26, 2003 and was capitalized on September 10, 2004 under the laws of the State of Delaware. It was created with the sole purpose of acquiring the non-memory business (the Business) of Hynix Semiconductor Inc. (Hynix), which acquisition was completed with effect from October 1, 2004 (the Original Acquisition).

## **2. Summary of Significant Accounting Policies**

### **Basis of Presentation**

The consolidated financial statements are presented in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP). Significant accounting policies followed by the Company in the preparation of the accompanying financial statements are summarized below.

For the periods as of and prior to September 30, 2004, the accompanying consolidated financial statements are presented on a carve-out basis reflecting the assets, liabilities, revenues, expenses and changes in owner's equity and cash flows that were directly attributable to the Business of Hynix (predecessor company), which was purchased on October 6, 2004. The Company has used October 1, 2004, as the effective date of the Original Acquisition since the financial results from October 1, 2004 onwards accrue to its benefit.

### **Principles of Consolidation**

The consolidated financial statements include the accounts of the Company including its wholly-owned subsidiaries. All significant intercompany transactions and balances are eliminated in consolidation.

### **Use of Estimates**

The preparation of financial statements in accordance with U.S. GAAP requires management to make estimates and assumptions that affect the amounts reported in the accompanying financial statements and disclosures. The most significant estimates and assumptions relate to the useful life of property, plant and equipment, allowance for uncollectible accounts receivable, contingent liabilities, inventory valuation, restructuring accrual and impairment of long-lived assets. Although these estimates are based on management's best knowledge of current events and actions that the Company may undertake in the future, actual results may be different from the estimates.

**Table of Contents**

**MagnaChip Semiconductor LLC and Subsidiaries**

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

**(Tabular dollars in thousands, except unit data)**

**Foreign Currency Translation**

The Company has assessed in accordance with Statements of Financial Accounting Standards ( SFAS ) No. 52, *Foreign Currency Translation*, the functional currency of each of its subsidiaries in Luxembourg, the Netherlands and the United Kingdom and has designated the U.S. dollar to be their respective functional currencies. The Company and its other subsidiaries are utilizing their local currencies as their functional currencies. The financial statements of the subsidiaries in functional currencies other than the U.S. dollar are translated into the U.S. dollar in accordance with SFAS No. 52. All the assets and liabilities are translated to the U.S. dollar at the end-of-period exchange rates. Capital accounts are determined to be of a permanent nature and are therefore translated using historical exchange rates. Revenues and expenses are translated using average exchange rates. Foreign currency translation adjustments arising from differences in exchange rates from period to period are included in the foreign currency translation adjustment account in accumulated comprehensive income (loss) of unitholders' equity. Transactions in currencies other than the functional currency are included as a component of other income (expense) in the statement of operations.

**Cash and Cash Equivalents**

Cash equivalents consist of highly liquid investments with an original maturity date of three months or less.

**Accounts receivable reserves**

An allowance for doubtful accounts is provided based on the aggregate estimated collectibility of their accounts receivable. The Company records an allowance for cash returns, presented within accounts receivable, based on the historical experience of the amount of goods that will be returned and refunded. In addition, the Company also includes in accounts receivable, an allowance for additional products that may have to be provided, free of charge, to compensate customers for products that do not meet previously agreed yield criteria, the low yield compensative reserve.

**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. Reserves are also established for excess inventory based on inventory levels in excess of six months of projected demand, as judged by management, for each specific product.

In addition, as prescribed in SFAS No. 151, 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 the management believes to be normal, the fixed overhead costs per production unit which exceeds those under normal capacity, are charged to cost of sales rather than capitalized as inventories.



**Table of Contents****MagnaChip Semiconductor LLC and Subsidiaries****Notes to Consolidated Financial Statements (Continued)****(Tabular dollars in thousands, except unit data)****Property, Plant and Equipment**

Property, plant and equipment are stated at cost, less accumulated depreciation. Depreciation is computed using the straight-line method over the estimated useful lives of the assets as set forth below.

Buildings	30 - 40 years
Building related structures	10 - 20 years
Machinery and equipment	5 - 10 years
Vehicles and others	5 years

Routine maintenance and repairs are charged to expense as incurred. Expenditures that enhance the value or significantly extend the useful lives of the related assets are capitalized.

Borrowing costs incurred during the construction period of assets are capitalized as part of the related assets.

**Impairment of Long-Lived Assets**

The Company reviews 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. Recoverability is measured by comparison of its carrying amount with the future net 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 value 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.

**Restructuring Charges**

The Company recognizes restructuring charges in accordance with SFAS No. 146, *Accounting for Costs Associated with Exit or Disposal Activities*. Certain costs and expenses related to exit or disposal activities are recorded as restructuring charges when liabilities for those costs and expenses are incurred.

**Lease Transactions**

The Company accounts for lease transactions as either operating leases or capital leases, depending on the terms of the underlying lease agreements. Machinery and equipment acquired under capital lease agreements are recorded at cost as property, plant and equipment and depreciated using the straight-line method over their estimated useful lives. In addition, the aggregate lease payments are recorded as capital lease obligations, net of unaccrued interest. Interest is amortized over the lease period using the effective interest rate method. Leases that do not qualify as capital leases are classified as operating leases, and the related rental payments are expensed on a straight-line basis over the lease term.

**Software**

The Company capitalizes certain external costs that are incurred to purchase and implement internal-use computer software. Direct costs relating to the development of software for internal use are capitalized after technological feasibility has been established, in accordance with Statement Of Position ( SOP ) No. 98-1, *Accounting for the Costs of Computer Software Developed or Obtained for Internal Use*. Depreciation is calculated on a straight line basis over five years.



**Table of Contents**

**MagnaChip Semiconductor LLC and Subsidiaries**

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

**(Tabular dollars in thousands, except unit data)**

**Intangible Assets**

Intangible assets acquired from Hynix include technology and customer relationships which are amortized on a straight-line basis over periods ranging from 4 to 8 years. Other intellectual property assets acquired represent rights under patents, trademarks and property use rights and are amortized over the periods of benefit, ranging up to 10 years, on a straight-line basis.

**Fair Value Disclosures of Financial Instruments**

The estimated fair value of financial instruments is determined by the Company, using available market information and valuation methodologies considered to be appropriate. However, considerable judgment is required in interpreting market data to develop the estimates of fair value. Carrying amounts of accounts receivable and accounts payable approximate fair value due to the short maturity of these financial instruments.

The estimated fair value of the Company's debt was \$612.6 million, \$738.8 million and \$750.0 million as of December 31, 2006, 2005 and 2004, respectively. The fair value estimates presented herein were based on market interest rates and other market information available to management as of each balance sheet date presented. The use of different market assumptions and/or estimation methodologies could have a material effect on the estimated fair value amounts. The approximate fair values do not take into consideration expenses that could be incurred in an actual settlement. Accordingly, the estimates presented herein are not necessarily indicative of the amounts that the Company could realize in a current market exchange.

**Accrued Severance Benefits**

The majority of accrued severance benefits is for employees in the Company's Korean subsidiary. Pursuant to the Labor Standards 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 December 31, 2006, 97% of all employees of the Company were eligible for severance benefits.

Accrued severance benefits are funded through a group severance insurance plan. The amounts funded under this insurance plan are classified as a deduction to the accrued severance benefits. Subsequent accruals are to be funded at the discretion of the Company.

In accordance with the National Pension Act of the Republic of Korea, a certain portion of accrued severance benefits is deposited with the National Pension Fund and deducted from the accrued severance benefits. The contributed amount is refunded to employees from the National Pension Fund upon their retirement.

**Revenue Recognition**

Revenue is recognized when persuasive evidence of an arrangement exists, the product has been delivered and title and risk of loss have transferred, the price is fixed and determinable, and collection of the resulting receivable is reasonably assured. Utilizing these criteria, product revenue is generally recognized upon delivery of the product at the end-customer's location when the risks and rewards of ownership have passed to the customer. Revenue is deferred from sales to distributors until the product is ultimately sold to the end-customer.

All amounts billed to a customer related to shipping and handling are classified as sales while all costs incurred by the Company for shipping and handling are classified as selling expenses. The amounts charged to selling expenses are \$1,332 thousand and \$1,867 thousand for the years ended December 31, 2006 and 2005, \$412 thousand for the three-month period ended December 31, 2004 (successor company) and \$1,394 thousand for the nine-month period ended September 30, 2004 (predecessor company).



## **Table of Contents**

### **MagnaChip Semiconductor LLC and Subsidiaries**

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

**(Tabular dollars in thousands, except unit data)**

#### **Derivative Financial Instruments**

The Company's primary objective for holding derivative financial instruments is to manage cash flow risk inherent in debts with variable interest rates. The company recognizes all derivative financial instruments at fair value as either assets or liabilities and reports changes in the fair value of those instruments in earnings or other comprehensive income depending on whether they meet the criteria for designation as hedging transactions under SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities*, as amended.

#### **Advertising**

The Company expenses advertising costs as incurred. Advertising expense was approximately \$81 thousand and \$310 thousand for the years ended December 31, 2006 and 2005, \$173 thousand for the three-month period ended December 31, 2004 (successor company), and \$71 thousand for the nine-month period ended September 30, 2004 (predecessor company).

#### **Product Warranties**

The Company records, in other current liabilities, warranty liabilities for the estimated costs that may be incurred under its basic limited warranty. This warranty covers defective products, and related liabilities are accrued when product revenues are recognized. Factors that affect the Company's warranty liability include historical and anticipated rates of warranty claims and repair costs per claim to satisfy the Company's warranty obligation. As these factors are impacted by actual experience and future expectations, the Company periodically assesses the adequacy of its recorded warranty liabilities and adjusts the amounts when necessary.

#### **Research and Development**

Research and development costs are expensed as incurred and include wafer, masks, employee expense, contractor fees, building costs, utilities, and administrative expenses.

#### **Licensed Patents and Technologies**

The Company has entered into a number of royalty agreements to license patents and technology used in the design and manufacture of its products. The payments under these agreements include an initial payment to acquire the rights, and a royalty payment, calculated based upon the sales of the related products. The initial payments, usually paid in installments, represents a non-refundable commitment, such that the total present value of these payments is recorded as a liability upon execution of the agreement, and the costs are deferred over the period of the agreement. The royalty payments are charged to the statement of operations as incurred.

#### **Unit-Based Compensation (Successor Company)**

Effective January 1, 2006, the Company adopted the provisions of SFAS 123(R), *Share-Based Payment (revised 2004)*. As the Company elected to use the modified prospective application method, no restatement was made to the consolidated statements of operations for prior periods. Under SFAS 123(R), unit-based compensation cost is measured at grant date, based on the fair value of the award, and is recognized as expense over the requisite service period. As permitted under SFAS No. 123(R), the Company elected to recognize compensation expense for all options with graded vesting based on the graded attribution method.

Prior to 2006, the Company accounted for its unit-based compensation using the intrinsic value method prescribed in Accounting Principles Board (APB) Opinion No. 25, *Accounting for Stock Issued to Employees*, and provided the required pro forma disclosures of SFAS No. 123, *Accounting for Stock-Based Compensation*.



**Table of Contents**

**MagnaChip Semiconductor LLC and Subsidiaries**

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

**(Tabular dollars in thousands, except unit data)**

As the exercise prices for all option grants were in excess of the fair value of the underlying units on the respective grant dates, no compensation cost was recorded for the year ended December 31, 2005 and for the three months ended December 31, 2004.

Consistent with the valuation method for the disclosure-only provisions of FAS No. 123, the Company uses the Black-Scholes option pricing-model to measure the grant-date-fair-value of options. The Black-Scholes model requires certain assumptions to determine an option's fair value, including expected term, risk free interest, expected volatility and fair value of underlying common unit. The expected term of each option grant was based on employees' expected exercises and post-vesting employment termination behavior and the risk free interest rate was based on the U.S. Treasury yield curve for the period corresponding with the expected term at the time of grant. The expected volatility was estimated using historical volatility of share prices of similar public entities. No dividends were assumed for this calculation of option value. The fair value of the underlying common unit is determined based on an independent appraisal from a third party and is updated to reflect changes in the Company's financial results and prospects.

**Stock option Plan (Predecessor Company)**

Stock options under employee stock plans prior to the Original Acquisition were accounted for using the intrinsic value method prescribed by APB Opinion No. 25, *Accounting for Stock Issued to Employees*. As part of the presentation of the Business on a carve-out basis, stock compensation was allocated to the Business based on the employees that historically have worked in the Business. The compensation cost for the Business was \$3,324 thousand for the nine-month period ended September 30, 2004.

**Earnings per Unit**

In accordance with SFAS No. 128, *Earnings Per Share*, the Company computes basic earnings per unit by dividing net income available to common unitholders by the weighted average number of common units outstanding during the period which would include to the extent their effect is dilutive: redeemable convertible preferred units, options to purchase common units and warrants to purchase common units. Diluted earnings per unit reflect the dilution of potential common units outstanding during the period. In determining the hypothetical units repurchased, the Company uses the average unit price for the period.

**Income Taxes**

MagnaChip Semiconductor LLC has elected to be treated as a partnership for U.S. federal income tax purposes, and therefore is not subject to income taxes on its income. Taxes on its income are the responsibility of the individual equity owners of MagnaChip Semiconductor LLC. The Company operates a number of subsidiaries, which are subject to local income taxes in those markets.

The Company accounts for income taxes in accordance with SFAS No. 109, *Accounting for Income Taxes*. SFAS No. 109 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 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.

---

**Table of Contents**

**MagnaChip Semiconductor LLC and Subsidiaries**

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

**(Tabular dollars in thousands, except unit data)**

**Segment Information**

The Company has determined, based on the nature of its operations and products offered to customers, that its reportable segments are Display Solutions, Imaging Solutions, and Semiconductor Manufacturing Services. The Display Solutions segment's primary products are flat panel display drivers and the Imaging Solutions segment's primary products are CMOS image sensors. The Semiconductor Manufacturing Service segment provides for wafer foundry services to clients. Net sales and gross profit for the All other category primarily relates to certain business activities that do not constitute operating or reportable segments.

The Company's chief operating decision maker ( CODM ) as defined by SFAS 131, *Disclosure about Segments of an Enterprise and Related Information*, allocates resources to and assesses the performance of each segment using information about its revenue and gross profit. The Company does not identify or allocate assets by segments, nor does the CODM evaluate operating segments using discrete asset information. In addition, the Company does not allocate operating expenses, interest income or expense, other income or expense, or income tax expenses to the segments. Management does not evaluate segments based on these criteria.

Prior to 2006, the Company had a single reportable segment. In 2006, subsequent to the appointment of our new CODM, the Company changed the manner in which the CODM reviewed the Company's operational results and made significant business decisions to include disaggregated financial information of its three primary business units. Segment information for the years ended December 31, 2005 and 2004 was prepared in conformity with the current segment structure.

**Concentration of Credit Risk**

The Company performs periodic credit evaluations of its customers' financial condition and generally does not require collateral for customers on accounts receivable. The Company maintains reserves for potential credit losses, but historically has not experienced significant losses related to individual customers or groups of customers in any particular industry or geographic area. The Company derives a substantial portion of its revenues from export sales through its overseas subsidiaries in Asia, North America and Europe.

**Recent Accounting Pronouncements**

In September 2006, the Financial Accounting Standards Board ( FASB ) issued SFAS No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plan* an amendment of SFAS No. 87, 88, 106 and 132(R). This Statement requires an employer to recognize the over funded or under funded status of a defined benefit post retirement plan (other than a multiemployer plan) as an asset or liability in its statement of financial position, and to recognize changes in that funded status in the year in which the changes occur through comprehensive income. SFAS 158 is effective for fiscal years ending after June 15, 2007. The Company does not expect that the implementation of SFAS No. 158 will have a material impact on its financial position and results of operations.

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements*. This Statement defines fair value, establishes a framework for measuring fair value and requires enhanced disclosures about fair value measurements. SFAS 157 requires companies to disclose the fair value of their financial instruments according to a fair value hierarchy, as defined and may be required to provide additional disclosures based on that hierarchy. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007. The Company is currently evaluating the impact that the adoption may have on its consolidated financial statements.

In September 2006, the Securities and Exchange Commission ( SEC ) issued Staff Accounting Bulletin ( SAB ) No. 108 which provides interpretive guidance on how the effects of the carryover or reversal of prior



**Table of Contents**

**MagnaChip Semiconductor LLC and Subsidiaries**

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

**(Tabular dollars in thousands, except unit data)**

year misstatements should be considered in quantifying a current year misstatement. The guidance is applicable for fiscal years ending after November 15, 2006. The Company does not expect that adoption of SAB 108 will have a material impact on its consolidated financial statements.

In June 2006, the FASB issued FASB Interpretation ( FIN ) No. 48, *Accounting for Uncertainty in Income Taxes* an interpretation of SFAS No. 109. FIN 48 clarifies the accounting for uncertain income tax positions accounted for in accordance with SFAS No. 109. The Interpretation stipulates recognition and measurement criteria in addition to classification and interim period accounting. The Interpretation significantly expanded disclosure provisions for uncertain tax positions that are expected to be taken in a company's tax return. FIN 48 is effective for fiscal years beginning after December 15, 2006. The Company is currently evaluating the impact that the adoption may have on its consolidated financial statements.

In March 2006, the FASB issued SFAS No. 156, *Accounting for Servicing of Financial Assets* an amendment of FASB Statement No. 140. This Statement addresses the accounting for recognized servicing assets and liabilities related to certain transfers of the servicer's financial assets and for acquisitions or assumptions of obligations to service financial assets that do not relate to the financial assets of the servicer and its related parties. SFAS 156 requires that all recognized servicing assets and liabilities are initially measured at fair value, and subsequently measured at either fair value or by applying an amortization method for each class of recognized servicing assets and liabilities. SFAS 156 is effective in fiscal years beginning after September 15, 2006. The adoption of SFAS 156 is not expected to have a material impact on the Company's consolidated financial statements.

In February 2006, the FASB issued SFAS No. 155, *Accounting for Certain Hybrid Financial Instruments* an amendment of FASB Statements No. 133 and 140. This Statement amends SFAS No. 133 and SFAS No. 140, and improves the financial reporting of certain hybrid financial instruments by requiring more consistent accounting. Specifically, this Statement allows fair value remeasurement for any hybrid financial instrument that contains an embedded derivative that otherwise would require bifurcation. This Statement is effective for all financial instruments acquired or issued after the beginning of an entity's first fiscal year that begins after September 15, 2006. The Company does not expect that adoption of this Statement will have a material impact on its consolidated financial statements.

**3. Original Acquisition**

On October 6, 2004, the Company completed its purchase of the Business, as outlined in the Business Transfer Agreement, as amended (the BTA ) from Hynix, for cash, liabilities assumed, plus a warrant to purchase 5,079,254 common equity interests in the Company, valued by independent valuation. In October 2005, the Company agreed to pay Hynix an additional \$6,238 thousand in cash as a working capital settlement payment. This additional amount, which was paid in full subsequently in October 2005, was included as part of the purchase consideration and therefore acquisition costs of related assets were subsequently adjusted.

**Table of Contents****MagnaChip Semiconductor LLC and Subsidiaries****Notes to Consolidated Financial Statements (Continued)****(Tabular dollars in thousands, except unit data)**

A summary of purchase consideration including such subsequent working capital settlement as well as assets and liabilities acquired is as follows:

Purchase consideration:	
Cash	\$ 475,471
Loan assumed	285,807
Warrant to purchase common units	2,100
	763,378
Fair value of assets and liabilities acquired:	
Current assets	(173,517)
Non-current assets	(755,618)
Current liabilities	119,262
Non-current liabilities	46,495
	\$

Intangible assets acquired in connection with this acquisition are included in non-current assets and summarized as below:

	Acquisition cost	Weighted average amortization period
Technology	\$ 24,536	5.3 years
Customer relationship	174,134	7.0 years
Intellectual property assets	7,928	5.2 years
	\$ 206,598	6.7 years

At the date of the Original Acquisition, the Company obtained an independent valuation of the acquired property, plant and equipment and the acquired intangible assets, to ascertain the fair value of these assets, and in addition, applied adjustments to the book value of the other assets and liabilities transferred from Hynix to calculate the total fair value of the assets and liabilities acquired. The Company also re-assessed the remaining useful lives of the acquired property, plant and equipment, and commenced depreciation on a straight-line basis, using the remaining useful lives of the acquired property, plant and equipment and acquired intangibles.

The aggregate fair values obtained exceeded the total purchase consideration of \$763,378 thousand, and this difference was applied to the Company's intangible and non-current tangible assets on a pro-rata basis, such that the adjusted fair value of the assets and liabilities acquired equaled the total purchase consideration, with no residual negative goodwill.

**4. Accounts Receivable**

Accounts receivable as of December 31, 2006 and 2005 consist of the following:

Edgar Filing: MAGNACHIP SEMICONDUCTOR LLC - Form 10-K

	December 31, 2006	December 31, 2005
Accounts receivable	\$ 65,203	\$ 93,221
Notes receivable	16,812	25,115
Less:		
Allowances for doubtful accounts	(1,418)	(617)
Cash return reserve	(1,450)	(3,000)
Low yield compensation reserve	(2,482)	(2,666)
Accounts receivable, net	\$ 76,665	\$ 112,053

**Table of Contents****MagnaChip Semiconductor LLC and Subsidiaries****Notes to Consolidated Financial Statements (Continued)**

(Tabular dollars in thousands, except unit data)

Changes in allowance for doubtful accounts for each period are as follows:

	Year ended December 31		Three months ended December 31,	Nine months ended September 30,
	2006	2005 (Successor Company)	2004	2004 (Predecessor Company)
Beginning balance	\$ (617)	\$ (383)	\$	\$ (145)
Bad debt expense	(739)	(229)	(340)	(57)
Write off				94
Translation adjustments	(62)	(5)	(43)	(5)
Ending balance	\$ (1,418)	\$ (617)	\$ (383)	\$ (113)

Changes in cash return reserve for each period are as follows:

	Year ended December 31		Three months ended December 31,	Nine months ended September 30,
	2006	2005 (Successor Company)	2004	2004 (Predecessor Company)
Beginning balance	\$ (3,000)	\$ (2,156)	\$ (815)	\$ (71)
Addition to (reversal of) reserve	(2,100)	(8,131)	(3,660)	(1,895)
Payment made	3,862	7,351	2,475	1,161
Translation adjustments	(212)	(64)	(156)	(10)
Ending balance	\$ (1,450)	\$ (3,000)	\$ (2,156)	\$ (815)

Changes in low yield compensation reserve for each period are as follows:

	Year ended December 31		Three months ended December 31,	Nine months ended September 30,
	2006	2005 (Successor Company)	2004	2004 (Predecessor Company)
Beginning balance	\$ (2,666)	\$ (2,911)	\$ (2,874)	\$
Addition to (reversal of) reserve	(4,117)	(4,747)	(2,260)	(4,430)
Payment made	4,520	5,059	2,533	1,584
Translation adjustments	(219)	(67)	(310)	(28)

Edgar Filing: MAGNACHIP SEMICONDUCTOR LLC - Form 10-K

Ending balance	\$ (2,482)	\$ (2,666)	\$ (2,911)	\$ (2,874)
----------------	------------	------------	------------	------------

**5. Inventories**

Inventories as of December 31, 2006 and 2005 consist of the following:

	<b>December 31, 2006</b>	<b>December 31, 2005</b>
Finished goods	\$ 16,169	\$ 28,414
Semi-finished goods and work-in-process	39,492	60,095
Raw materials	11,774	5,814
Materials in-transit	2,063	1,966
Less: valuation allowances	(11,652)	(7,612)
Inventories, net	\$ 57,846	\$ 88,677

**Table of Contents****MagnaChip Semiconductor LLC and Subsidiaries****Notes to Consolidated Financial Statements (Continued)**

(Tabular dollars in thousands, except unit data)

Changes in valuation allowances for each period are as follows:

	Year ended December 31		Three months ended December 31,	Nine months ended September 30,
	2006	2005 (Successor Company)	2004	2004 (Predecessor Company)
Beginning balance	\$ (7,612)	\$ (6,274)	\$	\$ (6,651)
Loss on valuation	(10,212)	(2,816)	(6,339)	(7,728)
Write off	6,868	1,627	383	7,923
Translation adjustments	(696)	(149)	(318)	(229)
Ending balance	\$ (11,652)	\$ (7,612)	\$ (6,274)	\$ (6,685)

**6. Property, Plant and Equipment**

Property, plant and equipment as of December 31, 2006 and 2005 are comprised of the following:

	December 31, 2006	December 31, 2005
Buildings and related structures	\$ 162,383	\$ 149,236
Machinery and equipment	369,683	472,388
Vehicles and others	42,772	32,438
	574,838	654,062
Less: accumulated depreciation	(252,814)	(181,806)
Land	12,481	11,492
Construction in-progress	1,774	1,329
Property, plant and equipment, net	\$ 336,279	\$ 485,077

Aggregate depreciation expenses totaled \$153,245 thousand and \$157,678 thousand for the years ended December 31, 2006 and 2005, \$34,421 thousand for the three-month period ended December 31, 2004 (successor company) and \$261,640 thousand for the nine-month period ended September 30, 2004 (predecessor company), respectively. In addition, capitalized interest costs totaled \$64 thousand and \$144 thousand for the years ended December 31, 2006 and 2005, \$53 thousand for the three-month period ended December 31, 2004 (successor company) and \$334 thousand for the nine-month period ended September 30, 2004 (predecessor company), respectively.

Property, plant and equipment are pledged as collateral for our senior secured revolving credit facility and our Second Priority Senior Secured Notes to a maximum of \$780 million as of December 31, 2006.



**Table of Contents****MagnaChip Semiconductor LLC and Subsidiaries****Notes to Consolidated Financial Statements (Continued)**

(Tabular dollars in thousands, except unit data)

**7. Intangible assets**

Intangible assets at December 31, 2006 and 2005 are as follows:

	December 31, 2006	December 31, 2005
Technology	\$ 21,289	\$ 23,911
Customer relationships	170,209	193,958
Goodwill	15,095	15,095
Intellectual property assets	9,742	10,969
Less: accumulated amortization	(76,606)	(52,544)
Intangible assets, net	\$ 139,729	\$ 191,389

Aggregate amortization expenses for intangible assets totaled \$35,315 thousand and \$45,251 thousand for the years ended December 31, 2006 and 2005, \$11,434 thousand for the three-month period ended December 31, 2004 (successor company) and \$5,222 thousand for the nine-month period ended September 30, 2004 (predecessor company), respectively. The estimated aggregate amortization expense of intangible assets for the next five years is \$29,334 thousand in 2007, \$26,477 thousand in 2008, \$17,725 thousand in 2009, \$16,252 thousand in 2010 and \$13,602 thousand in 2011.

Intangible assets are pledged as collateral for our senior secured revolving credit facility and our Second Priority Senior Secured Notes as of December 31, 2006.

**8. Product Warranties**

Changes in accrued warranty liabilities for each period are as follows:

	Year ended December 31		Three months ended December 31, 2004	Nine months ended September 30, 2004
	2006	2005 (Successor Company)		(Predecessor Company)
Beginning balance	\$ 1,036	\$ 1,448	\$ 2,677	\$ 794
Addition to (reversal of) warranty reserve	(340)	1,362	(977)	4,103
Payments made	(647)	(1,804)	(477)	(2,265)
Translation adjustments	63	30	225	45
Ending balance	\$ 112	\$ 1,036	\$ 1,448	\$ 2,677

**9. Long-Term Borrowings**



## Edgar Filing: MAGNACHIP SEMICONDUCTOR LLC - Form 10-K

On December 23, 2004, two of the Company's subsidiaries, MagnaChip Semiconductor S.A. and MagnaChip Semiconductor Finance Company, issued \$500 million aggregate principal amount of Second Priority Senior Secured Notes consisting of \$300 million aggregate principal amount of Floating Rate Second Priority Senior Secured Notes and \$200 million aggregate principal amount of 6<sup>7</sup>/<sub>8</sub>% Second Priority Senior Secured Notes. At the same time, such subsidiaries issued \$250 million aggregate principal amount of 8% Senior Subordinated Notes.

Concurrently with the issuance of the Second Priority Senior Secured Notes, the Company entered into a new senior credit agreement with a syndicate of banks, financial institutions and other entities providing for a \$100 million senior secured revolving credit facility. Interest is charged at current rates when drawn upon.

**Table of Contents****MagnaChip Semiconductor LLC and Subsidiaries****Notes to Consolidated Financial Statements (Continued)****(Tabular dollars in thousands, except unit data)**

Details of long-term borrowings as of December 31, 2006 and 2005 are presented as below:

	<b>Maturity</b>	<b>Annual interest rate (%)</b>	<b>Amount of principal</b>
Floating Rate Second Priority Senior Secured Notes	2011	3 month LIBOR +3.250	\$ 300,000
6 <sup>7</sup> / <sub>8</sub> % Second Priority Senior Secured Notes	2011	6.875	200,000
8% Senior Subordinated Notes	2014	8.000	250,000
			\$ 750,000

The senior secured revolving credit facility and Second Priority Senior Secured Notes are collateralized by substantially all of the assets of the Company. These notes will be paid in full upon maturity.

Each indenture governing the notes contains covenants that limit the ability of the Company and its subsidiaries to (i) incur additional indebtedness, (ii) pay dividends or make other distributions on its capital stock or repurchase, repay or redeem its capital stock, (iii) make certain investments, (iv) incur liens, (v) enter into certain types of transactions with affiliates, (vi) create restrictions on the payment of dividends or other amounts to the Company by its subsidiaries, and (vii) sell all or substantially all of its assets or merge with or into other companies.

Borrowings under the senior secured credit facility are subject to significant conditions, including compliance with financial ratios and other covenants and obligations.

As of December 31, 2006, the Company and all of its subsidiaries except for MagnaChip Semiconductor (Shanghai) Company Limited have jointly and severally guaranteed each series of the Second Priority Senior Secured Notes on a second priority senior secured basis. As of December 31, 2006, the Company and all of its subsidiaries except for MagnaChip Semiconductor Ltd. (Korea) and MagnaChip Semiconductor (Shanghai) Company Limited have jointly and severally guaranteed the Senior Subordinated Notes on an unsecured, senior subordinated basis. In addition, the Company and each of its current and future direct and indirect subsidiaries (subject to certain exceptions) will be guarantors of Second Priority Senior Secured Notes and Senior Subordinated Notes.

In connection with the issuance of the notes and obtaining of the credit facility, the Company capitalized certain costs and fees, which are being amortized using the effective interest method or straight-line method over their respective terms, 2009 to 2014. Amortization costs, which were included in interest expense in the accompanying statements of operations, amounted to \$3,701 thousand, \$3,432 thousand and \$167 thousand for the years ended December 31, 2006 and 2005, and the three-month period ended December 31, 2004, respectively. The remaining capitalized costs as of December 31, 2006, 2005 and 2004 were \$21,860 thousand, \$25,113 thousand and \$27,812 thousand, respectively. In addition, in connection with the repayment of the assumed debt from Hynix, the Company wrote off \$4,084 thousand of previously capitalized financing fees for the three-month period ended December 31, 2004. These amounts have all been included in interest expense in the accompanying statement of operations.

On December 29, 2006, the Company entered into the Fifth Amendment to Credit Agreement (as amended, the Credit Agreement), dated as of December 29, 2006 (the Fifth Amendment), with MagnaChip Semiconductor S.A. and MagnaChip Semiconductor Finance Company, as borrowers, the Subsidiary Guarantors party thereto, the Lenders party thereto (the Lenders), and UBS AG, Stamford Branch, as administrative agent and collateral agent (the Agent). Under the Fifth Amendment, among other things, (i) the Company agreed to furnish to the Agent and the Lenders (a) monthly liquidity and flash revenue reports along with an officer's



**Table of Contents**

**MagnaChip Semiconductor LLC and Subsidiaries**

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

**(Tabular dollars in thousands, except unit data)**

certificate, (b) monthly narrative reports and management's discussion and analysis regarding the Company's consolidated financial condition and results of operations, and (c) monthly reports regarding the cash accounts maintained by the Company and its subsidiaries; and (ii) the existing financial covenants set forth in Section 6.10 of the Credit Agreement were revised and additional financial covenants related to minimum EBITDA and liquidity requirements were added. The foregoing description does not purport to be complete and is qualified in its entirety by reference to the text of the Fifth Amendment, which is referenced herein as Exhibit 10.3.e to this report and is incorporated herein by reference.

On March 26, 2007, the Company entered into the Sixth Amendment to Credit Agreement, dated as of March 26, 2007 (the Sixth Amendment), with MagnaChip Semiconductor S.A. and MagnaChip Semiconductor Finance Company, as borrowers, the Subsidiary Guarantors party thereto, the Lenders party thereto, and the Agent. Under the Sixth Amendment, among other things, the existing financial covenants set forth in Section 6.10 of the Credit Agreement were revised to provide that authorized but unspent capital expenditures in a calendar quarter during 2007 carry over to increase the authorized limit on capital expenditures in successive quarters.

**Interest Rate Swap**

Effective June 27, 2005, the Company entered into an interest rate swap agreement (the Swap) that converted the variable interest rate based on the 3-month London Inter-bank Offering Rate (LIBOR) plus 3.25% to fixed interest rate on the Company's Floating Rate Second Priority Senior Secured Notes (the Notes). This Swap will be in effect until 15 June, 2008.

The Swap qualifies as a cash flow hedge under SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities*, as amended. 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. Under this methodology, the actual swap was effective when compared to the hypothetical hedge.

Changes in fair value of the Swap are recorded under other comprehensive income in the accompanying condensed consolidated financial statements. The Company recorded a decrease in the fair value of \$193 thousand and an increase in the fair value of \$4,534 thousand for the years ended December 31, 2006 and 2005, respectively. In addition, the Company recognized interest income of \$2,944 thousand and interest expense of \$550 thousand for the years ended December 31, 2006 and 2005, respectively, which represents the differences between fixed and variable rates.

**Table of Contents****MagnaChip Semiconductor LLC and Subsidiaries****Notes to Consolidated Financial Statements (Continued)****(Tabular dollars in thousands, except unit data)****10. Accrued Severance Benefits**

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

	Year ended December 31		Three months ended December 31, 2004	Nine months ended September 30, 2004 (Predecessor Company)
	2006	2005 (Successor Company)	2004	
Beginning balance	\$ 56,967	\$ 52,925	\$ 47,082	\$ 40,015
Provisions	11,497	16,583	3,397	15,352
Transferred from acquired company		196		
Severance payments	(8,589)	(13,831)	(2,898)	(6,837)
Effect of foreign currency translation	4,767	1,094	5,344	1,473
	64,642	56,967	52,925	50,003
Less: Cumulative contributions to the National Pension Fund	(867)	(900)	(1,234)	(1,304)
Group severance insurance plan	(939)	(943)	(977)	(1,202)
	\$ 62,836	\$ 55,124	\$ 50,714	\$ 47,497

The severance benefits are funded approximately 2.79%, 3.24% and 4.18% as of December 31, 2006, 2005 and 2004, respectively, through severance insurance deposits for the payment of severance benefits, and the account is deducted from accrued severance benefits. In addition, the Company expects to pay the following future benefits to its employees upon their normal retirement ages:

	Severance benefit
2007 2008	\$
2009	70
2010	215
2011	76
2012 2016	1,511

The above amounts were determined based on the 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 employees that will cease working with the Company before their normal retirement ages.

**11. Redeemable Convertible Preferred Unit**

The Company issued 49,727 units as Series A redeemable convertible preferred unit (the Series A ) and 447,420 units as Series B redeemable convertible preferred unit (the Series B ) on September 23, 2004 and additionally issued 364 units of Series A and 3,272 units of Series B on November 30, 2004, respectively. All of Series A were redeemed by cash on December 27, 2004 and a portion of the Series B were redeemed by cash on December 15, 2004 and December 27, 2004.



**Table of Contents****MagnaChip Semiconductor LLC and Subsidiaries****Notes to Consolidated Financial Statements (Continued)****(Tabular dollars in thousands, except unit data)**

Changes in Series B for the years ended December 31, 2006 and 2005 and for the three months ended December 31, 2004 are as follows:

	Year ended December 31				Three months ended	
	2006		2005		December 31, 2004	
	Units	Amount	Units	Amount	Units	Amount
<b>Series A</b>						
Beginning of period		\$		\$	49,727	\$ 49,727
Issuance					364	364
Redemption					(50,091)	(51,907)
Accrual of preferred dividends						1,816
End of period		\$		\$		\$
<b>Series B</b>						
Beginning of period	93,997	\$ 106,462	93,997	\$ 96,534	447,420	\$ 447,420
Issuance					3,272	3,272
Redemption					(356,695)	(365,770)
Accrual of preferred dividends		10,912		9,928		11,612
End of period	93,997	\$ 117,374	93,997	\$ 106,462	93,997	\$ 96,534

The Series B were issued to the original purchasers of the Company in 2004. Holders of Series B receive dividends which are cumulative, whether or not earned or declared by the board of directors. The cumulative cash dividends accrue at the rate of 10% per unit per annum on the Series B original issue price, compounded semi-annually.

**Conversion**

The outstanding Series B units are convertible, in whole or in part, into common equity interests upon or concurrently with the first public offering of the common equity interests of the Company at the Company's option or the holder's option based on a formula, represented by the conversion ratio. The conversion ratio for the Series B units is an amount equal to the original issue price per unit plus an amount per unit equal to full cumulative dividends accrued and unpaid to the date of the consummation of the first public offering, divided by the per common equity interest price to the public in the Company's first public offering of equity securities.

**Dividends**

Holders of Series B receive dividends which are cumulative, whether or not earned or declared by the board of directors. The cumulative cash dividends accrue at the rate of 10% per unit per annum on the Series B original issue price, compounded semi-annually. Such dividends are payable in semi-annual installments in arrears commencing March 15, 2005.

**Liquidation**

In the event of liquidation, the holders of Series B are entitled to receive, out of the assets of the Company legally available for distribution to its members, whether from capital, surplus or earnings, an amount equal to the Series B original issue price in cash per unit plus an amount equal to

Edgar Filing: MAGNACHIP SEMICONDUCTOR LLC - Form 10-K

full cumulative dividends accrued and unpaid thereon to the date of final distribution, and no more. If the net assets of the Company are insufficient to



**Table of Contents**

**MagnaChip Semiconductor LLC and Subsidiaries**

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

**(Tabular dollars in thousands, except unit data)**

pay the holders of all outstanding Series B and of any units ranking on a parity with the Series B, the full amounts to which they respectively shall be entitled, such assets, or the proceeds thereof, shall be distributed ratably among the holders of the Series B and any units ranking on a parity with the Series B in accordance with the amounts which would be payable on such distribution if the amount to which the holders of the Series B and any units ranking on a parity with the Series B are entitled were paid in full.

***Voting***

As provided in Company Operating Agreement, the holders of Series B shall not be entitled to vote on any matter submitted to a vote of the Members, and not be entitled to notice of any meeting of Members.

***Redemption***

If any outstanding Series B remain outstanding on the 14<sup>th</sup> anniversary after issuance of the Series B, then the holders of a majority of the then outstanding Series B shall have the right to elect to have the Company redeem all outstanding Series B from funds legally available, at a price per unit equal to \$1,000 plus an amount per unit equal to full cumulative dividends accrued and unpaid thereon to the redemption date.

Also the Series B may be redeemed from funds legally available, in whole or in part, at the election of the Company, expressed by resolution of the board of directors, at any time and from time to time at a price of \$1,000 per unit plus any cumulative dividends accrued and unpaid.

**12. Warrant**

In connection with the Original Acquisition, the Company issued a warrant, which is recorded as additional paid in capital, to Hynix, which enables Hynix to purchase 5,079,254 common units of the Company. The value of each warrant to purchase one common unit is \$0.414, which was estimated using the Black-Scholes option pricing model using the following assumptions: fair value of \$1.00 per unit; exercise price of \$1.00 per unit; risk free rate of interest of 2.50%; volatility of 86%; dividend rate of 0%; and term of 2 years. This warrant expired unexercised in accordance with its terms on October 6, 2006.

**13. Equity Incentive Plans**

The Company adopted two equity incentive plans effective October 6, 2004 and March 21, 2005, respectively, which are administered by the Compensation Committee designated by the board of directors. Employees, consultants and non-employee directors are eligible for the grant of options to purchase the Company's common units or restricted common units subject to terms and conditions determined by the Committee. The term of options in no event exceed ten years from the date of grant. As of December 31, 2006, an aggregate maximum of 7,890,864 common units were authorized and reserved for all future and outstanding grants of options.

Unit options are generally granted with exercise prices of no less than the fair market value of the Company's common units on the grant date. Generally, options vest and become exercisable in periodic installments, with 25% of the options vesting on the first anniversary of the grant date and 6.25% of options vesting on the last day of each calendar quarter thereafter. In most cases, the requisite service period, or the period during which a grantee is required to provide service in exchange for option grants, coincides with the vesting period.

**Table of Contents****MagnaChip Semiconductor LLC and Subsidiaries****Notes to Consolidated Financial Statements (Continued)****(Tabular dollars in thousands, except unit data)**

Restricted units are issued upon the exercise of certain options to purchase restricted common units. Restricted units issued are subject to restrictions which generally lapse in installments over a four-year period.

The following summarizes unit option and restricted unit activities for the year ended December 31, 2006. At the date of grant, all options had an exercise price at or above the fair value of common units:

	Number of restricted stock	Number of options	Weighted average exercise price (in US dollars)	Weighted average remaining contractual life
Outstanding at January 1, 2006	1,726,062	3,780,643	1.6	
Granted		2,107,500	1.6	
Exercised		46,063	1.9	
Forfeited / Repurchased	409,348	772,552	1.5	
Released from restriction	517,936		n/a	
Outstanding at December 31, 2006	798,778	5,069,528	1.6	8.6 years
Exercisable at December 31, 2006	N/A	1,588,000	1.6	7.9 years

Total unit option related compensation expense pursuant to SFAS No. 123(R) for the year ended December 31, 2006 was \$243 thousand. As of December 31, 2006, there was \$358 thousand of total unrecognized compensation cost related to unvested options, which is expected to be recognized over a weighted average future period of 1.2 years. Total fair value of options vested for the year ended December 31, 2006 is \$167 thousand.

The Company utilizes the Black-Scholes option-pricing model to measure the fair value of each option grant. The following summarizes the grant-date fair value of options granted during the specified periods and assumptions used in the Black-Scholes option-pricing model on a weighted average basis:

	Year ended December 31		Three months ended December 31, 2004	Nine months ended September 30, 2004 (Predecessor Company)
	2006	2005 (Successor Company)		
Grant-date fair value of option (in US dollars)	\$ 0.22	\$ 0.22	\$ 0.38	\$ 0.38
Expected term	2.3 Years	2.1 Years	2.2 Years	3.5 Years
Risk-free interest rate	4.9%	3.3%	2.6%	3.75%
Expected volatility	46.7%	57.8%	64.8%	144.5%
Expected dividends				

The total cash received from employees as a result of option exercises was \$88 thousand, \$112 thousand and \$2,456 thousand for the years ended December 31, 2006 and 2005 and for the three months ended December 31, 2004, respectively. None of the options exercised during these periods had any intrinsic value.



**Table of Contents****MagnaChip Semiconductor LLC and Subsidiaries****Notes to Consolidated Financial Statements (Continued)**

(Tabular dollars in thousands, except unit data)

The following presents pro forma net loss and per unit data as if the fair value based method had been applied to account for the unit-based compensation for the year ended December 31, 2005, three months ended December 31, 2004 and nine months ended September 30, 2004:

	Year ended	Three months ended	Nine months ended
	December 31,	December 31,	September 30,
	2005 (Successor Company)	2004	2004 (Predecessor Company)
Net income (loss), as reported	\$ (100,898)	\$ (5,825)	\$ 43,237
Dividends accrued on preferred units	9,928	13,428	
Net income (loss) attributable to common units (owner)	(110,826)	(19,253)	43,237
Add: unit(stock)-based compensation expense included in reported net income (loss), net of tax			3,324
Deduct: unit(stock)-based compensation expense determined under the fair value method, net of tax	(411)	(995)	(5,614)
Pro forma net income (loss)	\$ (111,237)	\$ (20,248)	\$ 40,947
As reported loss per unit	\$ (2.10)	\$ (0.38)	
Pro forma loss per unit	\$ (2.10)	\$ (0.40)	

The pro forma presentation for the nine months ended September 30, 2004 is based on stock options granted by Hynix before the Original Acquisition. However, none of these options were transferred as part of the Original Acquisition.

**14. Restructuring and Impairment Charges*****2006 Restructuring and Impairment Charges***

During the year ended December 31, 2006, the Company recorded restructuring and impairment charges totaling \$94,266 thousand, which included \$92,858 thousand of impairment charges under SFAS 144, *Accounting for the Impairment or Disposal of Long-lived assets* and \$1,408 thousand of restructuring charges under SFAS 146, *Accounting for Costs Associated with Exit or Disposal Activities*.

The impairment charges of \$92,540 thousand recorded during 2006 related to certain fixed assets and technology and customer-based intangible assets (the asset group) comprising our Imaging Solution business. At the end of fiscal year 2005, the capacity utilization of the Fab was under the level that we believe to be normal. This was primarily due to a transition in product mix coupled with a seasonal decrease in market demand, which was deemed to be temporary and recoverable. However, in 2006, our management determined, based on revised forecasting, that the projected demand for certain of its products was significantly less than previously forecasted and that this decline was not temporary or seasonal. Therefore, we assessed whether there had been a material impairment on the asset group pursuant to SFAS 144 and, based on the assessment, recorded impairment charges.

## Edgar Filing: MAGNACHIP SEMICONDUCTOR LLC - Form 10-K

The impairment charge was measured as the excess of the carrying value of the asset group over its fair value. The fair value of the asset group was estimated using a present value technique, where expected future cash flows from the use and eventual disposal of the asset group were discounted by an interest rate commensurate with the risk of the cash flows. The net book value of the asset group before the impairment charges was approximately \$185,985 thousand.

**Table of Contents****MagnaChip Semiconductor LLC and Subsidiaries****Notes to Consolidated Financial Statements (Continued)****(Tabular dollars in thousands, except unit data)**

In addition, the Company recorded impairment charges in the amount of \$318 thousand related to the disposition of certain assets previously designated as assets held-for-sale and \$1,408 thousand of restructuring charges in connection with the termination of certain of our management and employees.

**2005 Restructuring and Impairment Charges**

During the year ended December 31, 2005, the Company recorded \$36,234 thousand of restructuring and impairment charges which included \$33,576 thousand of asset impairments and \$2,658 thousand of restructuring.

In an effort to focus on its major business segments - Display Solutions, Imaging Solutions and Semiconductor Manufacturing Services, the Company made a strategic decision to divest its Application Processor business. Based on such decision, the Company recognized impairment charges on certain tangible and intangible assets related to the divestiture. The impairment charge was measured as the excess of the carrying value of the asset group over the fair value measured at the selling price of the assets.

In addition, the Company took a total of \$2,658 thousand of restructuring charges which included early retirement costs and other related costs associated with the sale of Application Processor business.

**15. Income Tax Expenses**

The Company's income tax expenses are composed of domestic and foreign income taxes depending on the relevant tax jurisdiction. For the Predecessor Company Domestic refers to the income before taxes, current income taxes and deferred income taxes generated or incurred in Korea. For the Successor Company, however, it refers to the income before taxes, current income taxes and deferred income taxes generated or incurred in the US, in which the ultimate parent of the Company resides.

The components of income tax expense are as follows:

	Year ended December 31		Three months ended	Nine months ended
	2006	2005	December 31, 2004	September 30, 2004
	(Successor Company)			(Predecessor Company)
Income before income taxes				
Domestic	\$ 5,862	\$ (3,528)	\$ 3,136	\$ 48,660
Foreign	(225,914)	(95,554)	(2,236)	(2,595)
	\$ (220,052)	\$ (99,082)	\$ 900	\$ 46,065
Current income taxes expense (benefits)				
Domestic	\$ (17)	\$ (9)	\$ 266	\$
Foreign	7,226	14,041	6,459	2,828
	7,209	14,032	6,725	2,828
Deferred income taxes expense (benefits)				

Edgar Filing: MAGNACHIP SEMICONDUCTOR LLC - Form 10-K

Domestic				
Foreign	2,049	(12,216)		
	2,049	(12,216)		
Total income tax expenses	\$ 9,258	\$ 1,816	\$ 6,725	\$ 2,828

**Table of Contents****MagnaChip Semiconductor LLC and Subsidiaries****Notes to Consolidated Financial Statements (Continued)****(Tabular dollars in thousands, except unit data)**

The ultimate parent of the Company is a limited liability company, a non-taxable entity for US tax purposes and thus the statutory income tax rate shall be zero. A substantial portion of the income tax expenses above is incurred from MagnaChip Korea, which is the principal operating entity within the Company. The statutory income tax rate of MagnaChip Korea, including tax surcharges, applicable to the Company was approximately 27.5% in 2006 and 2005, which was reduced from 29.7% in 2004 in accordance with the Corporate Income Tax Law as amended on December 31, 2003. MagnaChip Korea is eligible for a tax exemption in which its corporate income tax is reduced by 50% from 2004 to 2006 and 30% from 2007 to 2008.

The income tax rate used to calculate the tax provision by the Predecessor Company was the statutory income tax rate of Korea, which was 29.7%. For the Successor Company, the statutory income tax rate is zero as its ultimate parent is a non-taxable US entity. The provision for domestic and foreign income taxes incurred is different from the amount calculated by applying the statutory tax rate to the net income before income taxes. The significant items causing this difference are as follows:

	Year ended December 31		Three months ended December 31, 2004	Nine months ended September 30, 2004
	2006	2005 (Successor Company)		2004 (Predecessor Company)
Provision computed at statutory rate	\$	\$	\$	\$ 13,682
Permanent differences	1,850	(521)	(161)	532
Change in statutory tax rate	13,035	1,256	5,125	(818)
Adjustment for overseas tax rate	(58,493)	(27,745)	(1,492)	(181)
Exemption			(5,447)	
Change in valuation allowance	52,866	28,826	8,700	(10,387)
Total statutory income taxes	\$ 9,258	\$ 1,816	\$ 6,725	\$ 2,828



**Table of Contents****MagnaChip Semiconductor LLC and Subsidiaries****Notes to Consolidated Financial Statements (Continued)**

(Tabular dollars in thousands, except unit data)

A summary of the composition of net deferred income tax assets (liabilities) at December 31, 2006 and 2005 are as follows:

	December 31, 2006	December 31, 2005
<b>Deferred tax assets</b>		
Inventories	\$ 7,587	\$ 4,949
Accrued expenses	1,030	1,251
Product warranties	321	687
Other reserves	575	819
Severance benefits	7,802	4,679
Property, plant and equipments	34,712	33,749
NOL carry-forwards	46,537	9,990
Tax credit	15,752	10,011
Royalty income	10,163	11,520
Others	815	1,675
Total deferred tax assets	125,294	79,330
Less: valuation allowance	(100,016)	(42,695)
	25,278	36,635
<b>Deferred tax liabilities</b>		
Acquisition consideration		1
Foreign currency gain		456
Debt issuance cost	63	35
Intangible assets	15,048	23,927
Others		
Total deferred tax liabilities	15,111	24,419
Net deferred tax asset (liabilities)	\$ 10,167	\$ 12,216

Changes in valuation allowance for deferred tax assets for the years ended December 31, 2006 and 2005 are as follows:

	December 31, 2006	December 31, 2005
Beginning balance	\$ 42,695	\$ 8,700
Transferred from acquired company		4,179
Charge to expenses	52,866	28,826
Effect on foreign currency translation	4,455	990
Ending balance	\$ 100,016	\$ 42,695

Deferred income tax assets are recognized only to the extent that realization of the related tax benefit is more likely than not. Realization of the future tax benefits related to the deferred tax assets is dependent on many factors, including the Company's ability to generate taxable income within the period during which the temporary differences reverse, the outlook for the economic environment in which the Company operates, and the overall future industry outlook. Based on the Company's historical accounting and tax losses, management determined that it was more likely than not, that the Company would realize benefits related to its deferred tax assets in the amount of \$10,167 thousand as of December 31, 2006 and \$12,216 thousand as of December 31, 2005. Accordingly, the Company recorded a valuation allowance of \$100,016 thousand and \$42,695 thousand on its net deferred tax assets for 2006 and 2005, respectively.

**Table of Contents****MagnaChip Semiconductor LLC and Subsidiaries****Notes to Consolidated Financial Statements (Continued)**

(Tabular dollars in thousands, except unit data)

At December 31, 2006, the Company had approximately \$209,881 thousand of net operating loss carry-forwards available to offset future taxable income, which expires in varying amounts starting from 2007 to 2011. A majority of such net operating loss is related to MagnaChip Korea. The Company also has Korean and Dutch tax credit carry-forwards of approximately \$9,319 thousand and \$7,544 thousand, respectively. The Korean tax credits expire at various dates starting from 2010 to 2011, and the Dutch credits are carried forward to be used for an indefinite period of time.

**16. Geographic and Segment Information**

The following sets forth information relating to the reportable segments:

	Year ended December 31		Three months ended December 31,	Nine months ended September 30,
	2006	2005	2004	2004
	(Successor Company)			(Predecessor Company)
<b>Net Sales</b>				
Display Solutions	\$ 273,656	\$ 326,027	\$ 60,352	\$ 198,823
Imaging Solutions	60,479	163,326	58,069	142,050
Semiconductor Manufacturing Services	342,416	345,437	88,295	270,240
All other	67,802	102,866	36,866	230,475
Total segment net sales	\$ 744,353	\$ 937,656	\$ 243,582	\$ 841,588
<b>Gross Profit</b>				
Display Solutions	\$ 35,603	\$ 66,534	\$ 4,566	\$ 30,380
Imaging Solutions	(4,008)	25,423	12,695	56,659
Semiconductor Manufacturing Services	45,712	110,389	19,143	86,301
All other	22,134	6,311	2,717	13,679
Total segment gross profit	\$ 99,441	\$ 208,657	\$ 39,121	\$ 187,019

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

	Year ended December 31		Three months ended December 31,	Nine months ended September 30,
	2006	2005	2004	2004
	(Successor Company)			(Predecessor Company)
Korea	\$ 413,670	\$ 512,366	\$ 127,208	\$ 455,616
Asia Pacific	172,981	251,173	63,094	203,791
Japan	78,321	97,841	38,000	143,190
North America	62,357	56,907	11,677	17,388
Europe	17,024	19,369	3,603	21,603

Edgar Filing: MAGNACHIP SEMICONDUCTOR LLC - Form 10-K

\$ 744,353      \$ 937,656      \$ 243,582      \$ 841,588

Over 99% of the Company's property, plant and equipment are located in Korea as of December 31, 2006.

Net sales from the Company's top ten largest customers accounted for 66%, 63%, 62% and 63%, for the years ended December 31, 2006 and 2005, three months ended December 31, 2004, and nine months ended September 30, 2004, respectively.

**Table of Contents****MagnaChip Semiconductor LLC and Subsidiaries****Notes to Consolidated Financial Statements (Continued)****(Tabular dollars in thousands, except unit data)****17. Commitments and Contingencies*****Operating Agreements with Hynix***

In connection with the Original Acquisition, the Company entered into several definitive agreements with Hynix regarding key materials, campus facilities, research and development equipment and information technology, factory automation, wafer foundry services, and a non-exclusive cross license that provides the Company with access to certain of Hynix's intellectual property for use in the manufacture and sale of non-memory semiconductor products. The Company also agreed to provide certain utilities and infrastructure support services to Hynix. The obligation to provide services under these agreements generally lasts for one to five years from the date of the Original Acquisition. The obligation to provide certain services lasts indefinitely.

Upon the closing of the Original Acquisition, MagnaChip Korea and Hynix also entered into lease agreements under which MagnaChip Korea leases from Hynix (i) certain exclusive-use space plus common- and joint-use space in several buildings, primarily warehouses and utility facilities, in Cheongju, Korea. These leases are generally for an initial term of 20 years plus an indefinite number of renewal terms of 10 years each. Each of the leases is cancelable upon 90 days' notice by the lessee. The Company also leased from Hynix certain exclusive-use plus common- and joint-use land located in Cheongju, Korea. The term of this agreement is indefinite unless otherwise agreed between the both parties, and as long as the buildings remain on the lease site and are owned and used by the Company for permitted uses.

***Operating Leases***

The Company leases land, office building and equipments under various operating lease agreements that expire through 2034. Rental expenses were approximately \$12,008 thousand and \$13,913 thousand for the years ended December 31, 2006 and 2005, \$2,910 thousand for the three-month period ended December 31, 2004 (successor company) and \$2,318 thousand and \$1,556 thousand for the nine-month period ended September 30, 2004 (predecessor company), respectively.

As of December 31, 2006, the minimum aggregate rental payments due under non-cancelable lease contracts are as follows:

2007	\$ 11,934
2008	11,935
2009	11,936
2010	11,937
2011	11,939
	\$ 59,681

***Advisory Agreements***

An advisory agreement was entered into as of October 6, 2004 by and between the Company and advisors including CVC Management LLC (CVC Management), CVC Capital Partners Asia Limited (CVC Capital) and Francisco Partners Management LLC (Francisco Partners). The Company is to pay each of CVC Management and Francisco Partners an annual advisory fee the amount of which shall be the greater of \$1,379,163 per annum or 0.14777% per annum of annual consolidated revenue, and is also to pay CVC Capital an annual advisory fee the amount of which shall be the greater of \$741,673 per annum or 0.07946% per annum of annual consolidated revenue plus reasonable out-of-pocket expenses for an initial term of 10 years, subject to termination by either party upon written notice 90 days prior to the expiration of the initial term or any extension thereof. During the year ended



**Table of Contents****MagnaChip Semiconductor LLC and Subsidiaries****Notes to Consolidated Financial Statements (Continued)****(Tabular dollars in thousands, except unit data)**

December 31, 2005 and the three-month period ended December 31, 2004 (successor company), the Company accrued \$3,545 thousand and \$890 thousand of accrued expenses under these agreements, respectively, which is included in selling, general and administrative expenses in the accompanying consolidated financial statements. During the year ended December 31, 2006, due to lower Company financial performance, the advisors agreed to waive the advisory fee in exchange for an extension of the initial term of the advisory agreements for a period of one year and, therefore, the Company did not accrue any expenses.

***Undrawn line of credit***

The undrawn portion of the new senior secured credit line was \$93,792 thousand, \$82,956 thousand and \$86,295 thousand as of December 31, 2006, 2005 and 2004, respectively.

***Payments of Guarantee***

As of December 31, 2006 and 2005, the Company has provided guarantees for bank loans that employees borrowed to participate in the issuance of new shares of Hynix in 1999. The outstanding balances of guarantees for payments provided by the Company amounted to approximately \$248 thousand and \$304 thousand as of December 31, 2006 and 2005, respectively.

**18. Related Party Transactions**

Funds related to CVC, Francisco Partners and CVC Asia Pacific own 34.1%, 34.1% and 18.3%, respectively, of the common units, and 35.9%, 35.9% and 19.3%, respectively, of the Series B units outstanding at December 31, 2006. Refer to Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters for details of ownership of each party.

Hyundai Display Technology, Hyundai Information Technology and Hyundai ASTEC were all subsidiaries of Hynix. As a result of the Original Acquisition, these companies were all excluded from related parties of the Company.

Transactions between the Company and its related parties are as follows:

	Year ended December 31, 2006	Year ended December 31, 2005 (Successor Company)	Three months ended December 31, 2004	Nine months ended September 30, 2004 (Predecessor Company)
Net sales				
Hynix				\$ 163,760
				\$ 163,760
Purchases				
Hynix				\$ 11,999
Hyundai Information Technology				772
Hyundai ASTEC				9,346
Other related parties				15

				\$	22,132
Advisory Fee					
Citigroup Venture Capital	\$	\$	1,397	\$	351
Francisco Partners			1,397		351
CVC Asia Pacific			751		188
Total	\$	\$	3,545	\$	890



**Table of Contents****MagnaChip Semiconductor LLC and Subsidiaries****Notes to Consolidated Financial Statements (Continued)**

(Tabular dollars in thousands, except unit data)

Loans to employees as of December 31, 2006 and 2005 are as follows:

	December 31, 2006	December 31, 2005
Short-term loans	\$ 54	\$ 61
Long-term loans	434	125
<b>Total</b>	<b>\$ 488</b>	<b>\$ 186</b>

**19. Earnings per Unit**

The following table illustrates the computation of basic and diluted loss per common unit:

	Year ended		Three months ended
	December 31, 2006	December 31, 2005 (Successor Company)	December 31, 2004
Net loss	\$ (229,310)	\$ (100,898)	\$ (5,825)
Dividends to preferred unitholders	(10,912)	(9,928)	(13,428)
<b>Net loss attributable to common units</b>	<b>\$ (240,222)</b>	<b>\$ (110,826)</b>	<b>\$ (19,253)</b>
Weighted-average common units outstanding	52,911,734	52,898,497	50,061,910
<b>Basic and diluted loss per unit</b>	<b>\$ (4.54)</b>	<b>\$ (2.10)</b>	<b>\$ (0.38)</b>

The following outstanding redeemable convertible preferred unit issued, stock-options granted and warrants issued were excluded from the computation of diluted loss per unit as they would have an anti-dilutive effects on the calculation:

	December 31, 2006	December 31, 2005 (Successor Company)	December 31, 2004
Redeemable convertible preferred units	93,997	93,997	93,997
Options	5,069,528	3,780,643	1,146,178
Warrants		5,079,254	5,079,254

**20. Condensed Consolidating Financial Statements**

The senior secured credit facility and Second Priority Senior Secured Notes are each fully and unconditionally guaranteed by the Company and all of its subsidiaries, except for MagnaChip Semiconductor (Shanghai) Company Limited. The Senior Subordinated Notes are fully and unconditionally guaranteed by the Company and all of its subsidiaries, except for MagnaChip Semiconductor, Ltd. (Korea) and MagnaChip Semiconductor (Shanghai) Company Limited. The Senior Subordinated Notes are structurally subordinated to the creditors of our principal

## Edgar Filing: MAGNACHIP SEMICONDUCTOR LLC - Form 10-K

manufacturing subsidiary, MagnaChip Semiconductor, Ltd. (Korea), which accounts for a majority of our net sales and substantially all of our assets.

Below are condensed consolidating balance sheets as of December 31, 2006 and 2005, condensed consolidating statements of operations and of cash flows for the years ended December 31, 2006 and 2005 and for the three months ended December 31, 2004 of those entities that guarantee the Senior Subordinated Notes, those that do not, MagnaChip Semiconductor LLC, and the co-issuers.

**Table of Contents****MagnaChip Semiconductor LLC and Subsidiaries****Notes to Consolidated Financial Statements (Continued)**

(Tabular dollars in thousands, except unit data)

**Condensed Consolidating Statement of Operations**

For the year ended December 31, 2006

	<b>MagnaChip Semiconductor LLC (Parent)</b>	<b>Co-Issuers</b>	<b>Non- Guarantors</b>	<b>Guarantors</b>	<b>Eliminations</b>	<b>Consolidated</b>
Net sales	\$	\$	\$ 718,126	\$ 352,152	\$ (325,926)	\$ 744,352
Cost of sales			636,349	313,699	(305,137)	644,911
Gross profit			81,777	38,453	(20,789)	99,441
Selling, general and administrative expenses	104	947	75,949	10,842	(165)	87,677
Research and development expenses			135,361	17,828	(21,937)	131,252
Restructuring and impairment charge			94,041	225		94,266
Operating income (loss)	(104)	(947)	(223,574)	9,558	1,313	(213,754)
Other income (expenses)	3	9,755	38	(16,094)		(6,298)
Income (loss) before income taxes, equity in loss of related equity investment	(101)	8,808	(223,536)	(6,536)	1,313	(220,052)
Income tax expense (benefit)		170	156	8,932		9,258
Income (loss) before equity in loss of related Investment	(101)	8,638	(223,692)	(15,468)	1,313	(229,310)
Loss of related investment	(229,209)	(243,820)		(224,982)	698,011	
Net loss	\$ (229,310)	\$ (235,182)	\$ (223,692)	\$ (240,450)	\$ 699,324	\$ (229,310)
Dividends accrued on preferred units	10,912					10,912
Net loss attributable to common units	\$ (240,222)	\$ (235,182)	\$ (223,692)	\$ (240,450)	\$ 699,324	\$ (240,222)

**Table of Contents****MagnaChip Semiconductor LLC and Subsidiaries****Notes to Consolidated Financial Statements (Continued)**

(Tabular dollars in thousands, except unit data)

**Condensed Consolidating Statement of Operations**

For the year ended December 31, 2005

	<b>MagnaChip Semiconductor LLC (Parent)</b>	<b>Co-Issuers</b>	<b>Non- Guarantors</b>	<b>Guarantors</b>	<b>Eliminations</b>	<b>Consolidated</b>
Net sales	\$	\$	\$ 914,445	\$ 431,339	\$ (408,128)	\$ 937,656
Cost of sales			723,844	406,669	(401,514)	728,999
Gross profit			190,601	24,670	(6,614)	208,657
Selling, general and administrative expenses	539	1,876	107,326	15,501	(2,031)	123,211
Research and development expenses			101,318	11,018	(4,746)	107,590
Restructuring and impairment charge			36,234			36,234
Operating income (loss)	(539)	(1,876)	(54,277)	(1,849)	163	(58,378)
Other income (expenses)	5	(13,731)	(35,577)	8,599		(40,704)
Income (loss) before income taxes, equity in loss of related equity investment	(534)	(15,607)	(89,854)	6,750	163	(99,082)
Income tax expense (benefit)		163		1,653		1,816
Income (loss) before equity in loss of related Investment	(534)	(15,770)	(89,854)	5,097	163	(100,898)
Loss of related investment	(100,364)	(78,445)		(86,985)	265,794	
Net loss	\$ (100,898)	\$ (94,215)	\$ (89,854)	\$ (81,888)	\$ 265,957	\$ (100,898)
Dividends accrued on preferred units	9,928					9,928
Net loss attributable to common units	\$ (110,826)	\$ (94,215)	\$ (89,854)	\$ (81,888)	\$ 265,957	\$ (110,826)

**Table of Contents****MagnaChip Semiconductor LLC and Subsidiaries****Notes to Consolidated Financial Statements (Continued)**

(Tabular dollars in thousands, except unit data)

**Condensed Consolidating Statement of Operations****For the three months ended December 31, 2004**

	<b>MagnaChip Semiconductor LLC</b>		<b>Non- Guarantors</b>		<b>Guarantors</b>	<b>Eliminations</b>	<b>Consolidated</b>
	<b>(Parent)</b>	<b>Co-Issuers</b>	<b>Guarantors</b>	<b>Guarantors</b>			
Net sales	\$	\$	\$ 241,149	\$ 116,639	\$ (114,206)	\$ 243,582	
Cost of sales			203,089	114,063	(112,691)	204,461	
<b>Gross profit</b>			<b>38,060</b>	<b>2,576</b>	<b>(1,515)</b>	<b>39,121</b>	
Selling, general and administrative expenses	2	20	27,174	2,588		29,784	
Research and development expenses			22,058			22,058	
Operating income (loss)	(2)	(20)	(11,172)	(12)	(1,515)	(12,721)	
Other income (expenses)	2,588	11,908	7,857	(8,732)		13,621	
Income (loss) before income taxes, equity in earnings (loss) of related equity investment	2,586	11,888	(3,315)	(8,744)	(1,515)	900	
Income tax expense			6,105	620		6,725	
Income (loss) before equity in earnings (loss) of related Investment	2,586	11,888	(9,420)	(9,364)	(1,515)	(5,825)	
Earnings (loss) of related investment	(8,411)	(20,581)		(9,420)	38,412		
Net income (loss)	\$ (5,825)	\$ (8,693)	\$ (9,420)	\$ (18,784)	\$ 36,897	\$ (5,825)	
Dividends accrued on preferred units	13,428					13,428	
Net income (loss) attributable to common units	\$ (19,253)	\$ (8,693)	\$ (9,420)	\$ (18,784)	\$ 36,897	\$ (19,253)	

**Table of Contents****MagnaChip Semiconductor LLC and Subsidiaries****Notes to Consolidated Financial Statements (Continued)**

(Tabular dollars in thousands, except unit data)

**Condensed Consolidating Balance Sheet****December 31, 2006**

	<b>MagnaChip Semiconductor LLC (Parent)</b>	<b>Co-Issuers</b>	<b>Non- Guarantors</b>	<b>Guarantors</b>	<b>Eliminations</b>	<b>Consolidated</b>
<b>Assets</b>						
Current assets						
Cash and cash equivalents	\$ 321	\$ 892	\$ 72,608	\$ 15,352	\$	\$ 89,173
Restricted cash						
Accounts receivable, net			86,488	34,971	(44,794)	76,665
Inventories, net			55,676	2,208	(38)	57,846
Other receivables		718	5,244	28,133	(27,341)	6,754
Other current assets	58	15,862	12,843	6,692	(21,829)	13,626
<b>Total current assets</b>	<b>379</b>	<b>17,472</b>	<b>232,859</b>	<b>87,356</b>	<b>(94,002)</b>	<b>244,064</b>
Property, plant and equipment, net						
Intangible assets, net			334,809	1,470		336,279
Investments in subsidiaries	(167,545)	(246,126)	117,101	22,628		139,729
Long-term intercompany loans		791,648		(77,489)	491,160	
Other non-current assets		21,349	41,972	9,702	(23,042)	49,981
<b>Total assets</b>	<b>\$ (167,166)</b>	<b>\$ 584,343</b>	<b>\$ 726,741</b>	<b>\$ 677,654</b>	<b>\$ (1,051,519)</b>	<b>\$ 770,053</b>
<b>Liabilities and Unitholders equity</b>						
Current liabilities						
Accounts payable	\$	\$	\$ 67,002	\$ 40,191	\$ (44,794)	\$ 62,399
Other accounts payable		6	51,803	7,955	(27,341)	32,423
Accrued expenses	1	3,135	22,040	17,078	(18,607)	23,647
Other current liabilities		333	1,844	4,025	(3,222)	2,980
<b>Total current liabilities</b>	<b>1</b>	<b>3,474</b>	<b>142,689</b>	<b>69,249</b>	<b>(93,964)</b>	<b>121,449</b>
Long-term borrowings						
Accrued severance benefits, net		750,000	621,000	804,635	(1,425,635)	750,000
Other non-current liabilities			62,550	286	(23,042)	62,836
<b>Total liabilities</b>	<b>1</b>	<b>753,474</b>	<b>827,430</b>	<b>898,956</b>	<b>(1,542,641)</b>	<b>937,220</b>
Commitments and contingencies						
Series A redeemable convertible preferred units						
Series B redeemable convertible preferred unites	117,374					117,374

Edgar Filing: MAGNACHIP SEMICONDUCTOR LLC - Form 10-K

Total redeemable convertible preferred units	117,374					117,374
<b>Unitholders' equity</b>						
Common units	52,721	136,229	39,005	55,778	(231,012)	52,721
Additional paid-in capital	2,451	1,401	155,415	108,239	(265,055)	2,451
Accumulated deficit	(370,314)	(338,112)	(323,358)	(412,488)	1,073,958	(370,314)
Accumulated other comprehensive income	30,601	31,351	28,249	27,169	(86,769)	30,601
Total unitholders' equity	(284,541)	(169,131)	(100,689)	(221,302)	491,122	(284,541)
<b>Total liabilities, redeemable convertible preferred units and unitholders' equity</b>						
	\$ (167,166)	\$ 584,343	\$ 726,741	\$ 677,654	\$ (1,051,519)	\$ 770,053

**Table of Contents****MagnaChip Semiconductor LLC and Subsidiaries****Notes to Consolidated Financial Statements (Continued)**

(Tabular dollars in thousands, except unit data)

**Condensed Consolidating Balance Sheet**

December 31, 2005

	MagnaChip Semiconductor LLC (Parent)	Co-Issuers	Non- Guarantors	Guarantors	Eliminations	Consolidated
<b>Assets</b>						
Current assets						
Cash and cash equivalents	\$ 209	\$ 841	\$ 63,435	\$ 22,089	\$	\$ 86,574
Restricted cash			2,837			2,837
Accounts receivable, net			131,669	55,057	(74,673)	112,053
Inventories, net			82,348	7,638	(1,309)	88,677
Other receivables	35,013	718	7,792	20,097	(54,119)	9,501
Other current assets		22,382	9,987	6,063	(28,284)	10,148
<b>Total current assets</b>	<b>35,222</b>	<b>23,941</b>	<b>298,068</b>	<b>110,944</b>	<b>(158,385)</b>	<b>309,790</b>
Property, plant and equipment, net						
			484,019	1,058		485,077
Intangible assets, net						
			165,369	26,020		191,389
Investments in subsidiaries	25,756	(38,942)		144,131	(130,945)	
Long-term intercompany loans		774,199		621,311	(1,395,510)	
Other non-current assets		24,153	45,370	11,131	(26,263)	54,391
<b>Total assets</b>	<b>\$ 60,978</b>	<b>\$ 783,351</b>	<b>\$ 992,826</b>	<b>\$ 914,595</b>	<b>\$ (1,711,103)</b>	<b>\$ 1,040,647</b>
<b>Liabilities and Unitholders equity</b>						
Current liabilities						
Accounts payable	\$	\$	\$ 94,581	\$ 74,003	\$ (74,673)	\$ 93,911
Other accounts payable	1,000	440	68,703	19,344	(54,119)	35,368
Accrued expenses		3,139	24,560	26,331	(25,062)	28,968
Other current liabilities		162	3,746	9,416	(3,222)	10,102
<b>Total current liabilities</b>	<b>1,000</b>	<b>3,741</b>	<b>191,590</b>	<b>129,094</b>	<b>(157,076)</b>	<b>168,349</b>
Long-term borrowings						
		750,000	621,311	774,199	(1,395,510)	750,000
Accrued severance benefits, net			54,854	270		55,124
Other non-current liabilities			5,272	28,187	(26,263)	7,196
<b>Total liabilities</b>	<b>1,000</b>	<b>753,741</b>	<b>873,027</b>	<b>931,750</b>	<b>(1,578,849)</b>	<b>980,669</b>
Commitments and contingencies						
Series A redeemable convertible preferred units						
Series B redeemable convertible preferred unites	106,462					106,462



Edgar Filing: MAGNACHIP SEMICONDUCTOR LLC - Form 10-K

Total redeemable convertible preferred units		106,462				106,462
<b>Unitholders' equity</b>						
Common units	53,092	102,986	39,005	58,364	(200,355)	53,092
Additional paid-in capital	2,169	1,027	155,212	71,989	(228,228)	2,169
Accumulated deficit	(130,092)	(102,930)	(99,666)	(172,038)	374,634	(130,092)
Accumulated other comprehensive income	28,347	28,527	25,248	24,530	(78,305)	28,347
Total unitholders' equity	(46,484)	29,610	119,799	(17,155)	(132,254)	(46,484)
<b>Total liabilities, redeemable convertible preferred units and unitholders' equity</b>						
	\$ 60,978	\$ 783,351	\$ 992,826	\$ 914,595	\$ (1,711,103)	\$ 1,040,647

**Table of Contents****MagnaChip Semiconductor LLC and Subsidiaries****Notes to Consolidated Financial Statements (Continued)**

(Tabular dollars in thousands, except unit data)

**Condensed Consolidating Statement of Cash Flows**

For the year ended December 31, 2006

	<b>MagnaChip Semiconductor LLC (Parent)</b>	<b>Co-Issuers</b>	<b>Non- Guarantors</b>	<b>Guarantors</b>	<b>Eliminations</b>	<b>Consolidated</b>
<b>Cash flows from operating activities</b>						
Net income (loss)	\$ (229,310)	\$ (235,182)	\$ (223,692)	\$ (240,450)	\$ 699,324	\$ (229,310)
Adjustments to reconcile net income (loss) to net cash provided by operating activities						
Depreciation and amortization			184,430	4,130		188,560
Provision for severance benefits			11,478	19		11,497
Amortization of debt issuance costs		2,791	910			3,701
Loss (gain) on foreign currency translation, net		(17,449)	(54,564)	17,825		(54,188)
Loss (gain) on disposal of property, plant and equipment, net			1,362	128		1,490
Impairment charges			92,858			92,858
Unit/stock-based compensation			203	40		243
Loss (earnings) of related investment	229,209	243,820		224,982	(698,011)	
Other			2,838	185		3,023
<b>Changes in operating assets and liabilities</b>						
Accounts receivable			53,839	20,131	(29,879)	44,091
Inventories			32,884	5,450	(1,270)	37,064
Other receivables	1,602		3,145	9,716	(11,283)	3,180
Deferred tax assets				1,954		1,954
Accounts payable			(34,451)	(33,851)	29,879	(38,423)
Other accounts payable	(1,000)	(435)	(29,954)	4,209	11,283	(15,897)
Accrued expenses		(5)	(4,495)	(9,408)	6,455	(7,453)
Other current assets	(57)	6,521	9,752	(1,475)	(9,678)	5,063
Other current liabilities		170	(2,320)	(8,402)	3,223	(7,329)
Payment of severance benefits			(8,589)			(8,589)
Other		(180)	(467)	(418)		(1,065)
Net cash provided by (used in) operating activities	444	51	35,167	(5,235)	43	30,470
<b>Cash flows from investing activities</b>						
Purchase of plant, property and equipment			(38,194)	(1,080)	78	(39,196)
Payment for intellectual property registration			(2,085)	(118)		(2,203)
Proceeds from disposal of plant, property and equipment			3,723	6	(78)	3,651
Proceeds from disposal of intangible assets			2,819			2,819
Decrease in restricted cash			3,002			3,002
Other			(1,485)	27		(1,458)
Net cash provided by (used in) investing activities			(32,220)	(1,165)		(33,385)
<b>Cash flows from financing activities</b>						
Issuance of common units	88					88

## Edgar Filing: MAGNACHIP SEMICONDUCTOR LLC - Form 10-K

Repurchase of common units	(420)				(420)
Net cash provided by (used in) financing activities	(332)				(332)
Effect of exchange rates on cash and cash equivalents			6,226	(337)	(43)
Net increase (decrease) in cash and cash equivalents	112	51	9,173	(6,737)	2,599
<b>Cash and cash equivalents</b>					
Beginning of the period	209	841	63,435	22,089	86,574
End of the period	\$ 321	\$ 892	\$ 72,608	\$ 15,352	\$ 89,173

**Table of Contents****MagnaChip Semiconductor LLC and Subsidiaries****Notes to Consolidated Financial Statements (Continued)**

(Tabular dollars in thousands, except unit data)

**Condensed Consolidating Statement of Cash Flows**

For the year ended December 31, 2005

	MagnaChip Semiconductor LLC (Parent)	Co-Issuers	Non- Guarantors	Guarantors	Eliminations	Consolidated
<b>Cash flows from operating activities</b>						
Net income (loss)	\$ (100,898)	\$ (94,215)	\$ (89,854)	\$ (81,888)	\$ 265,957	\$ (100,898)
Adjustments to reconcile net income (loss) to net cash provided by operating activities						
Depreciation and amortization			196,669	6,260		202,929
Provision for severance benefits			16,486	97		16,583
Amortization of debt issuance costs		2,628	804			3,432
Loss (gain) on foreign currency translation, net		21,841	(16,288)	(21,433)		(15,880)
Loss (gain) on disposal of property, plant and equipment, net			(830)	1		(829)
Impairment charges			33,576			33,576
Loss (earnings) of related investment	100,364	78,445		86,985	(265,794)	
Other	1		290	(2,352)	2,782	721
Changes in operating assets and liabilities						
Accounts receivable			(31,412)	(13,816)	19,416	(25,812)
Inventories			(3,312)	2,110	396	(806)
Other receivables	(241)	826	63,970	(19,536)	17,802	62,821
Deferred tax assets				(12,935)		(12,935)
Accounts payable			29,438	14,906	(19,416)	24,928
Other accounts payable	(161)	188	(62,561)	14,267	(17,802)	(66,069)
Accrued expenses		2,011	(5,591)	17,549	(19,153)	(5,184)
Other current assets		(16,505)	1,878	(1,813)	19,153	2,713
Other current liabilities		163	(4,968)	5,005		200
Payment of severance benefits			(13,820)	(11)		(13,831)
Other			(31,266)	31,936	(2,682)	(2,012)
Net cash provided by (used in) operating activities	(935)	(4,618)	83,209	25,332	659	103,647
<b>Cash flows from investing activities</b>						
Purchase of plant, property and equipment			(62,113)	(622)	401	(62,334)
Payment for intellectual property registration			(2,174)			(2,174)
Acquisition of business, net of cash acquired of \$4,620 for the year ended December 31, 2005	(1,870)		18	(9,897)		(11,749)
Increase in short-term intercompany loans				(14,000)	14,000	
Increase in long-term intercompany loans		(1,009)		(1,009)	2,018	
Decrease in short-term intercompany loans		3,650		14,000	(17,650)	
Decrease in restricted cash			10,307			10,307
Other		(5)	2,045	198	(360)	1,878
Net cash provided by (used in) investing activities	(1,870)	2,636	(51,917)	(11,330)	(1,591)	(64,072)
<b>Cash flows from financing activities</b>						
Proceeds from short-term borrowings				14,000	(14,000)	

Edgar Filing: MAGNACHIP SEMICONDUCTOR LLC - Form 10-K

Proceeds from long-term borrowings			1,009	1,009	(2,018)	
Issuance of common units	628					628
Repayment of short-term borrowings			(757)	(29,776)	17,650	(12,883)
Debt issuance cost paid		(378)	(216)			(594)
Other			41		(41)	
Net cash provided by (used in) financing activities	628	(378)	77	(14,767)	1,591	(12,849)
Effect of exchange rates on cash and cash equivalents			2,395	(284)	(659)	1,452
Net increase (decrease) in cash and cash equivalents	(2,177)	(2,360)	33,764	(1,049)		28,178
<b>Cash and cash equivalents</b>						
Beginning of the period	2,386	3,201	29,671	23,138		58,396
End of the period	\$ 209	\$ 841	\$ 63,435	\$ 22,089	\$	\$ 86,574

**Table of Contents****MagnaChip Semiconductor LLC and Subsidiaries****Notes to Consolidated Financial Statements (Continued)**

(Tabular dollars in thousands, except unit data)

**Condensed Consolidating Statement of Cash Flows****For the three months ended December 31, 2004**

	<b>MagnaChip Semiconductor LLC</b>		<b>Non- Guarantors</b>		<b>Guarantors</b>	<b>Eliminations</b>	<b>Consolidated</b>
	<b>(Parent)</b>	<b>Co-Issuers</b>	<b>Guarantors</b>	<b>Guarantors</b>	<b>Guarantors</b>	<b>Eliminations</b>	<b>Consolidated</b>
<b>Cash flows from operating activities</b>							
Net income (loss)	\$ (5,825)	\$ (8,693)	\$ (9,420)	\$ (18,784)	\$ 36,897		\$ (5,825)
Adjustments to reconcile net income (loss) to net cash provided by operating activities							
Depreciation and amortization			45,847	8			45,855
Provision for severance benefits			3,397				3,397
Amortization of debt issuance costs		152	4,259				4,411
Loss (gain) on foreign currency translation, net		(7,914)	(32,733)	7,384			(33,263)
Loss (gain) on disposal of property, plant and equipment, net			(193)				(193)
Loss (earnings) of related investment	8,411	20,581		9,420	(38,412)		
Others			363	131			494
<b>Changes in operating assets and liabilities</b>							
Accounts receivable			(55,968)	(42,559)	55,257		(43,270)
Inventories			36,137	(1,172)	1,548		36,513
Other receivables	(2,243)	(810)	(55,266)	(1,651)	3,053		(56,917)
Accounts payable			(34,196)	56,392	(55,257)		(33,061)
Other accounts payable	(29,266)	189	121,181	(7,428)	(3,167)		81,509
Accrued expenses		1,128	16,257	6,235	(5,909)		17,711
Other current assets		(5,909)	(4,194)	(1,815)	5,909		(6,009)
Other current liabilities			6,965	2,877			9,842
Payment of severance benefits			(2,898)				(2,898)
Others			(1,003)	(8)			(1,011)
Net cash provided by operating activities	(28,923)	(1,276)	38,535	9,030	(81)		17,285
<b>Cash flows from investing activities</b>							
Purchase of plant, property and equipment			(23,261)	(85)			(23,346)
Payment for intellectual property registration			(101)	(7)			(108)
Acquisition of business			(488,152)				(488,152)
Increase in restricted cash			(12,350)				(12,350)
Disposal (purchase) of related investment	20,723	(26,026)		(194,015)	199,318		
Decrease (increase) of intercompany loans	291,824	(398,250)		(619,991)	726,417		
Others			(2,033)	6			(2,027)
Net cash used in investing activities	312,547	(424,276)	(525,897)	(814,092)	925,735		(525,983)
<b>Cash flows from financing activities</b>							
Proceeds from issuance of Senior Secured and Subordinated Notes		750,000					750,000
Proceeds from short-term borrowings		41,000	721	50,212	(91,213)		720

Edgar Filing: MAGNACHIP SEMICONDUCTOR LLC - Form 10-K

Proceeds from long-term borrowings			663,878	669,396	(1,287,407)	45,867
Issuance of common units	2,820	1,429	203,208	26,351	(230,988)	2,820
Issuance of redeemable convertible preferred units	3,636					3,636
Repayment of short-term borrowings		(332,824)		(321,030)	653,854	
Repayment of long-term borrowings			(347,718)			(347,718)
Redemption of redeemable convertible preferred units	(406,786)					(406,786)
Payment of preferred dividends	(10,891)					(10,891)
Debt issuance costs paid		(22,020)	(5,615)			(27,635)
Others		(22,476)	(16)		22,476	(16)
Net cash provided by (used in) financing activities	(411,221)	415,109	514,458	424,929	(933,278)	9,997
Effect of exchange rates on cash and cash equivalents			2,566	27	7,624	10,217
Net increase (decrease) in cash and cash equivalents	(127,597)	(10,443)	29,662	(380,106)		(488,484)
<b>Cash and cash equivalents</b>						
Beginning of the period	129,983	13,644	9	403,244		546,880
End of the period	\$ 2,386	\$ 3,201	\$ 29,671	\$ 23,138	\$	\$ 58,396

## **Table of Contents**

### **Item 9. Changes in and Disagreements With Accountants on Accounting and Financial Disclosure.**

None.

### **Item 9A. Controls and Procedures**

#### **Disclosure Controls and Procedures**

As required by the Securities Exchange Act of 1934, as amended (the Exchange Act), our management, including our Chief Executive Officer (CEO) and our Chief Financial Officer (CFO), conducted an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures as of the end of the period covered by this report. As defined in Rule 13a-15(e) and 15d-15(e) under the Exchange Act, disclosure controls and procedures are controls and other procedures that we use that are designed to ensure that information required to be disclosed by us in the reports we file or submit under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by us in the reports we file or submit under the Exchange Act is accumulated and communicated to our management, including our CEO and our CFO, as appropriate, to allow timely decisions regarding required disclosure. Management necessarily applies its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

Based upon that evaluation, our CEO and our CFO concluded that our disclosure controls and procedures were effective as of the end of the period covered by this report.

#### **Inherent Limitations on Effectiveness of Controls**

Our management, including our CEO and CFO, does not expect that our disclosure controls and procedures will prevent or detect all error and all fraud. A control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the control system's objectives will be met. The design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Further, because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that misstatements due to error or fraud will not occur or that all control issues and instances of fraud, if any, within the Company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty and that breakdowns can occur because of simple error or mistake. Controls can also be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the controls. The design of any system of controls is based in part on certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Projections of any evaluation of controls effectiveness to future periods are subject to risks. Over time, controls may become inadequate because of changes in conditions or deterioration in the degree of compliance with policies or procedures. Our internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of our financial reporting and preparation of financial statements for external purposes in accordance with generally accepted accounting principles. Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements.

#### **Changes in Internal Control Over Financial Reporting**

There has been no change in our internal controls over financial reporting during our most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal controls over financial reporting.



**Table of Contents**

**Item 9B. Other Information.**

**Entry into a Material Definitive Agreement**

On March 26, 2007, the Company entered into the Sixth Amendment to Credit Agreement, dated as of March 26, 2007 (the Sixth Amendment), with MagnaChip Semiconductor S.A. and MagnaChip Semiconductor Finance Company, as borrowers, the Subsidiary Guarantors party thereto, the Lenders party thereto, and UBS AG, Stamford Branch, as administrative agent and collateral agent. Under the Sixth Amendment, among other things, the existing financial covenants set forth in Section 6.10 of the Credit Agreement were revised to provide that authorized but unspent capital expenditures in a calendar quarter during 2007 carry over to increase the authorized limit on capital expenditures in successive calendar quarters.

**Termination of Material Definitive Agreement; Departure of an Officer**

On March 23, 2007, Jason Hartlove resigned from his position as our Senior Vice President and General Manager, Imaging Solutions Division, effective March 9, 2007, and terminated that certain Service Agreement dated as of May 16, 2005, by and between Mr. Hartlove and MagnaChip Semiconductor, Ltd., a subsidiary of the Company. Under the termination arrangement, Mr. Hartlove will receive a severance payment equal to seven months of his base salary of \$310,000 per annum.

**Table of Contents****PART III****Item 10. Directors, Executive Officers and Corporate Governance.**

The following table is a list of the current directors and executive officers of MagnaChip:

<b>Name</b>	<b>Age</b>	<b>Position</b>
Sang Park	59	Chairman of the Board of Directors and Chief Executive Officer
Robert J. Krakauer	41	President, Chief Financial Officer and Director
Tae Young Hwang	50	Executive Vice President, Manufacturing Division, and General Manager of Large Display Solutions
Chan Hee Lee	53	Executive Vice President and General Manager, Semiconductor Manufacturing Services
John McFarland	40	Senior Vice President, General Counsel and Secretary
Victoria Miller Nam	39	Senior Vice President, Strategic Operations
Brent Rowe	45	Senior Vice President of Worldwide Sales
Margaret Sakai	49	Senior Vice President, Finance
Jerry M. Baker	55	Director
Dipanjan Deb	37	Director
Armando Geday	44	Director
Roy Kuan	40	Director
R. Douglas Norby	71	Director and Chairman of the Audit Committee
Phokion Potamianos	43	Director
Paul C. Schorr IV	39	Director
David F. Thomas	57	Director

*Sang Park, Chairman of the Board of Directors and Chief Executive Officer.* Mr. Park became our Chairman of the Board of Directors and Chief Executive Officer on January 1, 2007, after serving as President, Chief Executive Officer and Director since May 2006. Mr. Park has served as an executive fellow for iSuppli Corporation since January 2005. Prior to joining iSuppli, he was founder and president of SP Associates from September 2003 to December 2004. Mr. Park served Hynix Semiconductor Inc. as Chief Executive Officer from May 2002 to March 2003 and Chief Operating Officer and President of the Semiconductor Division from July 1999 to April 2002.

*Robert J. Krakauer, President, Chief Financial Officer and Director.* Mr. Krakauer became our President, Chief Financial Officer, and Director in January 2007. In addition, Mr. Krakauer took on duties as General Manager, Imaging Solutions Division, in March 2007. He had previously served as our Executive Vice President of Strategic Operations, Chief Financial Officer and Director from October 2004. From 2003 to 2004, Mr. Krakauer served as Executive Vice President of Corporate Operations and Chief Financial Officer for ChipPAC, Ltd. (now STATS ChipPAC, Ltd.), and had served as its Chief Financial Officer since November 1999. From May 1998 to November 1999, Mr. Krakauer was Vice President of Finance, Chief Financial Officer for AlliedSignal Electronic Materials (now Honeywell). From 1996 to 1998, Mr. Krakauer was the Corporate Controller at Altera Corporation and from 1993 to 1996 he was the Chief Financial Officer at Alphatec U.S.A. From 1987 to 1991, Mr. Krakauer was an auditor and consultant at KPMG Peat Marwick and Coopers & Lybrand, respectively. Mr. Krakauer received a B.S.C. in accounting and a masters in business administration with an operations concentration from Santa Clara University.

*Tae Young Hwang, Executive Vice President, Manufacturing Division, and General Manager of Large Display Solutions.* Mr. Hwang became our Executive Vice President, Manufacturing Division, and General Manager of Large Display Solutions in January 2007. He had previously served as our Executive Vice President of Manufacturing Operations from October 2004. Prior to that time, Mr. Hwang served as Hynix's Senior Vice

## **Table of Contents**

President of Manufacturing Operations of System IC from 2002 to 2003. From 1999 to 2001, he was Vice President of Cheongju Operations for Hynix. Mr. Hwang holds a bachelor of science degree in mechanical engineering from Pusan National University and a masters in business administration from Cheongju University.

*Chan Hee Lee, Executive Vice President and General Manager, Semiconductor Manufacturing Services.* Mr. Lee became our Executive Vice President and General Manager, Semiconductor Manufacturing Services in September 2005, after serving as Executive Vice President of Product Lines since October 2004. Previously, Mr. Lee had been employed by Hynix as Vice President and General Manager of Semiconductor Manufacturing Services and Digital Driver IC, Business Division from 1999 until September 2004. Mr. Lee holds a bachelor of science degree in electronics from Kyungbuk National University.

*John McFarland, Senior Vice President, General Counsel and Secretary.* Mr. McFarland became our Senior Vice President, General Counsel and Secretary in April 2006, after serving as Vice President, General Counsel and Secretary since November 2004. Prior to joining our company, Mr. McFarland served as a foreign legal consultant at Bae, Kim & Lee from August 2003 to November 2004 and an associate at Wilson Sonsini Goodrich & Rosati, P.C., from August 2000 to July 2003. Mr. McFarland holds a bachelor of arts degree in Asian Studies, conferred with highest distinction from the University of Michigan, where he was elected to Phi Beta Kappa, and a juris doctor degree from the University of California, Los Angeles, School of Law.

*Victoria Miller Nam, Senior Vice President, Strategic Operations.* Ms. Miller Nam became our Senior Vice President, Strategic Operations in January 2007, after serving as Senior Vice President, Strategic Planning since October 2004. Prior to joining our company, Ms. Miller Nam worked in consulting with McKinsey & Company in the Los Angeles and Seoul offices from 1994 until 2003, when she left as a Partner to found and run a consulting business from 2003 until 2004. Earlier in her career, Ms. Miller Nam worked for Kidder, Peabody & Co. Incorporated, in the corporate finance department, in New York. Ms. Miller Nam holds a bachelor of arts degree, *magna cum laude*, in international relations from Brown University, where she was elected to Phi Beta Kappa, and a masters in business administration from Harvard Business School.

*Brent Rowe, Senior Vice President of Worldwide Sales.* Mr. Rowe became our Senior Vice President for Global Sales in April 2006. Prior to joining our company, Mr. Rowe served at Fairchild Semiconductor International, Inc. as Vice President of Americas Sales and Marketing from August 2003 to October 2005, Vice President of Europe Sales and Marketing from August 2002 to August 2003, and Vice President of Japan Sales and Marketing from April 2002 to August 2003. Mr. Rowe holds a bachelor of arts degree in chemical engineering from the University of Illinois.

*Margaret Sakai, Senior Vice President, Finance.* Ms. Sakai became our Senior Vice President, Finance, on November 1, 2006. Prior to joining our company, she had served as Chief Financial Officer of Asia Finance, Vice President, of Photronics, Inc. since November 2003. From June 1999 to October 2003, Ms. Sakai was Executive Vice President and Chief Financial Officer of PKL Corporation. From October 1995 to May 1999, Ms. Sakai served as Director of Finance of Acqutek International Limited, a lead-frame manufacturer, and from March 1992 to September 1995, Ms. Sakai was Financial Manager at National Semiconductor Corporation. Ms. Sakai worked as an Audit Supervisor at Coopers & Lybrand from January 1988 to March 1992. Ms. Sakai is a Certified Public Accountant in the State of California, and holds a bachelor's degree in accounting from Babson College.

*Jerry M. Baker, Director.* Mr. Baker has been a director since October 2004. He served as Chairman of the Board of Directors from October 2004 to December 2006. From 2000 until 2001, Mr. Baker served as Executive Vice President, Global Operations for Fairchild Semiconductor International, Inc. Previously, Mr. Baker had been Executive Vice President and General Manager, Discrete Power and Signal Technologies Group, since December 1996. Prior to that position, he spent more than 24 years in a variety of engineering and management positions within National Semiconductor, the most recent of which was Vice President and General Manager, Discrete Products Division.

---

**Table of Contents**

*Dipanjan Deb, Director.* Mr. Deb has been a director since September 2004. He is a founder and Managing Partner of Francisco Partners and has been a Partner since its formation in August 1999. Prior to joining Francisco Partners, Mr. Deb was a principal with Texas Pacific Group from 1998 to 1999. Earlier in his career, Mr. Deb was director of semiconductor banking at Robertson Stephens & Company and a management consultant at McKinsey & Company. Mr. Deb is also on the board of directors of AMIS Holdings, Inc., SMART Modular Technologies, Inc., and Metrologic Instruments, Inc. Mr. Deb holds a bachelor of science degree in electrical engineering and computer science from the University of California, Berkeley, where he was a Regents Scholar, and a masters in business administration from the Stanford University Graduate School of Business.

*Armando Geday, Director.* Mr. Geday has been a director since January 2006. He has served as Chief Executive Officer of Telesen, Inc. since January 2005. Prior to joining Telesen, Mr. Geday was Chief Executive Officer of Conexant systems from November 2003 to November 2004. From April 1997 to December 2001, Mr. Geday was President and CEO of GlobeSpan, and from December 2001 to February 2004, Mr. Geday served as the Chief Executive Officer of Globespanvirata. Earlier in his career, Mr. Geday was Vice President and General Manager of the Multimedia Communications Division of Rockwell Semiconductor Systems and held various technical marketing and engineering positions at Harris Semiconductor and MERET Inc. Mr. Geday holds a bachelor of science degree in electrical engineering from the Florida Institute of Technology.

*Roy Kuan, Director.* Mr. Kuan has been a director since September 2004. He serves as Managing Director of CVC Asia Pacific Limited, where he has worked since 1999. Prior to that Mr. Kuan worked at Citicorp's Asia private equity unit from 1996 until 1999. Mr. Kuan holds a bachelor of arts degree in economics from Georgetown University and a masters in business administration with a finance concentration from the Wharton School at the University of Pennsylvania.

*R. Douglas Norby, Director and Chairman of the Audit Committee.* Mr. Norby has been a director and the Chairperson of the Audit Committee of the company since May 2006. Mr. Norby served as Senior Vice President and Chief Financial Officer of Tessera Technologies, Inc. from July 2003 to January 2006. He worked as a management consultant with Tessera from May 2003 until July 2003, and was a private investor from March 2003 until May 2003. He served as Vice President and Chief Financial Officer of Zambeel, Inc., a data storage systems company, from March 2002 until February 2003, and as Chief Financial Officer of Novalux, Inc., an optoelectronics company, from December 2000 to March 2002. Prior to his tenure with Novalux, Inc., Mr. Norby served as Executive Vice President and Chief Financial Officer of LSI Logic Corporation from November 1996 to November 2000. Mr. Norby is a director of LSI Logic Corporation, Alexion Pharmaceuticals, Inc., and STATS ChipPAC Ltd. He received his bachelor of arts degree in Economics from Harvard University and a masters in business administration from Harvard Business School.

*Phokion Potamianos, Director.* Mr. Potamianos has been a director since March 2005. He has been a Principal with Francisco Partners since March 2005. Prior to joining Francisco Partners, Mr. Potamianos was the head of the UBS global semiconductor investment banking group, and a member of Donaldson Lufkin & Jenrette's investment banking group. Earlier in his career, Mr. Potamianos was an Institutional Investor ranked research analyst at Donaldson, Lufkin & Jenrette. Mr. Potamianos holds a B.A. from American University and received his Masters of Science (Economics) from the London School of Economics and Political Science.

*Paul C. Schorr IV, Director.* Mr. Schorr has been a director since September 2004. He has been a Senior Managing Director at Blackstone Group since September 2005. Prior to that, he was a Managing Partner of CVC from December 2001. Mr. Schorr joined CVC in 1996, after working as an Engagement Manager with McKinsey & Company, Inc. Mr. Schorr received his B.S.F.S. *magna cum laude* from Georgetown University's School of Foreign Service and his masters in business administration with distinction from Harvard Business School. He is also a director of AMI Semiconductor Inc.

*David F. Thomas, Director.* Mr. Thomas has been a director since October 2004. Mr. Thomas is the Managing Partner of Court Square Capital Partners (formerly known as Citigroup Venture Capital Equity

## **Table of Contents**

Partners, L.P.). He joined Court Square in 1980. Previously, he held various positions with Citibank's Transportation Finance and Acquisition Finance Groups. Prior to joining Citibank, Mr. Thomas was a certified public accountant with Arthur Andersen & Co. Mr. Thomas received degrees in finance and accounting from the University of Akron. He is a director of Network Communications, Inc.

### **Board Composition**

The securityholders' agreement among CVC, Francisco Partners, CVC Asia Pacific and the other securityholders of MagnaChip provides that our Board of Directors will consist of eight members, including two designees of CVC, two designees of Francisco Partners, one designee of CVC Asia Pacific, the Chief Executive Officer, the Chief Financial Officer and one additional member jointly designated by CVC and Francisco Partners, provided that the unitholders are permitted to elect additional directors designated as set forth in the securityholders' agreement. These rights of designation will expire when the initial ownership of these equity sponsors falls below defined ownership thresholds. Pursuant to the securityholders' agreement, our Board of Directors may not take certain significant actions without the approval of each of CVC and Francisco Partners.

Effective January 19, 2006, Armando Geday was elected to our Board of Directors to serve at the discretion of the unitholders of the Company until his successor is duly elected and qualified. Mr. Geday serves as an additional designee of Francisco Partners. Mr. Baker serves as an additional designee of CVC. Effective May 27, 2006, R. Douglas Norby was elected to our Board of Directors to serve at the discretion of the unitholders of the Company until his successor is duly elected and qualified. Mr. Norby serves as a joint designee of CVC and Francisco Partners, meaning that our Board of Directors consists of ten members as of the filing date of this report.

### **Code of Ethics**

We have adopted a Code of Business Conduct and Ethics that applies to all our directors, officers, and employees. We will provide a copy of our Code of Business Conduct and Ethics without charge to any person upon written request made to our Senior Vice President, General Counsel and Secretary at c/o MagnaChip Semiconductor, Ltd., 891 Daechi-dong, Gangnam-gu, Seoul, 135-738, Korea.

### **Nominating Committee**

There have been no material changes to the procedures by which security holders may recommend nominees to our Board of Directors.

### **Audit Committee**

Our audit committee is comprised of Chairperson R. Douglas Norby and directors Phokion Potamianos and Paul Schorr IV. Our Board of Directors has determined that R. Douglas Norby is an audit committee financial expert as defined in Item 407(d)(5) of Regulation S-K promulgated under the Securities Act of 1933, as amended, is an independent director as that term is defined in Rule 4200 of the Rules of The NASDAQ Stock Market LLC (the NASDAQ Rules) and is independent as that term is defined in both Rule 4350(d) of the NASDAQ Rules and Rule 10A-3 promulgated under the Securities Exchange Act of 1934, as amended.

## **Item 11. Executive Compensation.**

### **Compensation Discussion and Analysis**

*Objectives.* The Compensation Committee (for purposes of this section, the Committee) of our Board has overall responsibility for evaluating, approving, and monitoring our executive officer and director compensation plans, policies and programs, as well as all equity-based compensation plans and policies. The Committee

## **Table of Contents**

ensures that the total compensation paid to executive officers is fair, reasonable, and competitive. Throughout this Form 10-K, the individuals who served as our Chief Executive Officer and Chief Financial Officer during fiscal year 2006, as well as the other individuals included in the Summary Compensation Table within this Item 11, are referred to as the named executive officers.

The Committee evaluates our compensation packages to ensure that (i) we maintain our ability to attract and retain superior executives in critical positions, and (ii) compensation provided to critical executives remains competitive relative to the compensation paid to similarly situated executives of our peer companies. The Committee believes that the most effective executive compensation packages align executives' interests with those of our unitholders by rewarding performance above specific annual, long-term, and strategic goals that are intended to improve unitholder value. These goals include, but are not limited to, achievement of financial performance targets and progress in projects that our Board of Directors anticipates will lead to future growth.

*Determination of Compensation and Role of Executive Officers.* We offer compensation to our named executive officers in the form of salary, cash incentives, equity incentives, and perquisites. In making decisions regarding the pay of the named executive officers, the Committee looks to set a total compensation package for each officer that will retain high-quality talent and motivate executives to achieve the goals set by our Board of Directors.

The Committee annually reviews the performance of the Chief Executive Officer, and the Chief Executive Officer annually reviews the performance of every other executive officer. The Chief Executive Officer presents conclusions and recommendations regarding the named executive officers, including proposed salary adjustments and incentive amounts, to the Committee, which makes the final decision regarding any adjustments or awards. The Committee's annual determinations regarding executive compensation are subject to the terms of the respective service agreements between us and the named executive officers. In addition to the annual reviews, the Chief Executive Officer and the Committee also typically consider compensation changes upon a named executive officer's promotion or other change in job responsibility.

The Committee approves general guidelines and plans regarding the cash compensation of all other officers and employees, but has empowered the Chief Executive Officer to make final compensation decisions within the Committee guidelines and plans. The Committee makes all equity compensation decisions for our officers and employees.

In determining a compensation award, the Committee compares each element of total compensation against compensation offered by a group of peer companies in the semiconductor industry (collectively, the Benchmark Group). The composition of the Benchmark Group is determined annually by our Human Resources department in consultation with the Chief Executive Officer and the Committee. The Committee's general objective is to provide a total cash compensation package, including base salary and incentive, slightly above the median total cash compensation package of the Benchmark Group. Variations to this objective may occur as dictated by the experience level of the individual and market factors.

Cash incentives comprise a significant portion of the total compensation package and are designed to reward executives for their contributions to meeting and exceeding our goals and to recognize and reward the accountability of our executives in achieving these goals. Incentives are designed as a percentage of base salary and are awarded based on individual performance and our achievement of the annual, long-term, and strategic goals set by our Board of Directors.

*Equity Compensation.* In addition to cash incentives, we offer equity incentives as a way to enhance the link between the creation of unitholder value and executive incentive compensation and to give executives appropriate motivation and rewards for achieving increases in enterprise value. The Committee may grant participants restricted units, unit options, and unit appreciation rights. Although the Committee granted certain restricted units awards upon the Original Acquisition, the Committee has determined that it will only grant

## **Table of Contents**

restricted units in the future in exceptional cases. In granting equity awards, the Committee may establish any conditions or restrictions it deems appropriate. Grants of restricted units or unit options typically vest four years after the date of the grant, and all grants of our unit options are made at or above the fair market value of the units at the time of the grant. Vesting and exercise rights generally cease upon termination of employment. Prior to the exercise of a unit option, the holder has no rights as a unitholder with respect to the units subject to such option, including voting rights and the right to receive dividends or dividend equivalents.

Our unitholders and Board of Directors have delegated to the Committee the authority to grant unit option awards within a total pool of our common units available upon exercise of the unit options. The size of the option pool is based on market surveys of peer companies in a similar growth stage and on our unitholders' determination of an appropriately-sized pool to ensure recruitment and retention of key executives and employees. Unit option award levels vary among participants based on their job grade and position. The Committee provides higher awards to those executives and employees in positions considered by the Committee to be critical. Unit option awards are not tied to base salary or cash incentive amounts.

At this time, the Committee does not grant additional equity compensation to existing executives as part of the normal annual review process. However, the Committee will consider additional equity compensation in the event of a promotion or change in job responsibility. Upon the recommendation of our Board of Directors or Chief Executive Officer, the Committee will from time to time consider performance-based equity incentives. For example, in March 2006, the Committee granted certain executives, including four of the named executive officers, unit options that begin vesting only upon the earlier of the closing of the initial public offering of our common equity or the date on which the Committee determines that the unitholders of the Company as of October 6, 2004, have achieved a 2.5x return on their investment.

*Perquisites and Other Benefits.* We provide the named executive officers with perquisites and other personal benefits that the Committee believes are reasonable and consistent with its overall compensation program to better enable us to attract and retain superior employees for key positions. Several of our named executive officers are assigned to locations outside their home countries and therefore receive expatriate benefits. The Committee determines the level and types of expatriate benefits for the officers based on local market surveys taken by our Human Resources department. Attributed costs of the personal benefits for the named executive officers are as set forth in the Summary Compensation Table below.

*Tax and Accounting Implications.* Beginning on January 1, 2006, we began accounting for unit-based payments, including our unit option program, in accordance with the requirements of FASB Statement No. 123(R).

**Table of Contents****Summary Compensation Table**

The following table sets forth certain information concerning the compensation earned during the year ended December 31, 2006, of our Chief Executive Officer, of our Chief Financial Officer, of the three other most highly compensated executive officers who were executive officers on December 31, 2006, other than the Chief Executive Officer and Chief Financial Officer, and of our former President and Chief Executive Officer, who resigned as Chief Executive Officer and President effective May 27, 2006, but remained our Senior Advisor and received enough total compensation to qualify for disclosure on this table.

<b>Name and Principal Position</b>	<b>Year</b>	<b>Salary (\$)</b>	<b>Bonus (\$)</b>	<b>Stock Awards (\$)</b>	<b>Option Awards (\$) (1)</b>	<b>Non-Equity Incentive Plan Compensation (\$)</b>	<b>Change in Pension Value and Nonqualified Deferred Compensation Earnings (\$)</b>	<b>All Other Compensation (\$)</b>	<b>Total (\$)</b>
Sang Park Chairman and Chief Executive Officer	2006	262,500	130,000		62,473			321,129 (2)	776,102
Robert J. Krakauer President and Chief Financial Officer	2006	375,000	80,000					387,090 (3)	842,090
Victoria Miller Nam Senior Vice President, Strategic Operations	2006	300,000	30,000				25,246(4)	96,515 (5)	451,761
Tae Young Hwang Executive Vice President, Manufacturing Division, and General Manager of Large Display Solutions	2006	230,539	50,000		20,087		49,283(4)	11,617(6)	361,526
Chan Hee Lee Executive Vice President and General Manager, Semiconductor Manufacturing Services	2006	209,577	50,000		20,087		44,803(4)	20,272(7)	344,739
Jason Hartlove Former Senior Vice President and General Manager, Imaging Solutions Division (8)	2006	309,201	50,000		31,898			35,481 (9)	426,580
Youm Huh Senior Advisor and former Chief Executive Officer and President (10)	2006	400,000						275,964 (11)	675,964

Note: Amounts set forth in the above table that were originally paid in Korean Won have been converted into U.S. dollars at the exchange rate as of each payment date during our fiscal year ended December 31, 2006.

Footnotes:

(1)



## Edgar Filing: MAGNACHIP SEMICONDUCTOR LLC - Form 10-K

This amount is calculated using the dollar amount recognized for financial statement reporting purposes with respect to the fiscal year in accordance with FAS 123(R).

- (2) Includes the following personal benefits paid to Mr. Park: (a) \$62,872 equivalent to five months from \$301,785 for prepayment of Mr. Park's housing expenses for two years; (b) \$200,000 of Mr. Park's relocation allowance when he joined us; and (c) \$20,610 for insurance premiums paid during the fiscal year 2006 for the benefit of Mr. Park; and (d) \$37,647 for other personal benefits (including monthly rent for Mr. Park's housing lease for three months, and reimbursement of the use of a car, home leave flights and living expenses).
- (3) Includes the following personal benefits paid to Mr. Krakauer: (a) \$176,042 equivalent to one year from \$352,083 for prepayment of Mr. Krakauer's housing expenses for two years; (b) \$40,848 for reimbursement of living expenses; (c) \$69,485 for reimbursement of tuition expenses for Mr. Krakauer's children; (d) \$32,405 for the amount settled between Mr. Krakauer's receivables from us and his tax equalization payment to us for the fiscal year 2004; (e) \$23,547 for insurance premiums paid during the fiscal year 2006 for the benefit of Mr. Krakauer; (f) \$2,399 for tax equalization settlement from us for the fiscal year 2005; and (g) \$42,364 for other personal benefits (including reimbursement of the use of a car and personal tax advisory expenses).

**Table of Contents**

- (4) Consists of statutory severance accrued during the fiscal year ended December 31, 2006. See the section of this Item subtitled Further Information Regarding Summary Compensation Table and Grants of Plan-Based Awards Table for a description of the statutory severance benefit.
- (5) Includes the following personal benefits paid to Ms. Miller Nam: (a) \$22,924 for insurance premiums paid during the fiscal year 2006 for the benefit of Ms. Miller Nam;(b) \$68,376 for reimbursement of tuition expenses for Ms. Miller Nam's children; and (c) \$5,215 for reimbursement of the use of a car.
- (6) Reimbursement of the use of a car.
- (7) Includes the following personal benefits paid to Mr. Lee: (a) \$12,812 for reimbursement of the use of a car; and (b) \$7,460 for reimbursement of tuition expenses for Mr. Lee's children.
- (8) Mr. Hartlove resigned as Senior Vice President and General Manager, Imaging Solutions Division, effective March 9, 2007.
- (9) Includes the following personal benefits paid to Mr. Hartlove: (a) \$18,935 for insurance premiums paid during the fiscal year 2006 for the benefit of Mr. Hartlove; (b) \$7,802 for reimbursement of personal tax advisory expenses; and (c) \$8,744 for other personal benefits (including reimbursement of the use of a car, and personal legal advisory expenses).
- (10) Dr. Huh resigned as Chief Executive Officer, President, and Director effective May 27, 2006.
- (11) Includes the following personal benefits paid to Dr. Huh: (a) \$54,220 for insurance premiums paid during the fiscal year 2006 for the benefit of Dr. Huh; (b) \$31,792 for payment for unused annual holidays of Dr. Huh during the fiscal year 2006; (c) \$174,569 for the amount settled between Dr. Huh's receivables from us and his tax equalization payment to us for the fiscal year 2004; and (d) \$15,383 for other personal benefits (including reimbursement of the use of a car and tuition expenses for Dr. Huh's children).

**Grants of Plan Based Awards for the Fiscal Year Ended December 31, 2006**

Name	Grant Date	Board Approval Date	Non-Equity Incentive			Estimated Future Payouts Under Equity Incentive Plan Awards			All Other Stock Awards: Number of Shares or Units (#)	All Other Option Awards: Number of Securities Underlying Options (#)	Exercise or Base Price of Awards (\$/Sh)	Grant Date Fair Value of Stock and Option Awards (1)			
			Threshold (\$)	Target (\$)	Maximum (\$)	Threshold (#)	Target (#)	Maximum (#)							
													Plan Awards		
													Estimated Future		
Sang Park	May 27	May 17(2)					800,000			1.02	247,862				
Robert J. Krakauer	March 9	March 9					185,000			1.50	40,933				
Victoria Miller Nam	March 9	March 9					40,000			1.50	8,850				
Tae Young Hwang	March 9	March 9					25,000			1.50	5,532				
Chan Hee Lee	March 9	March 9					25,000			1.50	5,532				
Jason Hartlove	March 9	March 9					25,000(3)			1.50	5,532				
Youm Huh															

Footnotes:

- (1) We describe the option award calculation method under to SFAS No. 123(R) in Item 8. Financial Statements and Supplementary Data Notes to Consolidated Financial Statements Note 13. Equity Incentive Plan.
- (2) Although our Board approved the option grant to Mr. Park on May 17, 2006, the option grant was not effective until the start date of Mr. Park's employment on May 27, 2006.
- (3) Mr. Hartlove resigned as Senior Vice President and General Manager, Imaging Solutions Division, effective March 9, 2007. The reported equity award terminated unvested upon his resignation date.

**Further Information Regarding Summary Compensation Table and Grants of Plan-Based Awards Table**

As we discuss above in the Compensation Disclosure and Analysis subsection, our Board of Directors sets total cash compensation packages slightly above the median total cash compensation of the Benchmark Group, and sets equity awards in accordance with peer companies in a similar growth stage. Equity awards are not tied to base salary or cash incentive amounts, and will constitute lesser or greater proportions of total compensation depending on the fair value of the awards. Mr. Park, Mr. Krakauer, and Ms. Nam were expatriates during part or all of 2006 and received expatriate benefits commensurate with market practice in their assigned location of the Republic of Korea. The base salary and incentives for these named executive officers therefore constitute a lower proportion of total compensation in comparison to Mr. Hwang and Mr. Lee, both of whom reside in their home country.

The option grant to Mr. Park is described in the paragraph below labeled Sang Park. The option grants to Mr. Krakauer, Mr. Hartlove, Ms. Miller Nam, Mr. Hwang, and Mr. Lee were a performance-based incentive under the MagnaChip Semiconductor LLC Equity Incentive Plan and were intended by our Board of Directors to further encourage these named executive officers to progress MagnaChip toward an initial public offering of our common equity or other return on investment for our unitholders. The Board made the grants at an exercise price above the then-fair market value



---

**Table of Contents**

of our common units. An installment of 25% of the common units subject to the options become vested and exercisable upon the earlier of: (i) the date of the first closing of a firmly underwritten public offering for any of our equity securities, and (ii) the date as designated in the sole discretion of the Committee as the date upon which our unitholders as of October 6, 2004, have achieved a 2.5x return on their investment. The remaining 75% of the common units subject to the options become vested and exercisable as to 25% of such common units on each of the first three successive annual anniversaries of the first vesting event, subject to the Grantee's continuous employment from the grant date to each such vesting date. The options expire on the tenth anniversary of the grant date.

Pursuant to the Labor Standards Act of Korea, certain executive officers resident in Korea with one or more years of service are entitled to severance benefits upon the termination of their employment for any reason. For purposes of this section, we call this benefit statutory severance. The base statutory severance is approximately one month of base salary per year of service. Ms. Miller Nam, Mr. Hwang, and Mr. Lee all accrue statutory severance. Prior to the Original Acquisition, Hynix attached a multiplier to the statutory severance amounts for former Hynix executives Mr. Hwang and Mr. Lee. Although our Board has determined that we will not offer a statutory severance multiplier to any executives, in the interests of fairness our Board permitted Mr. Hwang and Mr. Lee to accrue a statutory severance multiplier of 3x, i.e., triple their statutory severance, for their service from October 6, 2004 to September 20, 2006, after which the sole unitholder of our Korean subsidiary disclaimed the severance multiplier for former Hynix executives.

Other than Youm Huh and Jason Hartlove, our named executive officers are all parties to service agreements. The material terms of these agreements, and the equity compensation granted pursuant to these agreements, are as follows:

*Sang Park.* Sang Park serves as Chairman and Chief Executive Officer of MagnaChip with an initial base salary of \$450,000 per year and with a target annual incentive bonus opportunity of 100% of his base salary. Mr. Park is entitled to customary employee benefits including the cost of housing accommodations and expenses, including relocation expenses. The term of the service agreement extends for two years from May 27, 2006, with such initial term automatically extending for additional two-year periods unless written notice is given by either party prior to the termination date. In accordance with the terms of his service agreement, Mr. Park received options to purchase 800,000 common units of the Company at a price of \$1.02 per unit, the then-fair market value of a common unit. Twenty-five percent of Mr. Park's options vest on the first anniversary of his service date and an additional 6.25% of the options vest at the end of each three month period thereafter on the same day of the month as the grant date or, if earlier, the last day of such month. If Mr. Park's employment is terminated without cause or if he resigns for good reason, Mr. Park is entitled to receive payment of all salary and benefits accrued up to the date of termination, payment of his base salary for twelve months and annual incentive bonus for the year in which the termination occurs, twelve months accelerated vesting on outstanding equity awards, and continued participation in our benefit plans for twelve months. If such termination occurs in connection with a change in control, Mr. Park is entitled to receive payment of all salary and benefits accrued up to the date of termination, payment of his base salary for two years and annual incentive bonus for the year in which the termination occurs, two years accelerated vesting on outstanding equity awards, and continued participation in our benefit plans for two years. In the event of his termination as a result of death or disability, Mr. Park (or his beneficiaries) will be entitled to receive payment of all salary and benefits accrued up to the date of termination and a prorated portion of the annual incentive bonus for the year in which the termination occurs. If Mr. Park's employment is terminated for cause or if he resigns without good reason, he will be entitled to receive payment of all salary and benefits accrued up to the date of termination and will not be entitled to any other compensation. The agreement also contains customary non-competition and non-solicitation covenants lasting two and three years, respectively, from the date of termination of employment and confidentiality covenants of unlimited duration.

*Robert Krakauer.* Mr. Krakauer serves as President and Chief Financial Officer of MagnaChip with an initial base salary of \$375,000 per year and with a target annual incentive bonus opportunity of 100% of his base salary. Mr. Krakauer is entitled to customary employee benefits and, for so long as his place of business is

---

**Table of Contents**

located in Korea, expatriate/repatriation benefits, including relocation expenses, tax equalization payments, cost of housing accommodations and expenses. The term of the service agreement extends for three years from October 6, 2004, with such initial term automatically extending for additional one-year periods unless written notice is given by either party prior to the termination date. In accordance with the terms of his service agreement, Mr. Krakauer was granted 682,247 immediately exercisable options for restricted common units of MagnaChip at a price of \$1.00 per unit. Mr. Krakauer exercised his options on November 30, 2004. Under his restricted unit subscription agreement, restrictions on the units lapse as to 25% of the units on September 30, 2005 and as to 6.25% of the units on the last day of each calendar quarter thereafter, subject to his continuous employment with MagnaChip. The restrictions lapse as to all restricted units held by Mr. Krakauer upon a change in control after which Mr. Krakauer no longer serves as the Chief Financial Officer of MagnaChip. The restricted unit subscription agreements provide that the units are nontransferable and shall be subject to forfeiture upon termination of his employment. Upon termination, MagnaChip may repurchase any units for which the restrictions have not lapsed for \$1.00, if termination is for cause (as defined in the agreement), or for fair market value, if termination is for any other reason. Mr. Krakauer has the right to vote the restricted units and to receive cash dividends, provided that dividends payable in units or other securities shall have the same status as restricted units. In connection with the exercise, Mr. Krakauer was entitled to a bonus of \$677,293 to pay the exercise price of a portion of the options and an additional payment of \$380,977 to cover U.S. federal income tax withholding related to such bonus. If Mr. Krakauer's employment is terminated without cause or if he resigns for good reason, Mr. Krakauer is entitled to receive his base salary for twelve months, payment of a prorated portion of the annual incentive bonus for the year in which the termination occurs and continued participation in our benefit plans for twelve months. In the event of his termination as a result of death or disability, Mr. Krakauer (or his beneficiaries) will be entitled to receive payment of all salary and benefits accrued up to the date of termination and a prorated portion of the annual incentive bonus for the year in which the termination occurs. If Mr. Krakauer's employment is terminated for cause or if he resigns without good reason, he will be entitled to receive payment of all salary and benefits accrued up to the date of termination and will not be entitled to any other compensation. The agreement also contains customary non-competition covenants lasting until the earlier of the first anniversary of the date of termination of employment or October 6, 2007, non-solicitation covenants lasting two years from the date of termination of employment and confidentiality covenants of unlimited duration.

*Victoria Miller Nam.* Ms. Miller Nam serves as the Senior Vice President of Strategic Planning of MagnaChip with an initial base salary of \$300,000 per year and with a target annual incentive bonus opportunity of 75% of her base salary. Ms. Miller Nam is entitled to customary employee benefits. The term of the service agreement extends for three years from December 29, 2004, with such initial term automatically extending for additional one-year periods absent prior written notice given by either party. Ms. Miller Nam was granted 136,450 immediately exercisable options for restricted common units of MagnaChip at a price of \$1.00 per unit. Ms. Miller Nam exercised her options on November 30, 2004. Under her restricted unit subscription agreement, restrictions on the units lapse as to 25% of the units on September 30, 2005 and as to 6.25% of the units on the last day of each calendar quarter thereafter, subject to her continuous employment with MagnaChip. The restricted unit subscription agreements provide that the units are nontransferable and shall be subject to forfeiture upon termination of the officer's employment. Upon termination, MagnaChip may repurchase any units for which the restrictions have not lapsed for \$1.00, if termination is for cause (as defined in the agreement), or for fair market value, if termination is for any other reason. Ms. Miller Nam has the right to vote the restricted units and to receive cash dividends, provided that dividends payable in units or other securities shall have the same status as restricted units. If Ms. Miller Nam's service is terminated without cause or if she resigns for good reason, Ms. Miller Nam will be entitled to receive her base salary for six months, payment of the annual incentive bonus in a prorated amount based on the number of days she was actually employed by us, continued participation in our benefit plans for six months, each of the foregoing net of any statutory severance accrued and payable, and, if such a termination or resignation occurs either prior to October 1, 2005 or within the twelve month period following a change of control, restrictions lapse with respect to 25% of her restricted common units on the date of termination. In the event of her termination as a result of death or disability, Ms. Miller Nam (or her beneficiaries) will be entitled to receive payment of all salary and benefits accrued up to the date of

---

**Table of Contents**

termination and a prorated portion of the annual incentive bonus for the year in which the termination occurs. If Ms. Miller Nam's service is terminated for cause or if she resigns without good reason, she will be entitled to receive payment of all salary and benefits accrued up to the date of termination and will not be entitled to any other compensation. All severance payable pursuant to Ms. Miller Nam's service agreement will be offset by any accrued statutory severance. The agreement also contains customary non-competition covenants lasting until the earlier of the first anniversary of the date of termination of employment or October 6, 2007, nonsolicitation covenants lasting two years from the date of termination of employment and confidentiality covenants of unlimited duration.

*Chan Hee Lee.* Mr. Lee serves as Executive Vice President and General Manager, Semiconductor Manufacturing Services of MagnaChip with an initial base salary of 200,000,000 Korean won per year (approximately \$209,600) and with a target annual incentive bonus opportunity of 80% of his base salary and rewards opportunities based on his performance. Mr. Lee is also entitled to customary employee benefits. The initial term of Mr. Lee's service agreement was October 1, 2004, to September 30, 2005, with the initial term automatically extending for additional one-year periods absent prior written notice by either party. In accordance with the terms of his service agreement, Mr. Lee received options to purchase 272,899 common units of MagnaChip at a price of \$1.00 per unit. Twenty-five percent of Mr. Lee's options vest on the first anniversary of his service date and an additional 6.25% of the options vest on the last day of each calendar quarter thereafter. Upon termination of Mr. Lee's employment for any reason, Mr. Lee is entitled to receive payment of all salary and benefits accrued up to the date of termination and a severance payment calculated as follows: statutory severance multiplied by three for service from the Original Acquisition to September 20, 2006, plus statutory severance with no multiplier for service after September 20, 2006. Mr. Lee's agreement contains customary service invention assignment provisions, customary non-competition covenants lasting a year from the date of termination of employment, and confidentiality covenants of unlimited duration.

*Tae Young Hwang.* Mr. Hwang serves as Executive Vice President, Manufacturing Division, and General Manager of Large Display Solutions of MagnaChip with an initial base salary of 220,000,000 Korean won per year (approximately \$230,500) and with a target annual incentive bonus opportunity of 80% of his base salary and rewards opportunities based on his performance. Mr. Hwang is also entitled to customary employee benefits. The initial term of Mr. Hwang's service agreement was October 1, 2004 to September 30, 2005, with the initial term automatically extending for additional one-year periods absent prior written notice by either party. In accordance with the terms of his service agreement, Mr. Hwang received options to purchase 272,899 common units of MagnaChip at a price of \$1.00 per unit. Twenty-five percent of Mr. Hwang's options vest on the first anniversary of his service date and an additional 6.25% of the options vest on the last day of each calendar quarter thereafter. Upon termination of Mr. Hwang's employment for any reason, Mr. Hwang is entitled to receive payment of all salary and benefits accrued up to the date of termination and a severance payment calculated as follows: statutory severance multiplied by three for service from the Original Acquisition to September 20, 2006, plus statutory severance with no multiplier for service after September 20, 2006. Mr. Hwang's agreement contains customary service invention assignment provisions, customary non-competition covenants lasting a year from the date of termination of employment, and confidentiality covenants of unlimited duration.

Prior to their respective resignations, Youm Huh and Jason Hartlove were parties to service agreements. Both received compensation packages similar our current executive officers in comparable positions, including similar base salaries, target incentives, and expatriate benefits. As our first Chief Executive Officer, Dr. Huh additionally received a grant of immediately exercisable options to purchase restricted common units of MagnaChip, while Mr. Hartlove received two grants of options to purchase our common units.

**Table of Contents****Outstanding Equity Awards at 2006 Fiscal Year-End**

Name	Option Awards				Stock Awards			Equity Incentive Plan Awards: Market or Payout Value of Unearned Shares, Units or Other Rights That Have Not Vested
	Number of Securities Underlying Options (#) Exercisable	Number of Securities Underlying Unexercised Options (#) Unexercisable	Equity Incentive Plan Awards: Number of Securities Underlying Unexercised Options (#)	Option Exercise Price	Option Expiration Date	Number of Shares or Units That Have Not Vested	Market Value of Shares or Units of Stock That Have Not Vested	
[column a]	[column b]	[column c]	[column d]	(\$)		(#)	(\$)	(#)
Sang Park		800,000(1)		1.02		05/27/16		
Robert J. Krakauer			185,000(2)	1.50		03/09/16	298,483.0625(3)	304,453(4)
Victoria Miller Nam			40,000(2)	1.50		03/09/16	59,696.875(3)	60,891(4)
Tae Young Hwang	153,505.6875	119,393.3125(5)	25,000(2)	cols. b, c: 1.00 col. d: 1.50	cols. b, c: 10/06/14 col. d: 03/09/16			
Chan Hee Lee	153,505.6875	119,393.3125(5)	25,000(2)	cols. b, c: 1.00 col. d: 1.50	cols. b, c: 10/06/14 col. d: 03/09/16			
Jason Hartlove	112,500	187,500(6)	25,000(6)	cols. b, c: 1.00 col. d: 1.50	cols. b, c: 05/16/15 col. d: 03/09/16			
Youm Huh								

## Footnotes:

- (1) An installment of 25% of the common units subject to the options become vested and exercisable on May 27, 2007, and an additional 6.25% of the options vest at the end of each three month period thereafter on the same day of the month as the grant date or, if earlier, the last day of such month.
- (2) An installment of 25% of the common units subject to the options become vested and exercisable upon the earlier of: (i) the date of the first closing of a firmly underwritten public offering for any of our equity securities, and (ii) the date as designated in the sole discretion of the Committee as the date upon which our unitholders as of October 6, 2004, have achieved a 2.5x return on their investment. The remaining 75% of the common units subject to the options become vested and exercisable as to 25% of such common units on each of the first three successive annual anniversaries of the first vesting event, subject to the Grantee's continuous employment from the grant date to each such vesting date.
- (3) Restricted common units received upon the exercise of a fully vested option granted November 30, 2004. The restrictions on the units lapse as to 6.25% of the units on the last day of each calendar quarter.
- (4) There is currently no established public trading market for our outstanding common equity. We determined the reported value based on a third-party fair value appraisal of our common units as of December 31, 2006.
- (5) Installments of 6.25% of the common units subject to the options become vested and exercisable on the last day of each calendar quarter.
- (6) Mr. Hartlove resigned as Senior Vice President and General Manager, Imaging Solutions Division, effective March 9, 2007. The reported unvested option awards terminated upon his resignation date.

**Table of Contents****Option Exercises and Stock Vested for the Fiscal Year Ended December 31, 2006**

Name	Option Awards		Stock Awards	
	Number of Shares Acquired on Exercise (#)	Value Realized on Exercise (\$)	Number of Shares Acquired on Vesting (#)	Value Realized on Vesting (\$)
Sang Park				
Robert J. Krakauer			170,561.75(1)	173,973(2)
Victoria Miller Nam			34,112.50(1)	34,795(2)
Tae Young Hwang				
Chan Hee Lee				
Jason Hartlove				
Youm Huh				

Footnote:

- (1) Restricted common units received upon the exercise of a fully vested option granted November 30, 2004. The restrictions on the units lapsed as to 6.25% of the units on the last day of each calendar quarter of 2006.
- (2) There is currently no established public trading market for our outstanding common equity. We determined the reported value based on a third-party fair value appraisal of our common units as of December 31, 2006.

**Pension Benefits for the Fiscal Year Ended December 31, 2006**

Name	Plan Name	Number of Years of Credited Service (#)	Present Value of Accumulated Benefit (\$) (1)	Payments During the Last Fiscal Year
Sang Park				
Robert J. Krakauer				
Victoria Miller Nam	Statutory Severance	2	56,802	
Tae Young Hwang	Statutory Severance with Multiplier	11	372,573	
Chan Hee Lee	Statutory Severance with Multiplier	10	218,006	
Jason Hartlove				
Youm Huh				

Footnote:

- (1) Actual present value of the accumulated benefit, as if the employment of the named executive officer had been terminated on the last day of our fiscal year ended December 31, 2006.

The only pension benefit that we offered in our fiscal year ended December 31, 2006, is statutory severance. See the section of this Item subtitled "Further Information Regarding Summary Compensation Table and Grants of Plan-Based Awards Table" for a description of the statutory severance benefit.

**Potential Payments Upon Termination or Change-in-Control.**

See the section of this Item above subtitled "Further Information Regarding Summary Compensation Table and Grants of Plan-Based Awards Table" for a description of the potential benefits to our named executive officers upon a termination or change in control.



**Table of Contents****Director Compensation for the Fiscal Year Ended December 31, 2006**

Name	Fees Earned or Paid in Cash (\$)	Stock Awards (\$)	Option Awards (\$)(1)	Non-Equity Incentive Plan Compensation (\$)	Change in Pension Value and Nonqualified Deferred Compensation Earnings	All Other Compensation (\$)	Total (\$)
Jerry M. Baker	50,000					80,956(2)	130,956
Dipanjan Deb							
Armando Geday	50,000		18,373(3)				68,373
Roy Kuan							
R. Douglas Norby	32,849						32,849
Phokion Potamianos							
Paul C. Schorr IV							
David F. Thomas							

## Footnotes:

- (1) We describe the option award calculation method under to SFAS No. 123(R) in Item 8. Financial Statements and Supplementary Data Notes to Consolidated Financial Statements Note 13. Equity Incentive Plan.
- (2) Includes \$19,115 for medical and accident insurance premiums, \$1,841 for life insurance premiums, and \$60,000 for consulting fees, the latter under a separate consulting arrangement effective January 1, 2006.
- (3) The grant date fair value of Mr. Geday's option award is \$55,253.

**Further Information Regarding Director Compensation Table**

Effective January 2006, our Board of Directors began providing director fees to non-employee directors who do not have a current or past affiliation with CVC, Francisco Partners, or CVC Asia. Jerry Baker and Armando Geday each receive \$50,000 per annum for service on our Board of Directors. R. Douglas Norby became our director on May 27, 2006. He receives board fees of \$55,000 per year for his service as a director and Chairman of our Audit Committee. In addition to director fees, effective January 19, 2006, Armando Geday received options to acquire 175,000 of our common units at a purchase price of \$1.04 per unit pursuant to the MagnaChip Semiconductor LLC Equity Incentive Plan. An installment of 25% of the options become exercisable on January 19, 2007, and additional installments of 6.25% of the options become exercisable on the last day of each calendar quarter thereafter. The options expire on the tenth anniversary of the grant date.

Mr. Baker serves as our consultant under a consulting agreement effective January 1, 2006, by and between MagnaChip Korea and Mr. Baker. Under our agreement with Mr. Baker, we pay \$60,000 per year as fees for advisory services regarding business development, marketing, executive recruiting, and strategic direction for the company's products and technology, and Mr. Baker is subject to certain restrictions on competition, solicitation of employees, and competition. The consulting agreement continues indefinitely but may be terminated by either party upon 30 days prior notice.

**Compensation Committee Interlocks and Insider Participation**

The Committee is comprised of directors Dipanjan Deb, Paul Schorr IV, and David Thomas, none of whom has been an officer or employee of the registrant during the last fiscal year. Prior to the Original Acquisition, both Mr. Deb and Mr. Schorr served as officers of the Company. None of our executive officers currently serves, or in the past has served, on the Committee or as a member of the board of directors or compensation committee of any entity that has one or more executive officers serving on the board or compensation committee of MagnaChip.

**Compensation Committee Report**

The Committee has reviewed and discussed the Compensation Discussion and Analysis as set forth above in Executive Compensation Compensation Discussion and Analysis with our management and, based on such review and discussion, has recommended to our Board of Directors that the Compensation Discussion and Analysis be included in this Annual Report on Form 10-K.

Members of the Committee:

Dipanjan Deb

Paul Schorr IV

David Thomas

**Table of Contents****Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.****Securities Authorized for Issuance Under Equity Compensation Plans as of the Fiscal Year Ended December 31, 2006**

<b>Plan category</b>	<b>Number of securities to be issued upon exercise of outstanding options, warrants and rights (a)</b>	<b>Weighted-average price of outstanding options, warrants and rights (b)</b>	<b>Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) (c)</b>
Equity compensation plans approved by security holders	5,069,527.5000	\$ 1.60	674,282.1250
Equity compensation plans not approved by security holders	n/a	n/a	n/a
<b>Total</b>	<b>5,069,527.5000</b>		<b>674,282.1250</b>

The MagnaChip Semiconductor LLC California Equity Incentive Plan and the MagnaChip Semiconductor LLC Equity Incentive Plan each provide for the award of nonstatutory options, unit appreciation rights, or SARs, and restricted unit awards to employees, consultants or non-employee directors of MagnaChip and its subsidiaries. Subject to adjustment in the event of certain corporate transactions or events, the maximum aggregate number of MagnaChip units that are available for grant under both plans is 7,890,864, all of which may be granted under either plan. Units subject to awards that expire, are forfeited or otherwise terminate will again be available for grant under the plans. The plans are administered by our Board of Directors.

The Compensation Committee of our Board of Directors will determine the number of options granted to each participant, the exercise price of each option, the duration of the options (not to exceed ten years), vesting provisions and all other terms and conditions of such options. Unless otherwise determined by the Compensation Committee, the exercise price of each option is required to be not less than the fair market value of the underlying common units subject to the option on the date of grant. The plans provide for payment of the exercise price of options in the form of cash or, subject to the discretion of the Compensation Committee, MagnaChip units. The plans provide that upon a termination of the option-holder's employment or service with MagnaChip or its subsidiaries, unless otherwise determined by the Compensation Committee at or after grant, the exercise period for vested options will be limited, provided that vested options will be cancelled immediately upon a termination for cause.

The Compensation Committee may elect to grant SARs to plan participants and may determine the number of common units subject to the award, the duration of the SARs (not to exceed ten years), vesting provisions and all other terms and conditions of such SARs. In no event may the base price of a SAR be less than the fair market value of the common units subject to the award on the date of grant. A termination of service or employment of the recipient will have the same effect on SARs granted under the plans as on options.

The Compensation Committee will determine the number of restricted units offered to each participant in the plans, the purchase price of the units, the period the units are unvested and subject to forfeiture, the effect of a termination of the recipient's employment or service and all other terms and conditions applicable to the restricted units.

The plans provide that upon a change in control or certain other corporate transactions, the Compensation Committee may, on a holder by holder basis, accelerate the vesting of outstanding options, SARs or restricted units, cancel any unexercised outstanding awards in whole or in part, and/or take actions to ensure that such awards shall be honored or assumed by the successor employer or take such other reasonable actions as the Compensation Committee shall determine.

**Table of Contents****Security Ownership of Certain Beneficial Owners and Management**

The following tables set forth information regarding the beneficial ownership of MagnaChip as of March 1, 2007, by (i) each person or entity known to us to beneficially own more than 5% of any class of outstanding securities of MagnaChip, (ii) each member of our Board of Directors, (iii) each of our named executive officers and (iv) all of the members of our Board of Directors and our executive officers as a group. As of March 1, 2007, MagnaChip's outstanding securities consisted of 52,720,784.047 common units and 93,997.4364 Series B preferred units. The tables do not include common units issuable upon conversion of Series B preferred units.

The amounts and percentages of common units beneficially owned are reported on the basis of SEC regulations governing the determination of beneficial ownership of securities. Under SEC rules, a person is deemed to be a beneficial owner of a security if that person has or shares voting power, which includes the power to vote or to direct the voting of such security, or investment power, which includes the power to dispose of or to direct the disposition of such security. A person is also deemed to be a beneficial owner of any securities of which that person has the right to acquire beneficial ownership within 60 days. Under these rules, more than one person may be deemed to be a beneficial owner of the same securities and a person may be deemed to be a beneficial owner of securities as to which he or she has no economic interest.

Except as indicated by footnote, the persons named in the tables below have sole voting and investment power with respect to all units shown as beneficially owned by them.

**Security Ownership of Certain Beneficial Owners**

Name and Address of Beneficial Owner	Title of Class	Amount and Nature of Beneficial Ownership	Percent of Class
CVC (1)  c/o Court Square Capital Partners  399 Park Avenue, 14th Floor  New York, NY 10022	Common Units	17,962,521.9300	34.1
	Series B Preferred Units	33,716.7546	35.9
Francisco Partners (2)  c/o Francisco Partners, L.P.  Sand Hill Road, Suite 280  Menlo Park, CA 94025	Common Units Series	17,962,521.9200	34.1
	B Preferred Units	33,716.7547	35.9
CVC Asia Pacific (3)  c/o CVC Capital Partners Asia Limited  22 Grenville Street  St. Helier, Jersey JE4 8PX  Channel Islands	Common Units Series	9,659,710.5600	18.3
	B Preferred Units	18,131.8699	19.3
Peninsula Investment Pte. Ltd  255 Shoreline Drive  Suite 600  Redwood City, CA 94065	Common Units Series	3,636,271.0700	6.9
	B Preferred Units	6,825.5041	7.3

---

Footnotes:

- (1) Includes (a) 17,630,628.4200 common units held by Citigroup Venture Capital Equity Partners, L.P., 156,381.7100 common units held by CVC Executive Fund LLC and 175,511.8000 common units held by CVC/SSB Employee Fund, L.P. and (b) 33,093.7702 Series B preferred units held by Citigroup Venture Capital Equity Partners, L.P., 293.5380 Series B preferred units held by CVC Executive Fund LLC and 329.4464 Series B preferred units held by CVC/SSB Employee Fund, L.P.
- (2) Includes (a) 16,941,762.2000 common units held by Francisco Partners, L.P., 83,423.4000 common units held by Francisco Partners Fund A, L.P., 909,067.7600 common units held by FP-MagnaChip Co-Invest, LLC and 28,268.5600 common units held by FP Annual Fund Investors, LLC and (b) 31,800.7261 Series B preferred units held by Francisco Partners, L.P., 156.5909 Series B preferred units held by Francisco Partners Fund A, L.P., 1,706.3760 Series B preferred units held by FP-MagnaChip Co-Invest, LLC and 53.0617 Series B preferred units held by FP Annual Fund Investors, LLC.
- (3) Includes (a) 3,219,903.5200 common units held by CVC Capital Partners Asia Pacific L.P., 4,048,152.3700 common units held by CVC Capital Partners Asia Pacific II L.P., 781,702.9100 common units held by CVC Capital Partners Asia Pacific II Parallel Fund A, L.P. and 1,609,951.7600 common units held by Asia Investors LLC and (b) 6,043.9566 Series B preferred units held by CVC Capital Partners Asia Pacific L.P., 7,598.6306 Series B preferred units held by CVC Capital Partners Asia Pacific II L.P., 1,467.3043 Series B preferred units held by CVC Capital Partners Asia Pacific II Parallel Fund A, L.P. and 3,021.9784 Series B preferred units held by Asia Investors LLC. Asia Investors LLC co-invests alongside of CVC Capital Partners Asia Pacific L.P., but is not a subsidiary of CVC Capital Partners.

**Table of Contents****Security Ownership of Management**

<b>Name and Address of Beneficial Owner</b>	<b>Title of Class</b>	<b>Amount and Nature of Beneficial Ownership</b>	<b>Percent of Class</b>
Jerry M. Baker(1)	Common Units	682,158.1600	1.3
	Series B Preferred Units	255.9564	*
Dipanjjan Deb(2)	Common Units	17,962,521.9200	34.1
	Series B Preferred Units	33,716.7547	35.9
Armando Geday(3)	Common Units	54,687.5000	*
	Series B Preferred Units		
Tae Young Hwang(4)(5)	Common Units	170,561.8750	*
	Series B Preferred Units		
Robert J. Krakauer(4)(6)	Common Units	773,153.7700	1.5
	Series B Preferred Units	170.6375	*
Roy Kuan(7)	Common Units	9,659,710.5600	18.3
	Series B Preferred Units	18,131.8699	19.3
Chan Hee Lee(4)(8)	Common Units	170,561.8750	*
	Series B Preferred Units		
Victoria Miller Nam(4)(9)	Common Units	181,903.3800	*
	Series B Preferred Units	85.3188	*
R. Douglas Norby(10)	Common Units		
	Series B Preferred Units		
Sang Park(4)	Common Units		
	Series B Preferred Units		
Phokion Potamianos(2)	Common Units	17,962,521.9200	34.1
	Series B Preferred Units	33,716.7547	35.9
Paul C. Schorr IV(11)	Common Units	36,362.7200	*
	Series B Preferred Units	68.2551	*
David F. Thomas(12)	Common Units	18,035,247.3400	34.2
	Series B Preferred Units	33,853.2646	36.0
Jason Hartlove(13)	Common Units	131,250.0000	*
	Series B Preferred Units		
Youm Huh(14)	Common Units	773,153.6550	1.5
	Series B Preferred Units	170.6376	*
<b>Directors and executive officers as a group (16 persons)(15)</b>	Common Units	47,795,619.1000	89.9
	Series B Preferred Units	86,282.0570	91.8

\* Less than one percent.

## Footnotes:

- (1) Includes (a) 136,360.1600 common units held by the Baker Family Revocable Trust and 204,674.2500 restricted common units held by Mr. Baker and (b) 255.9564 Series B preferred units held by the Baker Family Revocable Trust. Restricted common units are subject to a right of repurchase by MagnaChip. The address of Mr. Baker is 3101 North First Street, San Jose, CA 95134.
- (2) Includes (a) 16,941,762.2000 common units held by Francisco Partners, L.P., 83,423.4000 common units held by Francisco Partners Fund A, L.P., 909,067.7600 common units held by FP-MagnaChip Co-Invest, LLC and 28,268.5600 common units held by FP Annual Fund Investors, LLC and (b) 31,800.7261 Series B preferred units held by Francisco Partners, L.P., 156.5909 Series B preferred units held by Francisco Partners Fund A, L.P., 1,706.3760 Series B preferred units held by FP-MagnaChip Co-Invest, LLC and 53.0617 Series B preferred units held by FP Annual Fund Investors, LLC. Each of Mr. Deb and Mr. Potamianos is a member of management of Francisco Partners, L.P. and disclaims beneficial ownership of the units held by Francisco Partners, L.P., Francisco Partners Fund A, L.P., FP-MagnaChip Co-Invest, LLC and FP Annual Fund Investors, LLC. The address of each of

## Edgar Filing: MAGNACHIP SEMICONDUCTOR LLC - Form 10-K

Mr. Deb and Mr. Potamianos is c/o Francisco Partners, L.P., 2882 Sand Hill Road, Suite 280, Menlo Park, CA 94025.

- (3) Includes 54,687,5000 common units that Mr. Geday may purchase pursuant to the exercise of options vesting on April 19, 2007. The address of Mr. Geday is 16 Rue de Belzunce, 75010, Paris, France.
- (4) The address of each of Mr. Hwang, Mr. Krakauer, Mr. Lee, Ms. Miller Nam, and Mr. Park is c/o MagnaChip Semiconductor, Ltd., 1 Hyangjeong-dong, Hungduk-gu, Cheongju-si, 361-725, Korea.

**Table of Contents**

- (5) Includes 170,561.8750 common units that Mr. Hwang may purchase pursuant to the exercise of options vesting on March 31, 2007.
- (6) Includes (a) 54,544.0600 common units held jointly by Mr. Krakauer and his spouse, Theresa Krakauer, for which Mr. Krakauer shares voting and investment power with Theresa Krakauer, (b) 36,362.7100 common units held by the Krakauer Family Partnership, for which Mr. Krakauer shares voting and investment power with Theresa Krakauer and (c) 255,842.6250 restricted common units. Restricted common units are subject to a right of repurchase by MagnaChip.
- (7) Includes (a) 3,219,903.5200 common units held by CVC Capital Partners Asia Pacific L.P., 4,048,152.3700 common units held by CVC Capital Partners Asia Pacific II L.P., 781,702.9100 common units held by CVC Capital Partners Asia Pacific II Parallel Fund A, L.P. and 1,609,951.7600 common units held by Asia Investors LLC and (b) 6,043.9566 Series B preferred units held by CVC Capital Partners Asia Pacific L.P., 7,598.6306 Series B preferred units held by CVC Capital Partners Asia Pacific II L.P., 1,467.3043 Series B preferred units held by CVC Capital Partners Asia Pacific II Parallel Fund A, L.P. and 3,021.9784 Series B preferred units held by Asia Investors LLC. Asia Investors LLC co-invests alongside of CVC Capital Partners Asia Pacific L.P., but is not a subsidiary of CVC Capital Partners. Mr. Kuan is a member of management of CVC Asia Pacific Limited, an investment advisor to the general partners of CVC Capital Partners Asia Pacific L.P., CVC Capital Partners Asia Pacific II L.P. and CVC Capital Partners Asia Pacific II Parallel Fund A, L.P. and to Asia Investors LLC. Mr. Kuan disclaims beneficial ownership of the units held by these entities. The address of Mr. Kuan is c/o CVC Capital Partners Asia II Limited, 22 Grenville Street, St. Helier, Jersey JE4 8PX, Channel Islands.
- (8) Includes 170,561.8750 common units that Mr. Lee may purchase pursuant to the exercise of options vesting on March 31, 2007.
- (9) Includes 51,168.7500 restricted common units that are subject to a right of repurchase by MagnaChip.
- (10) The address of Mr. Norby is 12169 Hilltop Drive, Los Altos Hills, CA 94024.
- (11) Includes (a) 29,544.7100 common units held by BG Partners LP and 6,818.0100 common units held by BG/CVC-1 and (b) 55.4573 Series B preferred units held by BG Partners LP and 12.7978 Series B preferred units held by BG/CVC-1. The address of Mr. Schorr is c/o The Blackstone Group, 345 Park Avenue, New York, NY 10154.
- (12) Includes (a) 17,630,628.4200 common units held by Citigroup Venture Capital Equity Partners, L.P., 156,381.7100 common units held by CVC Executive Fund LLC and 175,511.8000 common units held by CVC/SSB Employee Fund, L.P. and (b) 33,093.7702 Series B preferred units held by Citigroup Venture Capital Equity Partners, L.P., 293.5380 Series B preferred units held by CVC Executive Fund LLC and 329.4464 Series B preferred units held by CVC/SSB Employee Fund, L.P. Mr. Thomas is a member of management of Citigroup Venture Capital Equity Partners, L.P. and disclaims beneficial ownership of the units held by Citigroup Venture Capital Equity Partners, L.P., CVC Executive Fund LLC and CVC/SSB Employee Fund, L.P. The address of Mr. Thomas is c/o Citigroup Venture Capital Equity Partners, L.P., 399 Park Avenue, 14th Floor, New York, NY 10022.
- (13) Includes 131,250.0000 common units that Mr. Hartlove may purchase pursuant to the exercise of options vesting on February 16, 2007. Mr. Hartlove's option to purchase these units terminates on May 8, 2007, if not exercised before that date. The address of Mr. Hartlove is 1943 Alford Ave., Los Altos, CA 94024.
- (14) The address of Dr. Huh is Misung Apt., 414 Apgujong-dong, Gangnam-gu, Seoul, Korea.
- (15) Excludes Youm Huh, who resigned as Chief Executive Officer, President, and Director effective May 27, 2006, and Jason Hartlove, who resigned as Senior Vice President and General Manager, Imaging Solutions Division, effective March 9, 2007.



**Table of Contents**

**Item 13. Certain Relationships and Related Transactions, and Director Independence.**

**ADVISORY AGREEMENTS**

In connection with the Original Acquisition, and the related equity financing, MagnaChip Korea and MagnaChip entered into advisory agreements with each of CVC Management LLC, Francisco Partners Management, LLC and CVC Capital Partners Asia Limited, which are related to CVC, Francisco Partners and CVC Asia Pacific, respectively, pursuant to which each may provide financial, advisory and consulting services to MagnaChip Korea and MagnaChip. Under such agreements, each of CVC Management, Francisco Partners Management and CVC Capital Partners Asia is entitled to receive fees billed at such firm's customary rates for actual time spent performing such services plus reimbursement for out-of-pocket expenses or, at such firm's option and upon certain conditions, an annual advisory fee, the amount of which is the greater of a fixed dollar amount or a percentage of the annual consolidated revenue of MagnaChip Korea and MagnaChip for the last twelve months, plus out-of-pocket expenses, for the remaining term of the advisory agreement. The annual advisory fees under the agreements are as follows: CVC Management and Francisco Partners Management are each entitled to the greater of \$1,379,163.42 or 0.14777% of annual consolidated revenue and CVC Capital Partners Asia is entitled to the greater of \$741,673.15 or 0.07946% of annual consolidated revenue. There are no minimum levels of service required to be provided pursuant to the advisory agreements. Each advisory agreement has an initial term of ten years from the date of the Original Acquisition, subject to termination by either party upon written notice 90 days prior to the expiration of the initial term or any extension thereof. Each advisory agreement includes customary indemnification provisions in favor of each of CVC Management, Francisco Partners Management and CVC Capital Partners Asia. In exchange for an extension of the initial term of these advisory agreements for a period of one year, each of the three advisors under these advisory agreements agreed to waive all fees accruing in our fiscal year 2006.

**RELATED PARTY TRANSACTIONS**

Under our Code of Business Conduct and Ethics, all conflicts of interest and related-party transactions that are determined to be material by the Chief Financial Officer must be reviewed and approved in writing by our audit committee. All conflicts of interest and related-party transactions involving our directors or executive officers must be reviewed and approved in writing by our full Board of Directors. In the approval process, the approving authority will review all aspects of the conflict of interest or related-party transaction, including but not limited to, (i) compliance with laws, rules, and regulations, (ii) the adverse affect on our business and results of operations, (iii) the adverse affect on our relationships with third parties such as customers, vendors, and potential investors, (iii) the benefit to the director, officer, or employee at issue, and (iv) the creation of morale problems among other employees.

The securityholders' agreement executed by and among us, CVC, Francisco Partners, CVC Asia Pacific and other securityholders of MagnaChip provides that our Board of Directors must approve any contract with, obligation to or transaction or series of transactions between, us and one or more of our securityholders or their affiliates.

**Table of Contents****DIRECTOR INDEPENDENCE**

We are not a listed issuer. For purposes of determining whether our directors are independent under this Item 13, we apply the definition of director independence as set forth in the Rules of The NASDAQ Stock Market LLC. The following directors marked with an asterisk ( \* ) are independent under the Rules with respect to our Board of Directors and each board committee.

<b>Board of Directors</b>	<b>Audit Committee</b>	<b>Compensation Committee</b>	<b>Nominating and Governance Committee</b>
Jerry M. Baker	R. Douglas Norby*	Dipanjan Deb	R. Douglas Norby*
Dipanjan Deb	Phokion Potamianos	Paul C. Schorr IV	Phokion Potamianos
Armando Geday	Paul C. Schorr IV	David F. Thomas	David F. Thomas
Youm Huh (1)			
Robert Krakauer			
Roy Kuan			
R. Douglas Norby*			
Sang Park			
Phokion Potamianos			
Paul C. Schorr IV			
David F. Thomas			

Footnote:

(1) Dr. Huh resigned as a director effective May 27, 2006.

**Item 14. Principal Accounting Fees and Services.****Audit fees and services**

The following table presents fees for professional services rendered by Samil PricewaterhouseCoopers and its affiliates for the years ended December 31, 2006 and 2005. Audit related fees paid in 2005 were for assurance services provided by Samil PricewaterhouseCoopers associated with S-4 filing. Tax services provided by Samil PricewaterhouseCoopers in 2005 were primarily related to a transfer price study for intercompany transactions.

	<b>Year ended December 31</b>	
	<b>2006</b>	<b>2005</b>
	<i>(in millions of US dollars)</i>	
Audit fees	\$ 1.3	\$ 1.3
Audit related fees		0.4

Tax fees	0.5
All other fees	

**Policy and procedure for approval of audit and permitted non-audit services**

All audit, audit-related and tax services were pre-approved by the Company's Audit Committee, which concluded that the provision of such services by Samil PricewaterhouseCoopers and its affiliates was compatible with the maintenance of that firm's independence in the conduct of its auditing functions. The Audit Committee's Outside Auditor Independence Policy provides for pre-approval of specifically described audit, audit-related, non-audit related and tax services by the Committee on an annual basis. Individual engagements must be separately approved. The policy also requires specific approval by the Committee if total fees for audit-related and tax services would exceed total fees for audit services in any fiscal year. The policy authorizes the Committee to delegate to one or more of its members pre-approval authority with respect to permitted services that will be ratified by the entire Audit Committee at a future committee meeting in accordance with requirements of the SEC. In 2005 and 2006, the Audit Committee followed these guidelines in approving all services rendered by Samil PricewaterhouseCoopers and its affiliates.

**Table of Contents**

**PART IV**

**Item 15. Exhibits and Financial Statement Schedules**

(a) The following documents are filed as part of this report:

1. Financial Statements: See Index to Consolidated Financial Statements under Item 8.
2. Financial Statement Schedules are omitted because of the absence of the conditions under which they are required or because the information required by such omitted schedules is set forth in the financial statements or the notes thereto.
3. Exhibits.

(b) Exhibits

- 2.1 Business Transfer Agreement, dated as of June 12, 2004, between Hynix Semiconductor Inc. and MagnaChip Semiconductor, Ltd. (Korea)(1)
- 2.2 First Amendment to Business Transfer Agreement, dated as of October 6, 2004, between Hynix Semiconductor Inc. and MagnaChip Semiconductor, Ltd. (Korea)(1)
- 3.1 Certificate of Formation of MagnaChip Semiconductor LLC (formerly System Semiconductor Holding LLC)(1)
- 3.2 Certificate of Amendment to Certificate of Formation of MagnaChip Semiconductor LLC(1)
- 3.3 Third Amended and Restated Limited Liability Company Operating Agreement of MagnaChip Semiconductor LLC(1)
- 3.4 Articles of Incorporation of MagnaChip Semiconductor S.A.(1)
- 3.5 Certificate of Incorporation of MagnaChip Semiconductor Finance Company(1)
- 3.6 Bylaws of MagnaChip Semiconductor Finance Company(1)
- 3.7 Certificate of Formation for MagnaChip Semiconductor SA Holdings LLC(1)
- 3.8 Limited Liability Company Agreement of MagnaChip Semiconductor SA Holdings LLC(1)
- 3.9 Deed of Amendment to the Articles of Association of MagnaChip Semiconductor B.V. (English translation)(1)
- 3.12 Articles of Incorporation of MagnaChip Semiconductor, Ltd. (Korea)(1)
- 3.14 Memorandum of Association of MagnaChip Semiconductor Ltd. (Hong Kong)(1)
- 3.15 Articles of Association of MagnaChip Semiconductor Ltd. (Hong Kong)(1)
- 3.16 Memorandum of Association of MagnaChip Semiconductor Ltd. (United Kingdom)(1)
- 3.17 Articles of Association of MagnaChip Semiconductor Ltd. (United Kingdom)(1)
- 3.18 Articles of Incorporation of MagnaChip Semiconductor Ltd. (Taiwan) (English translation)(1)
- 3.19 Merger Agreement by and between ISRON Corporation and MagnaChip Semiconductor Inc. dated December 21, 2005, as amended on February 22, 2006, including Articles of Incorporation of MagnaChip Semiconductor Inc. (formerly ISRON Corporation) (Japan) (English translation)(2)
- 3.21 Bylaws of MagnaChip Semiconductor, Inc. (formerly IC Media Corporation)(1)
- 3.22 Certificate of Amendment to the Bylaws of MagnaChip Semiconductor, Inc. (formerly IC Media Corporation)(1)

**Table of Contents**

3.23	Certificate of Amendment to the Bylaws of MagnaChip Semiconductor, Inc. (formerly IC Media Corporation)(1)
3.24	Memorandum of Association of IC Media International Corporation(1)
3.25	Articles of Association of IC Media International Corporation(1)
3.26	Memorandum of Association of MagnaChip Semiconductor Holding Company Limited (formerly IC Media Holding Company Limited)(1)
3.27	Articles of Association of MagnaChip Semiconductor Holding Company Limited (formerly IC Media Holding Company Limited)(1)
3.27.a	Amendment to Memorandum and Articles of Association of MagnaChip Semiconductor Holding Company Limited (formerly IC Media Holding Company Limited)(2)
3.28	Articles of Incorporation of IC Media Technology Corporation (English translation)(1)
3.29	Agreement and Plan of Merger by and between IC Media Corporation and MagnaChip Semiconductor, Inc., including Amended and Restated Articles of Incorporation, as filed with the State of California Secretary of State on November 17, 2005, and as corrected on February 6, 2006(2)
4.1	Indenture, dated as of December 23, 2004, among MagnaChip Semiconductor S.A., MagnaChip Semiconductor Finance Company, the guarantors as named therein and The Bank of New York, as trustee for the Floating Rate Second Priority Senior Secured Notes due 2011 and the 6 <sup>7</sup> / <sub>8</sub> % Second Priority Senior Secured Notes due 2011(1)
4.2	Form of Floating Rate Second Priority Senior Secured Notes due 2011 and related guarantees (included in Exhibit 4.1)(1)
4.3	Form of 6 <sup>7</sup> / <sub>8</sub> % Second Priority Senior Secured Notes due 2011 and related guarantees (included in Exhibit 4.1)(1)
4.4	Registration Rights Agreement, dated as of December 23, 2004, by and among MagnaChip Semiconductor S.A., MagnaChip Semiconductor Finance Company, the guarantors named therein, UBS Securities LLC, Citigroup Global Markets Inc., Goldman, Sachs & Co., J.P. Morgan Securities Inc. and Deutsche Bank Securities Inc.(1)
4.5	Indenture, dated as of December 23, 2004, among MagnaChip Semiconductor S.A., MagnaChip Semiconductor Finance Company, the guarantors as named therein and The Bank of New York, as trustee for the 8% Senior Subordinated Notes due 2014(1)
4.6	Form 8% Senior Subordinated Notes due 2014 and related guarantees (included in Exhibit 4.5)(1)
4.7	Registration Rights Agreement, dated as of December 23, 2004, by and among MagnaChip Semiconductor S.A., MagnaChip Semiconductor Finance Company, the guarantors named therein, UBS Securities LLC, Citigroup Global Markets Inc., Goldman, Sachs & Co., J.P. Morgan Securities Inc. and Deutsche Bank Securities Inc.(1)
10.1	Purchase Agreement, dated as of December 16, 2004, among MagnaChip Semiconductor S.A., MagnaChip Semiconductor Finance Company, UBS Securities LLC, Citigroup Global Markets Inc., Goldman, Sachs & Co., J.P. Morgan Securities Inc. and Deutsche Bank Securities Inc.(1)
10.2	Credit Agreement, dated as of December 23, 2004, among MagnaChip Semiconductor S.A., MagnaChip Semiconductor Finance Company, the guarantors named therein, the lenders named therein, UBS Securities LLC, Korea Exchange Bank, UBS AG, Stamford Branch and UBS Loan Finance LLC(1)

**Table of Contents**

- 10.3.a First Amendment to Credit Agreement and Waiver, dated as of May 6, 2005, to the Credit Agreement, dated as of December 23, 2004, among MagnaChip Semiconductor S.A., MagnaChip Semiconductor Finance Company, the guarantors named therein, the lenders named therein, UBS Securities LLC, Korea Exchange Bank, UBS AG, Stamford Branch and UBS Loan Finance LLC(1)
- 10.3.b Second Amendment to Credit Agreement and Waiver dated as of June 21, 2005, to the Credit Agreement, dated as of December 23, 2004, among MagnaChip Semiconductor S.A., MagnaChip Semiconductor Finance Company, the guarantors named therein, the lenders named therein, UBS Securities LLC, Korea Exchange Bank, UBS AG, Stamford Branch and UBS Loan Finance LLC(1)
- 10.3.c Third Amendment to Credit Agreement dated as of March 27, 2006, to the Credit Agreement, dated as of December 23, 2004, among MagnaChip Semiconductor S.A., MagnaChip Semiconductor Finance Company, the guarantors named therein, the lenders named therein, UBS Securities LLC, Korea Exchange Bank, UBS AG, Stamford Branch and UBS Loan Finance LLC(2)
- 10.3.d Fourth Amendment to Credit Agreement, dated as of July 26, 2006, by and among MagnaChip Semiconductor S.A. and MagnaChip Semiconductor Finance Company, as borrowers, MagnaChip Semiconductor LLC, the Subsidiary Guarantors party thereto, the Lenders party thereto, UBS AG, Stamford Branch, as administrative agent and collateral agent, and U.S. Bank National Association(3)
- 10.3.e Fifth Amendment to Credit Agreement, dated as of December 29, 2006, by and among MagnaChip Semiconductor S.A. and MagnaChip Semiconductor Finance Company, as borrowers, MagnaChip Semiconductor LLC, the Subsidiary Guarantors party thereto, the Lenders party thereto, and UBS AG, Stamford Branch, as administrative agent and collateral agent(4)
- 10.3.f Sixth Amendment to Credit Agreement dated as of March 26, 2007, by and among MagnaChip Semiconductor S.A. and MagnaChip Semiconductor Finance Company, as borrowers, MagnaChip Semiconductor LLC, the Subsidiary Guarantors party thereto, the Lenders party thereto, and UBS AG, Stamford Branch, as administrative agent and collateral agent.
- 10.4 Intercreditor Agreement dated as of December 23, 2004 among MagnaChip Semiconductor Finance Company, the other Pledgors party thereto, UBS AG, Stamford Branch, The Bank of New York and U.S. Bank National Association(1)
- 10.5 Second Amended and Restated Securityholders Agreement of MagnaChip Semiconductor LLC(1)
- 10.6 Warrant held by Hynix Semiconductor Inc. to purchase common units of MagnaChip Semiconductor LLC(1)
- 10.7 Intellectual Property License Agreement, dated as of October 6, 2004, by and between Hynix Semiconductor Inc. and MagnaChip Semiconductor, Ltd. (Korea)(1)
- 10.8 Trademark License Agreement, dated as of October 6, 2004, by and between Hynix Semiconductor Inc. and MagnaChip Semiconductor, Ltd. (Korea)(1)
- 10.9 Building Lease Agreement for Warehouses, dated as of October 6, 2004, by and between Hynix Semiconductor Inc. and MagnaChip Semiconductor, Ltd. (Korea)(1)
- 10.9.a First Amendment to Building Lease Agreement for Warehouses, dated as of December 30, 2005, by and between Hynix Semiconductor Inc. and MagnaChip Semiconductor, Ltd. (Korea)(2)
- 10.10 Building Lease Agreement for M4 Building, dated as of October 6, 2004, by and between Hynix Semiconductor Inc. and MagnaChip Semiconductor, Ltd. (Korea)(1)(5)
- 10.11 Building Lease Agreement for R, C1 and C2 Buildings, dated as of October 6, 2004, by and between Hynix Semiconductor Inc. and MagnaChip Semiconductor, Ltd. (Korea)(1)
- 10.11.a First Amendment to Building Lease Agreement for R, C1 and C2 Buildings, dated as of December 30, 2005, by and between Hynix Semiconductor Inc. and MagnaChip Semiconductor, Ltd. (Korea)(2)

**Table of Contents**

10.12	Land Lease and Easement Agreement, dated as of October 6, 2004, by and between Hynix Semiconductor Inc. and MagnaChip Semiconductor, Ltd. (Korea)(1)(5)
10.12.a	First Amendment to Land Lease and Easement Agreement, dated as of December 30, 2005, by and between Hynix Semiconductor Inc. and MagnaChip Semiconductor, Ltd. (Korea)(2)
10.13	Wafer Foundry Service Agreement, dated as of October 6, 2004, by and between Hynix Semiconductor Inc. and MagnaChip Semiconductor, Ltd. (Korea)(1)(5)
10.14	Wafer Mask Production and Supply Agreement, dated as of October 6, 2004, by and between Hynix Semiconductor Inc. and MagnaChip Semiconductor, Ltd. (Korea)(1)(5)
10.14.a	First Amendment to Wafer Mask Production and Supply Agreement, dated as of December 30, 2005, by and between Hynix Semiconductor Inc. and MagnaChip Semiconductor, Ltd. (Korea)(2)(6)
10.15	General Service Supply Agreement, dated as of October 6, 2004, by and between Hynix Semiconductor Inc. and MagnaChip Semiconductor, Ltd. (Korea)(1)
10.15.a	First Amendment to General Service Supply Agreement, dated as of December 30, 2005, by and between Hynix Semiconductor Inc. and MagnaChip Semiconductor, Ltd. (Korea)(2)
10.16	IT and FA Service Agreement, dated as of October 6, 2004, by and between Hynix Semiconductor Inc. and MagnaChip Semiconductor, Ltd. (Korea)(1)
10.16.a	First Amendment to IT and FA Service Agreement, dated as of December 30, 2005, by and between Hynix Semiconductor Inc. and MagnaChip Semiconductor, Ltd. (Korea)(2)
10.17	Service Agreement, dated as of October 6, 2004, by and between MagnaChip Semiconductor, Ltd. (Korea) and Youm Huh(1)
10.18	Service Agreement, dated as of October 1, 2004, by and between MagnaChip Semiconductor, Ltd. (Korea) and Jerry Baker(1)
10.19	Service Agreement, dated as of October 6, 2004, by and between MagnaChip Semiconductor, Ltd. (Korea) and Robert Krakauer(1)
10.20	Service Agreement, dated as of December 29, 2004, by and between MagnaChip Semiconductor, Ltd. (Korea) and Victoria Miller Nam(1)
10.21	Service Agreement, dated as of October 6, 2004, by and between MagnaChip Semiconductor, Ltd. (Korea) and Tae Young Hwang(1)
10.22	Service Agreement, dated as of May 16, 2005, by and among MagnaChip Semiconductor, Ltd. (Korea), MagnaChip Semiconductor, Inc. (California) and Jason Hartlove(1)
10.23	Service Agreement, dated as of April 14, 2005 by and between MagnaChip Semiconductor, Ltd. (Korea) and Dale Lindly(1)
10.24	MagnaChip Semiconductor LLC Equity Incentive Plan(1)
10.25	MagnaChip Semiconductor LLC California Equity Incentive Plan(1)
10.26	R&D Equipment Utilization Agreement, dated as of October 6, 2004, by and between Hynix Semiconductor Inc. and MagnaChip Semiconductor, Ltd. (Korea)(1)(5)
10.26.a	First Amendment to R&D Equipment Utilization Agreement, dated as of December 30, 2005, by and between Hynix Semiconductor Inc. and MagnaChip Semiconductor, Ltd. (Korea)(2)
10.27	License Agreement (ModularBCD), dated as of March 18, 2005, by and between Advanced Analogic Technologies, Inc. and MagnaChip Semiconductor, Ltd. (Korea)(1)(5)

**Table of Contents**

10.28	License Agreement (TrenchDMOS), dated as of March 18, 2005, by and between Advanced Analogic Technologies, Inc. and MagnaChip Semiconductor, Ltd. (Korea)(1)(5)
10.29	RFID Development and Licensing Agreement, dated as of March 29, 2004, by and between Celis Semiconductor Corporation and MagnaChip Semiconductor, Ltd. (Korea) (successor in interest to Hynix Semiconductor Inc.)(1)(5)
10.30	Technology License Agreement, dated as of July 2001, by and between ARM Limited and MagnaChip Semiconductor, Ltd. (Korea) (successor in interest to Hynix Semiconductor Inc.)(1)(5)
10.31	Technology License Agreement, dated as of December 16, 1996, by and between Advanced RISC Machines Limited and MagnaChip Semiconductor, Ltd. (Korea) (successor in interest to LG Semicon Company Limited)(1)(5)
10.32	ARM7201TDSP Device License Agreement, dated as of August 26, 1997, by and between Advanced RISC Machines Limited and MagnaChip Semiconductor, Ltd. (Korea) (successor in interest to LG Semicon Company Limited)(1)(5)
10.33	Technology License Agreement, dated as of August 22, 2001, by and between ARM Limited and MagnaChip Semiconductor, Ltd. (Korea) (successor in interest to Hynix Semiconductor Inc.)(1)(5)
10.34	Technology License Agreement, dated as of May 20, 2004, by and between ARM Limited and MagnaChip Semiconductor, Ltd. (Korea) (successor in interest to Hynix Semiconductor Inc.)(1)
10.35	Interest Rate Swap Transaction Letter Agreement, dated as of June 30, 2005, by and between MagnaChip Semiconductor S.A. and Deutsche Bank AG(7)
10.36	Service Agreement, dated as of May 27, 2006, by and between MagnaChip Semiconductor, Ltd. (Korea) and Sang Park(8)
10.37	Consulting Agreement, dated as of January 1, 2006, by and between MagnaChip Semiconductor, Ltd. (Korea) and Jerry Baker
21.1	Subsidiaries of MagnaChip Semiconductor LLC
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.

Footnotes:

- (1) Incorporated by reference to identically numbered exhibits filed in response to Item 21(a), Exhibits, of the Company's Registration Statement on Form S-4, as amended (File No. 33-126019), which became effective July 20, 2005.
- (2) Incorporated by reference to an identically numbered exhibit filed in response to Item 15, Exhibits, Financial Statement Schedules and Reports on Form 8-K, of the Company's Annual Report on Form 10-K for the period ended December 31, 2005 filed on March 31, 2006 (File No. 33-126019-09).
- (3) Incorporated by reference to an identically numbered exhibit filed in response to Item 9.01, Financial Statements and Exhibits, of the Company's Current Report on Form 8-K dated July 25, 2006 (File No. 33-126019-09).
- (4) Incorporated by reference to an identically numbered exhibit filed in response to Item 9.01, Financial Statements and Exhibits, of the Company's Current Report on Form 8-K dated December 29, 2006 (File No. 33-126019-09).



**Table of Contents**

- (5) Certain portions of this document have been omitted and granted confidential treatment by the SEC.
- (6) Certain portions of this document have been omitted pursuant to a confidential treatment request.
- (7) Incorporated by reference to an identically numbered exhibit filed in response to Item 6, Exhibits, of the Company's Quarterly Report on Form 10-Q for the quarter ended July 3, 2005 (File No. 33-126019-09).
- (8) Incorporated by reference to an identically numbered exhibit filed in response to Item 9.01, Financial Statements and Exhibits, of the Company's Current Report on Form 8-K dated May 27, 2006 (File No. 33-126019-09).
- (c) Financial Statement Schedules:

Schedules are omitted because of the absence of the conditions under which they are required or because the information required by such omitted schedules is set forth in the financial statements or the notes thereto.

**Table of Contents****SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) 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 LLC**

Dated: March 29, 2007

By: /s/ SANG PARK  
Sang Park

**Chief Executive Officer and Chairman**

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

<b>Signature</b>	<b>Title</b>	<b>Date</b>
/s/ SANG PARK <b>Sang Park</b>	Chief Executive Officer and Chairman of the Board of Directors (Principal Executive Officer)	March 29, 2007
/s/ ROBERT J. KRAKAUER <b>Robert J. Krakauer</b>	President, Chief Financial Officer and Director (Principal Financial Officer)	March 29, 2007
/s/ MARGARET SAKAI <b>Margaret Sakai</b>	Senior Vice President, Finance (Principal Accounting Officer)	March 29, 2007
/s/ JERRY M. BAKER <b>Jerry M. Baker</b>	Director	March 29, 2007
/s/ DIPANJAN DEB <b>Dipanjan Deb</b>	Director	March 29, 2007
/s/ ARMANDO GEDAY <b>Armando Geday</b>	Director	March 29, 2007
/s/ ROY KUAN <b>Roy Kuan</b>	Director	March 29, 2007
/s/ PHOKION POTAMIANOS <b>Phokion Potamianos</b>	Director	March 29, 2007
/s/ R. DOUGLAS NORBY <b>R. Douglas Norby</b>	Director	March 29, 2007

Edgar Filing: MAGNACHIP SEMICONDUCTOR LLC - Form 10-K

/s/ PAUL C. SCHORR IV	Director	March 29, 2007
<b>Paul C. Schorr IV</b>		
/s/ DAVID F. THOMAS	Director	March 29, 2007
<b>David F. Thomas</b>		

104