



**COUNCIL OF
THE EUROPEAN UNION**

**Brussels, 28 March 2008
(OR. en)**

7471/08

**ANTIDUMPING 39
COMER 54
COREE 3**

LEGISLATIVE ACTS AND OTHER INSTRUMENTS

Subject: COUNCIL REGULATION repealing the countervailing duty imposed on imports of certain electronic microcircuits known as DRAMs (Dynamic Random Access Memories) originating in the Republic of Korea and terminating the proceeding

COUNCIL REGULATION (EC) No .../...

of

**repealing the countervailing duty imposed on
imports of certain electronic microcircuits known as DRAMs
(Dynamic Random Access Memories)
originating in the Republic of Korea
and terminating the proceeding**

THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty establishing the European Community,

Having regard to Council Regulation (EC) No 2026/97 of 6 October 1997 on protection against subsidised imports from countries not members of the European Community¹ (the "basic Regulation") and in particular Article 19 thereof,

Having regard to the proposal submitted by the Commission after consulting the Advisory Committee,

¹ OJ L 288, 21.10.1997, p. 1. Regulation as last amended by Regulation (EC) No 461/2004 (OJ L 77, 13.3.2004, p. 12).

Whereas:

A. PROCEDURE

I. Existing measures

- (1) By Regulation (EC) No 1480/2003¹ (the "definitive duty Regulation"), the Council imposed a definitive countervailing duty of 34,8 % on imports of certain electronic microcircuits known as Dynamic Random Access Memories ("DRAMs") originating in the Republic of Korea and manufactured by all companies other than Samsung Electronics Co., Ltd ("Samsung"), for which a 0 % duty rate was established. The definitive duty Regulation was preceded by Commission Regulation (EC) No 708/2003 imposing a provisional countervailing duty on imports of DRAMs originating in the Republic of Korea² (the "provisional duty Regulation").
- (2) Following a report adopted by the Dispute Settlement Body of the World Trade Organisation³ (the "*EC-Korea DRAMs Panel Report*"), the Council adopted Regulation (EC) No 584/2006⁴, implementing the recommendations made by the Panel Report and lowering the definitive countervailing duty to 32,9 % (the "implementing Regulation").

¹ OJ L 212, 22.8.2003, p. 1. Regulation as amended by Regulation (EC) No 2116/2005, OJ L 340, 23.12.2005, p. 7.

² OJ L 102, 24.4.2003, p. 7.

³ WT/DS299/R *European Communities – Countervailing Measures on Dynamic Random Access Memory Chips from Korea*, adopted on 3 August 2005.

⁴ OJ L 103, 12.4.2006, p. 1.

II. *Ex Officio* initiation of a partial interim review

- (3) The Community producers Micron Europe Ltd and Qimonda AG (formerly, Infineon Technologies AG) provided *prima facie* evidence to the Commission indicating that Hynix Semiconductor Inc. ("Hynix") was in receipt of additional subsidies in the period following the investigation period of the original investigation. Additionally, Hynix submitted a request for a partial interim review alleging that the subsidies found to be countervailable in the original investigation had ceased to exist.
- (4) In view of the submissions above, the Commission decided to proceed *ex officio*.

III. Investigation

- (5) Having determined that sufficient evidence existed to justify the initiation of a partial interim review and having consulted the Advisory Committee, the Commission announced on 18 March 2006, by a Notice of Initiation published in the *Official Journal of the European Union*¹, the *ex officio* initiation of a partial interim review, in accordance with Article 19 of the basic Regulation.
- (6) The review was limited in scope to the examination of subsidisation of one exporting producer, Hynix, in order to assess the need for the continuation, removal or amendment of the existing measures. The investigation period ran from 1 January 2005 to 31 December 2005 ("IP").

¹ OJ C 67, 18.3.2006, p. 16.

- (7) The Commission officially advised the exporting producer concerned (Hynix), the Government of the Republic of Korea (the "GOK") and the Community producers of the initiation of the partial interim review. Interested parties were given the opportunity to make their views known in writing and to request a hearing within the time limits set out in the Notice of Initiation.
- (8) In order to obtain the information necessary for its investigation, the Commission sent questionnaires to all parties known to be concerned and received replies from the company, the GOK and a number of Korean banks, as well as Deutsche Bank AG.
- (9) The Commission sought to verify the information received and carried out verification visits at the premises of the GOK (Ministry of Finance and Economy – "MOFE" and the Financial Supervisory Commission – "FSC") and the following companies and institutions in Seoul:

Hynix Semiconductor Inc.

Korea Exchange Bank ("KEB")

Korea Development Bank ("KDB")

Woori Bank

Shinhan Bank

Deutsche Bank AG

National Agricultural Cooperative Federation ("NACF")

Hyundai Marine & Fire Insurance

B. PRODUCT UNDER CONSIDERATION AND LIKE PRODUCT

- (10) The product under consideration and the like product are the same as that covered in the original investigation, i.e., certain electronic microcircuits known as Dynamic Random Access Memories ("DRAMs") of all types, densities and variations, whether assembled, in processed wafer or chips (dies), manufactured using variations of Metal Oxide-Semiconductors ("MOS") process technology, including complementary MOS types ("CMOS"), of all densities (including future densities), irrespective of access speed, configuration, package or frame etc., originating in the Republic of Korea. The product concerned also includes DRAMs presented in (non-customised) memory modules or (non-customised) memory boards or in some other kind of aggregate form provided the main purpose of which is to provide memory.
- (11) The product concerned is currently classifiable within CN codes ex 8473 30 20, ex 8473 50 20, ex 8542 32 10, ex 8542 32 31, ex 8542 32 39 and ex 8548 90 20.

C. SUBSIDIES

I. Introduction

- (12) On the basis of the information available to the Commission at initiation and the replies given to the Commission's questionnaires, the following measures were investigated:
- (a) a rescue package approved by the Hynix Creditors' and Financial Institutions Council ("CFIC") on 30 December 2002 (the "new restructuring"), comprising a debt-to-equity swap, a debt rollover and changes in the interest payment conditions;
 - (b) alleged preferential financing provided by Korean banks to Beijing Orient Electronics ("BOE") to facilitate the purchase of Hydis, a Hynix operation;
 - (c) alleged preferential financing provided by Korean banks to CVC to facilitate the purchase of System IC, a Hynix operation, including the transfer of Hynix debt to another entity at a discount;
 - (d) a discounted cash buyout of the Hynix debt;
 - (e) preferential tax treatment allegedly given to Hynix by GOK;
 - (f) the July 2005 refinancing of Hynix debt.

- (13) All the measures listed above were *ad hoc* measures. With the exception of (e) above, all investigated measures were taken by the creditor banks/institutions of Hynix, allegedly under direction by the GOK. The issue of "financial contribution by a government", within the meaning of Article 2 of the basic Regulation, is, as in the original investigation, central to this proceeding and recitals (9) to (15) of the definitive duty Regulation are hereby recalled.

II. The financial situation of Hynix after the original investigation

- (14) Despite the large bail-out packages received by Hynix in 2001, its financial situation did not improve and in 2002 it was still rated Selective Default by Standard & Poor. It reported a loss of KRW 1,03 trillion for the first nine months of 2002; it was obvious that it was in no position to pay any maturing debt. Its ratios, based on its 2002 financial statement, show that it could not cover its current liabilities with current assets, could not cover its interest expense with its earning, was financed with significantly more debt than equity and had large net losses. Although the October 2001 bailout had helped matters to some degree, the company was still in considerable distress. Morgan Stanley Dean Witter, one of Hynix's external advisors, in a report produced in September 2002, stated that Hynix would be very unlikely to "accumulate enough cash in the next two years to meet maturing debt obligations" or "expand capacity and fund the technological upgrades and R&D necessary for it to remain a competitive DRAM producer." Morgan Stanley Dean Witter went on to say that "Hynix is technically bankrupt, kept alive only through debt restructuring programmes" and that "The financial commitment required to bring the company back to a competitive level looks too great. Creditors cannot afford to nurse the company back to health. Whatever the outcome, the message is clear to investors: Hynix is not an investment grade company."

- (15) Merrill Lynch, again in September 2002, stated that: "We are increasingly concerned about Hynix's dismal earnings prospects. We are cutting 02-03 estimates into deficit territory as cost improvements and supply growth is constrained by lack of investment in the process technology upgrade". Another one of Hynix's advisors, Deutsche Bank Korea, admitted that their equities department, although it followed the semiconductor industry, did not follow Hynix, as "there was a lack of investor appetite". The company itself does not dispute the severity of its financial difficulties at the relevant time.

III. The New Restructuring

- (16) In October 2001, a business normalisation plan was adopted by the CFIC to pursue the reconstruction of the company. The CFIC was made up of banks and other institutions which were Hynix's creditors. The decisions of the CFIC were taken by a 75 % majority. The voting rights of each institution were determined in accordance with its exposure to Hynix.
- (17) Hynix was under the Corporate Restructuring Promotion Act (the "CRPA") and, as such, was effectively under the control of its creditors. The CFIC decided to sell the business or part of the business to a third party. In December 2002, the Restructuring Committee, which is a sub-committee of the CFIC, initiated negotiations with Micron Technology Inc. These lasted for 5 months; a Memorandum of Understanding was signed between the parties, but the terms of the sale were eventually rejected by the Hynix Board of Directors.

- (18) In May 2002, as a follow-up measure given the continuing deterioration of Hynix's finances, the CFIC hired a number of external advisors, including Deutsche Bank ("DB"), Morgan Stanley Dean Witter, Deloitte & Touche and A. D. Little, to analyse Hynix and come up with a plan to rescue the company. Together with these external advisors, KEB, which was the head of the CFIC as lead creditor, performed due diligence on Hynix until November 2002. The resulting report, prepared by Deutsche Bank and KEB (the "DB Report"), was submitted to the CFIC.
- (19) On 30 December 2002, the CFIC decided to implement a corporate turnaround and sell-off of the business, as outlined in the DB Report. The corporate turnaround involved a restructuring, comprising:
- a debt-to-equity swap of KRW 1.861,5bn,
 - a capital write-down on a ratio of 21:1,
 - a rollover of debt amounting to KRW 3.293bn, and
 - changes to the interest payment conditions of the rolled-over debt.

IV. Description of the Measures

i. Debt-to-Equity Swap

- (20) The CFIC decided to swap debt amounting to KRW 1.861,5bn for Hynix shares; this amounted to approximately 50 % of Hynix's unsecured loans. The swap share price was fixed to KRW 435 at the time the decision was taken in December 2002, by taking the one-month average market price. Although there is an obligation under the CRPA on the CFIC to use a reasonable method in calculating the swap price, no specific method is provided.
- (21) The restructuring plan involved a capital write-down prior to the swap taking place, which required shareholder approval; hence the swap could not take place immediately. Once the capital write-down was implemented, at a ratio of 21:1, the share swap price became KRW 9.135 (21 x KRW 435) and the swap went ahead. As the shares pursuant to the swap were not to be issued until April 2003, this price was to serve as a floor, but no ceiling was set. The actual share price at the time of the decision was in fact KRW 280; it fell to KRW 167 in April 2003.

ii. Debt Rollover

- (22) The maturity of the Hynix debt which was not converted to equity was extended to December 2006. This rolled-over debt amounted, in total, to KRW 3.293bn.

iii. Changes in the terms of interest payments

- (23) The interest rate on the rolled-over debt was reduced to 3,5 % from 6,5 %. The 3 % difference was treated as additional principal and was added on to the outstanding debt, with a maturity date of December 2006, as well. Interest on this additional principal was set at 6 %, to be paid quarterly.

V. The Policy of the GOK as regards Hynix

- (24) As described in the provisional and the definitive duty Regulations, the GOK had a keen interest in the fact of Hynix. The GOK admitted that, due to Hynix's situation, foreign investors were not willing to invest in Korea, because the Korean banks' exposure to Hynix was so high. It need the Hynix problem to be solved, in order to remove the uncertainty; in fact, Hynix's "structural adjustment" was cited as a main policy issue for the second half of 2002 in a report by the Ministry of Finance and Economy. A report submitted to the National Assembly by Korea's Grand National Party ("GNP"), in opposition, criticised the GOK's insistence on rescuing the Hyundai Group, in which Hynix was a subsidiary, stating that the GOK, by saving Hynix, was "injecting money into bottomless pits". Hynix claims that, as the report was submitted in November 2002, it should not be considered as evidence of the GOK's involvement in the new restructuring. However, the new restructuring was approved by the creditors only a month following the submission of the GNP report and deliberations on the best way to rescue Hynix had been ongoing for months before that. The GNP report, therefore, is not irrelevant to the question of whether the GOK had a policy to save Hynix.

(25) During the first half of the year, the Vice Minister for Finance stated that "creditors will have to find a solution to Hynix as soon as possible to minimise the adverse impact on the economy". To that end, a meeting between the GOK and Hynix's creditors had taken place to express the GOK's views with regard to the then ongoing negotiations with Micron. The MOFE could neither confirm nor deny whether other meetings had taken place and claimed that records of meetings were not always kept. The FSC, on the other hand, said that no other meetings had taken place, although it was kept abreast of what was happening by informal telephone calls. However, evidence on the record suggests that the GOK, mindful of the previous investigations in its involvement in Hynix by the European Communities and the United States, directed that any communication relating to Hynix should be made orally to avoid being traceable¹. The FSC stated that it had no power to intervene in the restructuring efforts of each company, but that it did conduct partial monitoring of the process, for example, where they thought there could be a potential shock to the markets. The FSC conducts such monitoring by contacts with "work-level" persons, but not records are kept of such contacts. Although the FSC admitted that Hynix was restructured because it was so big, it insisted that the manner and mode of such restructuring was determined solely by the creditors. The Hynix creditor banks confirmed that the FSC kept a close eye on the restructuring by telephone calls and requests for information.

¹ Kangwon Lee, CEO of KEB "I will not tell", Maeil Business Newspaper, 23 August 2002.

(26) The GOK, in the meetings of April 2002, communicated its official position to Hynix's creditors, which was either to sell Hynix or to rescue it to buffer the shock. Although the GOK insisted that the decision of whether liquidation was on the table or not was left to the creditors, its statements regarding the importance of rescuing Hynix (by a restructuring or a sale) in order to restore confidence in the Korean markets belies such insistence. The GOK's belief that Hynix was too big to fail is corroborated by a statement by one of the creditor banks that Hynix was such a big company, employing such a large number of people and and contracts "you can imagine what would happen if it went bankrupt or insolvent". Further, one of Hynix's external advisors, in its engagement letter wrote that it would assist "... in [the] effort to find a realistic and viable restructuring solution for Hynix that would *minimise social damage* ..." (emphasis added). It was plain that the liquidation of Hynix was not an option.

VI. GOK involvement in Hynix creditor banks

(27) The GOK is a major shareholder in a large number of Hynix creditor banks. The information on the record provided by the banks, Hynix and the GOK shows that the GOK has at least a significant shareholding (>20 %) in creditor banks/financial institutions holding at least 75 % of the voting rights in the CFIC. It is recalled that the required majority in the CFIC was 75 %; therefore, the GOK's involvement in the decisions taken by the Creditors' Council cannot be doubted.

- (28) As in the original investigation, KDB and NACF are wholly-owned government entities and are thus considered public bodies within the meaning of Article 1(3) of the basic Regulation.
- (29) There is no evidence on the record to suggest that the situation as regards Woori Bank changed from the one described in recitals (80) to (82) of the provisional duty Regulation. Further, as stated in the provisional duty Regulation, Chohung Bank, now called Shinhan Bank since its merged with Shinhan Bank on 1 April 2006, entered into a Memorandum of Understanding with the Korean Deposit Insurance Corporation ("KDIC") in January 2002, giving KDIC, a public body, a decisive influence over Chohung Bank's decision-making.
- (30) Prime Minister's Decree 408 is further evidence that there is legal scope for GOK intervention in the financial sector for policy reasons. The GOK cites the Decree as evidence that the Korean government officially stated that it would not intervene in banks and financial institutions. However, Article 5(1) of Prime Minister's Decree 408 stipulates that "In case a financial supervisory organisation makes a request for a financial institution's cooperation or support in necessity for the stabilisation of the financial market ... it shall be done in a document or by meeting." Therefore, not only does the Decree not preclude government intervention in financial institutions, it expressly sets out the ways in which such intervention may be carried out.

- (31) Hynix claimed that KEB was not controlled by the GOK and presented Commerzbank's shareholding as evidence of its independence from GOK intervention. It also submitted documents which refer to Commerzbank's veto right over some issues, including risk management. However, KEB could not confirm that Commerzbank, although it had sent a person to become a member of the credit team, actually exercised any control over credit decisions and, in fact, stated that they were unaware of the existence of such veto rights. Further, the recent investigation into the GOK's involvement in Lone Star's purchase of shares in KEB in 2003 demonstrates further that KEB is controlled by the GOK. Therefore, it is considered that there is no reason to depart from the conclusions of the original investigation regarding the GOK's influence on the decisions of KEB.
- (32) Another example of GOK involvement in the Hynix creditor banks was the appointment of a former Minister of Industry and Commerce as Chairman of the Restructuring Committee of Hynix's CFIC, by the Steering Committee of that body, only for him to be re-appointed Minister a few months later.
- (33) Kookmin and Woori Bank have also indicated that GOK interference might lead them to make policy-based decisions in their prospectuses to the Securities Exchange Commission in 2002. Hynix has submitted evidence that the wording in question did not refer specifically to Hynix and should not be taken as intending to imply that the GOK exercised control over the Korean banking sector. However, the evidence submitted by Hynix does not dispute other parts of the prospectus warning, for example, that GOK shareholding "could cause us to take actions or pursue policy objectives that may be against [creditors'] interests".

- (34) The Commission asked to see the internal documentation relating to creditors institutions' decision to approve the restructuring plan. These confidential documents show that, although the creditors each went through their standard internal procedures in deciding to participate in the restructuring, they did not act in accordance with the credit rating they had each ascribed to Hynix for the period in question. Although all creditors had given Hynix a rating equivalent to Standard & Poor's Selective Default, they nevertheless proceeded to approve the restructuring plan. For example, at the time the restructuring was approved, one bank's credit rating for Hynix indicated that the company was highly vulnerable and that the possibility of the business being restored was very unlikely. The rating given to Hynix by another of the banks involved indicated that the possibility of default was very high and that there was no possibility of future recovery. Instead, these banks went ahead and approved the restructuring proposal, even though the evidence suggests that this was not consistent with a market-oriented approach and the DB report does not indicate otherwise.
- (35) This was demonstrated by the creditors' treatment of both the debt they rolled over and the equity they received under the debt-to-equity swap: around 80-90 % of the Hynix debt had been written off as a loss – in one case, even 100 % – and the equity was booked at around 20 % of the price the creditors paid.

- (36) The company claims that subsequent events demonstrate that the creditors' decision was the correct one; Hynix has been profitable since 2005 and the creditors sold their shares in the company for a considerable profit. However, first of all this is an *ex post facto* analysis, which does not at all justify the conclusion that at the time the creditors approved the restructuring plan, this was consistent with a market oriented approach. Moreover, the fact that Hynix survived was due to the enormous subsidies it received. One cannot argue that, because Hynix survived, subsidies were not subsidies, if that survival was only possible because of those subsidies. Finally, the creditors were in the position they were in at the end of 2002 because they had participated in the 2001 restructuring, which constituted a subsidy. Therefore, they cannot argue that they should be compared to private creditors who have taken all the steps leading to their position at a certain point in time entirely of their own volition. Thus, Hynix's argument does not affect the conclusion that the creditors were not acting conformity with a market-oriented approach.

VII. Conclusion on Financial Contribution

- (37) In view of the evidence on the record regarding the GOK's policy as regards Hynix and its involvement in the decision-making process of Hynix's creditors, as well as the evidence relating to the dire state of Hynix and the market's unwillingness to advance capital, as well as the lack of evidence that the existing creditors acted in accordance with a market benchmark, itself undistorted by subsidies, it is concluded that the GOK entrusted and directed Hynix's creditors to rescue Hynix by approving the restructuring described in recital (19) above. This constituted a financial contribution within the meaning of Article 2(1) of the basic Regulation.

(38) Hynix claimed that the GOK had nothing to do with the new restructuring, which was devised by the creditors with the help of the external advisors. Further, it claimed that the evidence on record only showed that the GOK was concerned about Hynix's future, but that it fell short of the requirement for a demonstrable link between the GOK and the banks' actions. Although GOK shareholding is not conclusive proof of direction or entrustment, it is strong evidence of the extent to which the GOK can influence the banks' decision-making process. As was the case in the original investigation, evidence on the record shows that, as major shareholder, the GOK can appoint directors and is thus able to influence the outcome of voting at board meetings. Further, the various press articles and reports on record demonstrate clearly that the GOK would not allow Hynix to fail; this is also demonstrated by the fact that one of the wholly-owned GOK banks purchased Hynix debt from the other creditors to ease the financial burden on the banks that had been entrusted to save Hynix. It is not disputed that the new restructuring plan was devised by Hynix's external advisors in conjunction with its creditors; however, the evidence on the record suggests that the GOK had entrusted and directed Hynix's creditors to restructure Hynix and not let it fail.

(39) The behaviour of the banks also clearly demonstrates that they were not acting in accordance with normal commercial considerations. None of the banks rated Hynix as an investment grade company; in fact, all the rating ascribed to Hynix by its creditors show that they considered it a substantial risk and doubted that it would be able to survive. The company claimed that the creditors' behaviour should be examined from the point of view of an "existing creditor". However, as is discussed in more detail in recital (36) above and recitals (41)-(44) below, certainly in this case, which is affected by very large and similar subsidies having been granted only around a year earlier, the correct test to be applied with regard to the commercial reasonableness of the creditors is the private investor test. Therefore, the question of whether an existing creditor would have behaved in a manner similar to that of the Hynix creditors need not be addressed.

VIII. Benefit

(40) With regard to any benefit conferred to Hynix, KEB, Woori Bank, Shinhan Bank, KDB and NACF all argued that they had participated in the new restructuring because they wanted to maximise the recovery rate for the loans already granted to Hynix. They considered that the value of Hynix as a going concern was higher than its immediate liquidation value. Nevertheless, this comparison, whatever its merits are as a standard for analysis of the existence of a benefit, would in any case not be applicable in the present case for the reasons explained in recital (36) above and (41)-(44) below. Furthermore, the existence of a potential benefit to the heavily exposed creditors does not demonstrate that there was no benefit to Hynix.

- (41) Hynix claims that the new restructuring was market-based, as it was devised by external advisors, such as DB and Deloitte, after months of due diligence and was based on the DB report which recommended the course of action which was eventually followed. However, the DB report was addressed to Hynix's creditors. Its aim was to maximise debt recovery for such creditors while keeping the company from failing. Hynix argued that the test to be applied to ascertain the benefit received by the company from the new restructuring should be the "private creditor" test and not the "private investor" test. The position of the creditors is a factor which could be considered in an analysis; however, as explained in recital (36) and below, it cannot play a role in this case.
- (42) In general terms, the relevant standard is whether or not a market-oriented investor with or without an existing exposure to Hynix, would have assessed the proposed investment in Hynix as one worth making. The DB report does not provide a reliable response to that question, because, being addressed to the existing creditors, it is premised on using what are in general terms the existing Hynix debt and equity structures as a vehicle for the proposed investment, thus reducing to vanishing point any possibility for hypothetical outside investment on the same terms. The DB report contains no evidence that outside private investors would have had any interest in putting money into Hynix. Indeed, DB's advice to private investors was, in fact, not to invest in Hynix, as shown by the fact that its research department did not follow Hynix equity.

- (43) In any event, the financial situation of Hynix at the time of the new restructuring, as described in recital (14) above, was dire and it was evident that Hynix was not in a position to service its liabilities; hence, no funding was forthcoming from the market, as is evident from the statements of financial advisors cited in recitals (14) and (15) above. While the DB report points the way for Hynix's creditors to minimise their losses, it gives no indication as to why the market would have continued to lend or invest money in Hynix, a company in selective default. Therefore, such other data as are available concerning the position of Hynix and the market situation confirm that the DB report does not provide any reliable response to the question of whether or not a market-oriented investor would have assessed the proposed investment in Hynix as one worth making.
- (44) In addition, leaving aside the question of what course of action might or might not have been open to the parties in 2002 given the situation as it then existed, the fact remains that Hynix had been put in this situation by economically irrational investment and lending decisions taken by or on behalf of the GOK in 2001, the effects of which continued into 2002 and beyond. The express purpose of the new restructuring was to re-finance Hynix and it cannot be divorced from the initial 2001 bailout. The two are inextricably linked. In other words, it is only because of the irrational nature and the subsequent failure of the earlier restructuring that it became necessary to rollover the exposure of the existing creditors in the 2002 measure. Therefore, the solution proposed in the DB report was only possible on the back of the 2001 measures. It is not possible to treat a certain proposed course of action as a market benchmark if that course of action is itself a continuation of a previous unreasonable government investment decision. For this reason also, the DB report does not provide a reliable answer to the question of whether or not a market-oriented investor would have assessed the proposed investment in Hynix as one worth making.

(45) It is therefore considered that the new restructuring conferred a benefit to the company, within the meaning of Article 2(2) of the basic Regulation.

IX. Specificity

(46) As the measures comprising the new restructuring were taken exclusively for Hynix, the debt rollover, the principalisation of interest and the debt-to-equity swap are considered to be specific within the meaning of Article 3 of the basic Regulation.

X. Calculation of the amount of benefit

i. Timing of the benefit

(47) According to Article 5 of the basic Regulation, the amount of countervailable subsidies shall be calculated in terms of the benefit to the recipient which is found to exist during the investigation period of subsidisation. The amount of debt equivalent to the amount to be swapped into equity was moved away from loans and booked as a capital adjustment when the decision for the restructuring was taken on 30 December 2002 (Note 14 to Hynix's Financial Statements 2002). Similarly, Hynix was released from its interest payment obligations with regard to this debt on the same date.

(48) The Community industry argued that the benefit from the new restructuring did not accrue to Hynix until 13 April 2003, when shares were in fact issued to the creditors. On the other hand, the company argued that the effective date of the benefit is, in fact, December 2002, as that was the date when the decision to approve the restructuring was taken by the creditors and the date on which Hynix was released from its obligations as regards its debt.

- (49) As the DSB Panel on DRAMs stated that the benefit of a subsidy must be viewed from the point of view of the recipient and the company was no longer under any obligation vis-à-vis its debt exposure to its creditors from the date the decision to proceed with the new restructuring was taken, it is considered that the effective date for the accrual of the benefit to Hynix was 30 December 2002.

ii. Basis for calculation

Debt Rollover and Changes to the Interest Rate and Payment Conditions

- (50) In accordance with the methodology adopted in the original investigation, a debt rollover is taken to be a loan for the purposes of the benefit calculation. The principalised interest will also be treated as a loan for these purposes. In the original investigation, the subsidy was considered to be the face amount of the principal of the loan, allocated over the normal five-year depreciation period of assets. Each annual amount so allocated was increased by adding the standard commercial interest rate in Korea (7 %). The *EC-Korea DRAMs* Panel criticised this as being a "grant methodology" which did not reflect the fact that loans, unlike grants, are repayable and that "It is thus obviously less beneficial for a company to be given a loan than it is to be given a grant"¹. The Panel considered that the EC should base its calculation on benchmarks reflecting normal investment practices.
- (51) Following the WTO Panel's comments with regard to the grant methodology employed in the original investigation, it was considered appropriate in this review to find a loan-based benchmark against which the benefit could be calculated.

¹ *EC-Korea DRAMs Panel Report, Para 7.212.*

- (52) The financial situation of Hynix at the time of the new restructuring, as described in recitals (14) and (15) above, was dire and it was evident that Hynix was not in a position to service its liabilities; hence, no funding was forthcoming from the market. No commercially comparable lending had been provided to Hynix at the time of the new restructuring, nor was there any verified evidence on record regarding the cost and terms of a comparable commercial loan that Hynix or another firm in a situation comparable to Hynix had been provided at the relevant time. The fact that private entities had also participated in the new restructuring does not provide a reliable benchmark; the entities involved were small and held insignificant amounts of debt in Hynix, compared to the GOK-directed entities. Further, in accordance with the findings of the WTO Panel in the *Japan DRAMs* case, which considered the same facts as the current investigation, the presence of contemporaneous government involvement in the decision-making process regarding the new restructuring acts to distort the market and thus private, non-directed entities cannot be taken as a reliable benchmark¹.
- (53) The Commission has therefore constructed a proxy benchmark, based on a commercial interest rate, with the addition of a risk premium reflecting the default rates of companies exhibiting comparable risk. Such a benchmark takes into account the term of the loan, a benchmark interest rate that would be paid by a creditworthy company, the probability of default by an uncreditworthy company within a specified period of time and the probability of default by a creditworthy company within the same period of time.

¹ *Japan – Korea DRAMs WT/DS336/R Panel Report Para 7.283 – 7.298.*

- (54) The Commission has used the following formula to calculate an appropriate uncreditworthy benchmark interest rate:

$$i_b = [(1-q_n)(1+i_f)^n/(1-p_n)]^{1/n} - 1$$

Where:

n = the term of the loan

i_b = the benchmark interest rate for an uncreditworthy borrower

i_f = the long-term interest rate that would be paid by a creditworthy company

p_n = the probability of default by an uncreditworthy company within n years

q_n = the probability of default by a creditworthy company within n years.

- (55) For the purposes of this calculation, the Commission has used as the creditworthy rate for KRW loans the average Bank of Korea interest rate on investment grade corporate bonds in 2003, which was 10,43 %. The default rates for both creditworthy and uncreditworthy companies for the term of the measures in question were taken from Moody's Investor Services. The rate of default of an uncreditworthy company in 2003 within 3 years (the term of the rollover) was 54,86 %, whereas the rate of default of a creditworthy company within 3 years in 2003 was 0,33 %. This led to a total interest rate of 43,8 %. In contrast, the interest rate payable by Hynix on the rolled-over debt was 3,5 %, i.e., an interest rate differential of 40,3 %, which leads to a countervailing duty rate of 23,7 %.

Debt-to-Equity Swap

- (56) As described in recital (21) above, the CFIC calculated a swap price for the debt-to-equity swap of KRW 435 on 30 December 2002, based on the one-month average market price. The company claims that this was a commercially valid method to determine the share price and that it reflected market reality. In fact, this price reflected a ceiling; if the share price went up between 30 December 2002 and the day the shares were actually issued, the price would have changed accordingly. The actual price on the day the decision to proceed with the new restructuring was taken was KRW 280. When the debt was eventually converted into equity, following the capital reduction, at a price of KRW 9.513 (KRW 435 x 21), the share price was, in fact, KRW 3.500. If the effect of the capital writedown is ignored, the shares issued were trading well below par, at KRW 167. It is not disputed that the CFIC had a discretion as to the method by which it could set the swap price. Notwithstanding such a discretion, however, as the swap price was not a fixed price, but a guarantee that the company would receive a minimum amount for its shares, it cannot be considered to be a price which corresponds to commercial reality, especially given the actual price at the time the swap price was set and the unsurprising downward trend between the time of the CFIC meetings until the swap date in April 2003.

(57) In order to calculate the benefit received by Hynix from the debt-to-equity swap, the cost of issuing equity to Hynix must be considered. The Commission noted that, in order to examine the cost, if any, of the swap from the point of view of the recipient, the obligations imposed on a company when issuing new equity would have to be considered. The Commission noted in this respect, that injections of ordinary share capital do not generally impose particular obligations on a company, as there is neither a fixed rate of return which the company must achieve nor, in fact, do any payments need to be made. However, the company has at least a theoretical obligation to distribute its profits, or part thereof, to its shareholders; the return on equity ratio ("ROE") could provide some indication of the level of return the company is expected to provide to its shareholders and could be used in the calculation of the amount of the benefit to Hynix. However, the ROE of Hynix in 2003 was a negative percentage, as calculated by reference to its financial statements for the year. Therefore, on the basis of an objective evaluation of Hynix's financial standing at the time of the debt-to-equity swap, it is unreasonable to expect that Hynix would be in a position to distributed any sort of return to its shareholders for the relevant year. Hence, using the ROE as a benchmark, it would still be concluded that the entire amount of the debt-to-equity swap is a countervailable subsidy.

- (58) The Commission has also examined whether there are costs to Hynix associated with having to surrender ownership shares as a result of the swap or the cost to Hynix from a potential dilution of the share price resulting from the issuance of new shares. Based on its review of the record evidence, the Commission does not believe that the net benefit to Hynix of the full debt-to-equity swap is diminished as a result of the issuance of new shares. In this regard, the Commission believes it is essential to recognise the impact that the debt-to-equity swap had on Hynix's financial situation.
- (59) As a threshold matter, it is key to recognise that this was not a straight equity infusion. The fundamental benefit to Hynix resulted from the massive amount of debt that was extinguished as a result of the swap, namely KRW 1.861,5 billion. This absolved Hynix from having to repay any of this principal amount and from having to pay interest. Instead, this massive amount of debt was replaced with shares issued to the creditor banks. However, there was no real quantifiable cost to Hynix of issuing the new shares. While the existing share value was diluted as a result of the issuance, this had absolutely no balance sheet impact for Hynix. It did not result in any cash outlays (apart from the expense associated with the issuance of the new shares) and did not obligate Hynix to make any kind of cash payments in the future, as would have been the case with debt instruments.

- (60) The company claimed that the market value of the shares has to be deducted from any finding of benefit and cited the Commission's Guidelines for the Calculation of Subsidy in Countervailing Duty Investigations, which provide, in paragraph E(f)(iii), that "if the government buys shares in a company and pays above the market price for these shares (*taking into account of any other factors which may have influenced a private investor*), the amount of subsidy is the difference between the two prices (emphasis added)". However, a private investor would not have purchased Hynix shares in the relevant period at all. In fact, evidence on the record shows that Hynix's shares were trading at such a low level that they should have been suspended, but for an exception to the Korean Listing Regulations which appeared to have been carved out for Hynix alone. Further, the fact that there was a market value attached to the shares does not impact on the company, which does not have to pay it. This would only be a relevant consideration if there was an element in the debt-to-equity swap which obliged Hynix to enter into a share buyback.
- (61) Consequently, in light of the above considerations and since Hynix did not report any costs associated with the issuance of equity, it is considered that the appropriate approach to measuring the benefit from the debt-to-equity swap is to take the full amount of the swap.

iii. Final calculation of benefit

- (62) As explained in recital (61) above, the full amount of the debt-to-equity swap has been taken as the benefit accruing to Hynix from that measure. This subsidy confers a large, non-recurring benefit as, as described above, the allocation method over a period of 5 years was considered appropriate. The amount of subsidy so allocated was expressed as a percentage of the total sales of Hynix in 2005. With interest, using the average commercial interest rates applicable in Korea for the review investigation period, the countervailable subsidy is 6,8 %. However, as the debt-to-equity swap is a one-off, non-recurring subsidy, allocated over a set period of time and as such allocation period is deemed to begin at the time the benefit was actually received, it is considered it expired on 31 December 2007.
- (63) As mentioned in recital (50) above, the debt-rollover and the principalised interest were treated as loans and are considered to be a recurring subsidy. The company argued that it has repaid the subsidy received in the December 2002 restructuring when it refinanced its debt in July 2005 to a consortium of Korean and non-Korean banks (see recitals (75) and (76) below). Hynix claims that the refinancing, by which it assumed new debt in order to pay the debt under the new restructuring and graduate from the CRPA, extinguished the subsidy. When the refinancing took place in 2005, Hynix had returned to profit and had a credit rating of BBB+ according to the Korea Investors Service Inc. The refinancing of its debt on commercial terms by Hynix effectively stopped the subsidy from recurring, thus the benefit ceased to exist. As a result, it is considered that from 13 July 2005 the debt-rollover and the principalised interest ceased to confer a benefit to Hynix.

XI. Other alleged subsidy schemes

The BOE-Hydis Sale

- (64) In January 2003, Hynix sold its liquid crystal display business ("Hydis") to Beijing Orient Electronics Technology Group Co. Limited ("BOE"), a Chinese company, for approximately USD 380 million. The purchase price was funded to a large degree by loans provided by Hynix creditor banks, namely, KEB, KDB, Woori Bank and Hyundai Marine and Fire Insurance ("HMFI"), which collectively lent USD 188 million to the new company formed to buy the assets, BOE-Hydis.
- (65) The Community industry alleged that the GOK entrusted and directed the Korean banks to provide funding on preferential terms in order to enable BOE to purchase the assets, thus providing a much-needed cash injection to Hynix.

- (66) Although there was some evidence that pressure was exerted on to some of the other lenders by KEB and Hynix and that BOE was not able to attract financing from independent creditors, there was no evidence that the funding provided was, in fact, a countervailable subsidy. A finding of entrustment and/or direction of the Korean banks by the GOK is not enough; in order to find a countervailable subsidy in the circumstances described by the Community industry, it must be shown that BOE was itself entrusted and directed by the GOK to purchase Hydis. Even though the terms of the funding provided by the Korean banks were generous, BOE still assumed a debt of USD 188 million and paid the remainder of the purchase price in cash; there is no evidence of entrustment/direction by the GOK of BOE. In any event, the funding was given to BOE-Hydis, and no evidence has been presented that a benefit passed through to Hynix. Therefore, the loans of USD 188 million given to BOE-Hydis by Korean banks are not considered to constitute a subsidy within the meaning of Article 2 of the basic Regulation.

The System IC Sale

- (67) As envisaged by the terms of the new restructuring, in October 2004 Hynix sold its System IC assets to a consortium led by CVC Partners, a private equity fund managed by Citigroup Venture Capital for KRW 954,3 billion. Acquisition financing made up KRW 481,3 billion of the purchase price and it mostly took the form of a debt transfer from Hynix to MagnaChip, the company formed to buy the System IC assets. Hynix creditors transferred their unsecured Hynix debts to MagnaChip at a 21 % discount rate, but secured debts were assumed by the new company without any concession.

- (68) The Community industry alleged that the discounted debt transfer amounted to a countervailable subsidy. However, given that MagnaChip assumed debt of KRW 481,3 billion and paid KRW 481,3 billion in cash, in order to find that the transaction involved a financial contribution there should first be evidence of entrustment or direction of MagnaChip/CVC Partners and none was provided or found. Participation in the discounted debt transfer by the creditors was voluntary. Similarly to the BOE-Hydis sale, the funding was given to a third party and not Hynix, thus there is no evidence of a benefit having passed through to Hynix. Therefore, the discounted debt transfer to MagnaChip is not considered to constitute a subsidy within the meaning of Article 2 of the basic Regulation.

Cash BuyOut

- (69) In October 2004, Hynix used the proceeds from the sale of the System IC assets to implement a Cash Buyout plan, approved by the CFIC, according to which Hynix "bought back" the debt it owed to its creditors at a discount. In effect, Hynix offered to repay its debt early, albeit at a reduced rate. A second cash buyout ("CBO") took place in December 2004. The Community industry alleged that these discounted cash CBOs were a countervailable subsidy.
- (70) The creditors who wished to participate in the October CBO agreed that Hynix would repay 70 % of the unsecured debt owed to them and 96 % of any secured debt. The discount rate for unsecured debt was reduced to 21,84 % in for the December CBO.

- (71) Evidence on the record show that participation in the CBOs was voluntary. Further, there is no evidence suggesting that the participating creditors' behaviour was commercially unreasonable as the discount on the unsecured debt was compensated by the fact of early repayment and, hence, the time value of money. Therefore, the CBOs are not considered to constitute a subsidy within the meaning of Article 2 of the basic Regulation.

Preferential Tax Treatment

- (72) The Community industry alleged that the GOK gave preferential tax treatment to Hynix by not requiring it to recognise the gains from the debt-to-equity swap in the new restructuring as income. Although Hynix's losses were such in 2003 that it would not have been required to pay corporation tax even if it had recognised the gain from the swap as income, the Community industry claimed that Hynix received a benefit because, by not recognising the gain, it did not reduce its loss carryforwards, which it was then able to set off against taxable gains in 2005, when it became profitable.

(73) The alleged preferential tax treatment stems from a postponement of a change in the law which would require companies under voluntary restructurings, such as Hynix, to recognise gains from debt-to-equity swaps as taxable income. The Community industry has alleged that the GOK originally intended the change in legislation to come into force in March 2003, thus making the gains from Hynix's debt-to-equity swap pursuant to the new restructuring taxable. The Community industry claimed that following complaints from at least one of three companies directly affected by this change in the law, of which Hynix was one, the GOK postponed the coming into force of this new provision to 1 January 2004. Hynix claimed that the postponement of the effective date of the new provision was made when the GOK realised that the ruling's immediate effect would have been contrary to the principles of non-retroactivity and to the established practice of tax provisions coming into force at the beginning of the tax year.

(74) The Community industry reiterated its claims in its comments submitted following the disclosure of the essential facts and findings of the investigation. However, there is insufficient evidence on the record of the GOK's intention to ensure that Hynix's gain from its debt-to-equity swap was not taxed or that the alleged preferential treatment was, in fact, specific, within the meaning of Article 3 of the basic Regulation. Further, it is doubtful whether Hynix received any benefit from this tax exemption given the size of its net operating losses and the fact that these could be carried forward only for five years. Hynix eventually made a profit in 2005, but its losses were such that, even if the gain from the debt-to-equity swap was recognised as taxable income, its remaining loss carryforward was still more than enough to absorb the profit made in 2005, thus, no benefit would have accrued to Hynix during (or before) the IP. Moreover, as the benefit from the debt-to-equity swap was countervailed "gross", i.e., without taking any potential taxation impact into account, any benefit from such preferential tax treatment, has already been taken into account and to countervail it again would be double counting. Therefore, the tax treatment of Hynix's debt-to-equity by the GOK is not considered to be a subsidy within the meaning of Article 2 of the basic Regulation.

July 2005 Refinancing

- (75) In July 2005, Hynix refinanced KRW 1,2 trillion of its debt and graduated early from the CRPA. The refinancing involved a term loan of USD 500 million, raised by a bond issue on the New York Stock Exchange, and KRW 250 billion and a USD 550 million revolving credit agreement with the participation of both Korean and foreign banks (the "July 2005 refinancing"). The Community industry claimed that the July 2005 refinancing involves a further subsidy, as Hynix was still a heavily indebted company to which no funding was available on the market.
- (76) By July 2005, Hynix was a much healthier company, although a highly indebted one. It had returned to profitability and its credit rating was BBB+. Evidence on the record show that the terms of the financing provided by the Korean banks were not inconsistent with its credit rating. Further, the degree of participation of foreign banks supports Hynix's claim that the refinancing was made on commercial terms. In addition, there was no evidence of entrustment or direction of the Korean banks in relation to the loans extended to Hynix pursuant to this refinancing. Therefore, the July 2005 refinancing is not considered to be a subsidy within Article 2 of the basic Regulation.

XII. Conclusion on measures

- (77) The benefit from the subsidies countervailed in the original investigation was deemed to have been received on 1 January 2001 and was allocated over a period of five years, which corresponded to the normal depreciation period of the assets in the semiconductor industry.

- (78) The measures imposed in the original investigation related to one-off, non-recurring subsidies, allocated over a set period of time and as such allocation period is deemed to begin at the time the benefit was actually received, it is considered that the measures imposed by the definitive duty Regulation expired on 1 January 2006. As the debt rollover and the principalised interest of December 2002 ceased to confer a benefit on Hynix on 13 July 2005 and as the debt-to-equity swap of December 2002 expired on 31 December 2007, the measures should be repealed with effect from 31 December 2007 and the proceeding terminated.
- (79) Consequently, the definitive countervailing duties paid or entered in the accounts pursuant to Council Regulation (EC) No 1480/2003 on imports of certain electronic integrated circuits known as Dynamic Random Access Memories (DRAMs) manufactured using variations of metal oxide-semiconductors (MOS) process technology, including complementary MOS types (CMOS), of all types, densities, variations, access speed, configuration, package or frame etc., originating in the Republic of Korea and released for free circulation as from 31 December 2007 should be repaid or remitted.
- (80) Hynix, the GOK, the Community industry and all other interested parties were informed of the essential facts and considerations on the basis of which it is intended to recommend the repeal of the measures in force and the termination of the proceeding and had the opportunity to comment. Where appropriate, such comments were addressed in the sections of this Regulation specifically dealing with the issues raised.

- (81) Repayment or remission must be requested from national customs authorities in accordance with applicable customs legislation.
- (82) In its comments, the Community industry also claimed that measures should remain in force until they expire in August 2008, five years after the imposition of the definitive measures in order to offset countervailable subsidisation and cite Article 19 of the basic Regulation in support of such claim. However, Article 19 provides *inter alia* the possibility to repeal measures if they are no longer necessary to countervail subsidisation. Furthermore, Article 15 of the basic Regulation, which provides the basis for the imposition of measures, states that measures can be imposed – and by analogy, maintained – "unless the subsidy or subsidies are withdrawn or it has been demonstrated that the subsidies no longer confer any benefit on the exporters involved." As the result of the investigation indicates that the subsidies given to Hynix have ceased to confer a benefit, the measures cannot be kept in force and the claim of the Community industry has to be rejected,

HAS ADOPTED THIS REGULATION:

Article 1

The countervailing duty imposed on imports of certain electronic integrated circuits known as Dynamic Random Access Memories (DRAMs) manufactured using variations of metal oxide-semiconductors (MOS) process technology, including complementary MOS types (CMOS), of all types, densities, variations, access speed, configuration, package or frame etc., originating in the Republic of Korea imposed by Regulation (EC) No 1480/2003 is repealed as of 31 December 2007 and the proceeding is terminated.

Article 2

The definitive countervailing duties paid or entered into account pursuant to Article 1 of Regulation (EC) No 1480/2003 as from 31 December 2007 shall be repaid or remitted, pursuant to Article 236 of Council Regulation (EEC) No 2913/92 of 12 October 1992 establishing the Community Customs Code¹. Repayment or remission shall be requested from national customs authorities in accordance with applicable customs legislation.

¹ OJ L 302, 19.10.1992, p. 1. Regulation as last amended by Regulation (EC) No 1791/2006 (OJ L 363, 20.12.2006, p. 1).

Article 3

This Regulation shall enter into force on the day following that of its publication in the *Official Journal of the European Union*.

This Regulation shall be binding in its entirety and directly applicable in all Member States.

Done at Brussels,

For the Council

The President
