UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For the Quarterly Period Ended June 29, 2007

OR

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

For the Transition Period From ______ To ______

Commission File Number: 001-32431

DOLBY LABORATORIES, INC.
(Exact name of registrant as specified in its charter)

Delaware *(State or other jurisdiction of incorporation or organization)*	**90-0199783** *(I.R.S. Employer Identification No.)*
100 Potrero Avenue **San Francisco, CA** *(Address of principal executive offices)*	**94103-4813** *(Zip Code)*

(415) 558-0200
(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant 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 Exchange Act). Yes ☐ No ☒

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

On July 18, 2007, the registrant had 49,049,160 shares of Class A common stock, par value $0.001 per share, and 60,955,790 shares of Class B common stock, par value $0.001 per share, outstanding.

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PART I – FINANCIAL INFORMATION
ITEM 1 – CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

DOLBY LABORATORIES, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(in thousands)

	September 29, 2006	June 29, 2007
		(unaudited)
ASSETS		
Current assets:		
Cash and cash equivalents	$ 363,537	$325,909
Short-term investments	122,162	210,548
Accounts receivable, net of allowance	23,550	25,021
Inventories	11,104	14,091
Income tax receivable	1,371	20,875
Deferred income taxes	44,568	57,831
Prepaid expenses and other current assets	6,340	13,819
Total current assets	572,632	668,094
Property, plant and equipment, net	76,995	81,457
Intangible assets, net	14,954	33,028
Goodwill	23,188	41,908
Long-term investments	32,909	80,047
Long-term deferred income taxes	11,100	11,015
Other non-current assets	7,510	8,151
Total assets	**$ 739,288**	**$923,700**
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable and accrued liabilities	$ 79,336	$103,223
Income taxes payable	5,719	6,233
Current portion of debt	1,441	1,528
Deferred revenue	6,358	11,927
Total current liabilities	92,854	122,911
Long-term debt	10,893	10,037
Long-term deferred revenue	4,563	5,072
Long-term deferred income tax liability	—	6,312
Other non-current liabilities	16,779	14,274
Total liabilities	125,089	158,606
Controlling interest	19,911	21,825
Stockholders' equity:		
Class A common stock	37	49
Class B common stock	70	61
Additional paid-in capital	323,449	365,907
Retained earnings	266,918	365,591
Accumulated other comprehensive income	3,814	11,661
Total stockholders' equity	594,288	743,269
Total liabilities and stockholders' equity	**$ 739,288**	**$923,700**

See accompanying notes to unaudited condensed consolidated financial statements

DOLBY LABORATORIES, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(in thousands, except per share amounts)

	Fiscal Quarter Ended		Fiscal Year-to-Date Ended	
	June 30, 2006	June 29, 2007	June 30, 2006	June 29, 2007
	(unaudited)			
Revenue:				
Licensing	$ 69,138	$ 94,795	$221,303	$283,812
Product sales	18,862	17,191	50,574	47,870
Services	5,650	7,627	17,522	21,383
Total revenue	93,650	119,613	289,399	353,065
Cost of revenue:				
Cost of licensing	6,008	8,478	19,786	26,287
Cost of product sales (1)	10,190	8,119	29,754	24,519
Cost of services (1)	2,686	2,963	7,913	8,470
Total cost of revenue	18,884	19,560	57,453	59,276
Gross margin	74,766	100,053	231,946	293,789
Operating expenses:				
Selling, general and administrative (1)	38,477	48,430	113,598	128,266
Research and development (1)	9,108	11,854	25,413	31,650
Gain on settlements	—	(350)	—	(1,850)
Total operating expenses	47,585	59,934	139,011	158,066
Operating income	27,181	40,119	92,935	135,723
Interest income	4,671	6,592	13,383	19,216
Interest expense	(477)	(825)	(1,327)	(1,751)
Other income (expense), net	(174)	(8)	257	(347)
Income before provision for income taxes and controlling interest	31,201	45,878	105,248	152,841
Provision for income taxes	11,778	15,839	39,916	53,067
Income before controlling interest	19,423	30,039	65,332	99,774
Controlling interest in net income, net of tax	(339)	(354)	(1,000)	(1,101)
Net income	**$ 19,084**	**$ 29,685**	**$ 64,332**	**$ 98,673**
Basic earnings per share	$ 0.18	$ 0.27	$ 0.61	$ 0.91
Diluted earnings per share	$ 0.17	$ 0.26	$ 0.58	$ 0.87
Weighted-average shares outstanding (basic)	106,238	109,692	105,262	108,898
Weighted-average shares outstanding (diluted)	111,983	113,696	111,446	113,389
Expense for rent payable to related party included in selling, general and administrative expenses	337	340	1,546	1,021

(1) Stock-based compensation included above was classified as follows:

Cost of product sales	$ 201	$ 269	$ 599	$ 679
Cost of services	129	39	385	107
Selling, general and administrative	3,731	3,838	11,941	11,459
Research and development	679	993	2,015	2,512

See accompanying notes to unaudited condensed consolidated financial statements

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DOLBY LABORATORIES, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)

	Fiscal Year-to-Date Ended	
	June 30, 2006	June 29, 2007
	(unaudited)	
Operating activities:		
Net income	$ 64,332	$ 98,673
Adjustments to reconcile net income to net cash flows from operating activities:		
Depreciation and amortization	9,452	10,533
Stock-based compensation expense	14,940	14,757
Accretion of discounts on debt securities	—	(1,816)
Excess tax benefit from exercise of stock options	(11,016)	(18,524)
Provision for doubtful accounts	601	1,021
Deferred income taxes	(8,174)	(13,389)
Other non-cash items affecting net income	1,292	1,558
Changes in operating assets and liabilities:		
Accounts receivable	1,235	(2,039)
Inventories	(1,797)	(6,664)
Prepaid expenses and other assets	502	(8,017)
Accounts payable and accrued liabilities	7,047	23,485
Income taxes, net	8,194	3,132
Deferred revenues	2,994	5,880
Other non-current liabilities	(182)	(113)
Payment on litigation settlement	(3,000)	(3,000)
Cash flows from operating activities	86,420	105,477
Investing activities:		
Purchases of available-for-sale securities	(405,239)	(307,383)
Proceeds from sale of available-for-sale securities	255,145	173,172
Purchases of property, plant and equipment	(5,697)	(6,945)
Acquisitions, net of cash acquired	—	(30,230)
Purchase of intangible assets	—	(750)
Other investing activities	(1,000)	88
Cash flows from investing activities	(156,791)	(172,048)
Financing activities:		
Payments on debt	(1,011)	(1,087)
Proceeds from the exercise of stock options	4,309	7,253
Issuance of Class A common stock from ESPP purchase	2,207	967
Excess tax benefit from exercise of stock options	11,016	18,524
Cash flows from financing activities	16,521	25,657
Effect of foreign exchange rate changes on cash and cash equivalents	2,093	3,286
Net decrease in cash and cash equivalents	(51,757)	(37,628)
Cash and cash equivalents at beginning of period	372,403	363,537
Cash and cash equivalents at end of period	**$ 320,646**	**$ 325,909**
Supplemental disclosure:		
Cash paid for income taxes	$ 41,573	$ 63,317
Cash paid for interest	1,348	1,335

See accompanying notes to unaudited condensed consolidated financial statements

DOLBY LABORATORIES, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

1. Summary of Business and Significant Accounting Policies

Dolby Laboratories develops and delivers innovative products and technologies that make the entertainment experience more realistic and immersive. Since Ray Dolby founded Dolby Laboratories in 1965, we have been at the forefront of delivering sound technologies that assist the entertainment creation process and enhance the entertainment experience. Today, Dolby technologies are standard in a wide range of entertainment platforms. For example, Dolby products are widely used in movie theatres around the world and our technologies are used in virtually all DVD players and DVD playback software for personal computers. In addition, Dolby Digital is mandated in all North American digital televisions and digital set-top boxes that include Advanced Television Systems Committee (ATSC) television tuners and is widely included in high-definition set-top boxes used for European high-definition television broadcasts.

Unaudited Interim Financial Statements

The accompanying interim condensed consolidated balance sheet as of June 29, 2007, the condensed consolidated statements of operations for the fiscal quarters and fiscal year-to-date periods ended June 30, 2006 and June 29, 2007 and the condensed consolidated statements of cash flows for the fiscal year-to-date periods ended June 30, 2006 and June 29, 2007 are unaudited. These interim consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP). In our opinion, the interim consolidated financial statements have been prepared on the same basis as the audited consolidated financial statements for the year ended September 29, 2006 and include all adjustments necessary for fair presentation. The results for the fiscal quarter and fiscal year-to-date period ended June 29, 2007 are not necessarily indicative of the results to be expected for any subsequent quarterly or annual financial period, including the fiscal year ending September 28, 2007.

The accompanying interim financial statements are prepared in accordance with Securities and Exchange Commission rules and regulations, which allow certain information and footnote disclosures that are normally included in annual financial statements to be condensed or omitted. As a result, the accompanying interim financial statements should be read in conjunction with our consolidated financial statements for the year ended September 29, 2006 that are included in our Annual Report on Form 10-K and filed with the Securities and Exchange Commission.

Use of Estimates

The preparation of the consolidated financial statements in accordance with U.S. GAAP requires management to make certain estimates and assumptions that affect the amounts reported and disclosed in our consolidated financial statements and accompanying notes. Significant items subject to such estimates and assumptions include valuation allowances for receivables, carrying values of inventories, goodwill, intangible assets, stock-based compensation and deferred income tax assets. Actual results could differ from our estimates.

Prior Period Presentation

During the second quarter of fiscal 2007, we determined that certain immaterial corrections were needed to properly classify variable rate demand notes (VRDNs) as short-term investments rather than cash and cash equivalents, which resulted in a reduction of cash and cash equivalents of $49.0 and $52.8 million and a corresponding increase in short-term investments of the same amounts as of September 29, 2006 and June 30, 2006, respectively. The corrections were made to adjust the prior misclassification of VRDNs based on the current interpretation of cash equivalents pursuant to Statement of Financial Accounting Standards No. 95, *Statement of Cash Flows*. Additionally, the corrections increased cash outflows from investing activities by $49.0 million and $52.8 million, thereby reducing net cash flows by the same amounts for fiscal 2006 and the fiscal year-to-date period ended June 30, 2006, respectively.

The following table illustrates the impact of the prior period reclassification on investing activities and net cash flows for the fiscal year-to-date period ended June 30, 2006.

	Fiscal Year-To-Date Period Ended June 30, 2006
	(in thousands)
Investing activities:	
Cash flows from investing activities (as reported)	$ (104,016)
Reclassification of VRDNs to short-term investments	(52,775)
Cash flows from investing activities (reclassified)	$ (156,791)
Net increase (decrease) in cash and cash equivalents:	
Net increase in cash and cash equivalents (as reported)	$ 1,018
Reclassification of VRDNs to short-term investments	(52,775)
Net decrease in cash and cash equivalents (reclassified)	$ (51,757)

Per Share Data

Basic earnings per share is computed by dividing net income by the weighted-average number of shares of Class A common stock and Class B common stock outstanding during the period. Diluted earnings per share is computed by dividing net income by the sum of the weighted-average number of shares of Class A common stock and Class B common stock outstanding and the potential number of shares of dilutive Class A common stock and Class B common stock outstanding during the period. The potential common shares are comprised entirely of options to purchase shares of Class A common stock and Class B common stock.

The following table sets forth the computation of basic and diluted earnings per share:

	Fiscal Quarter Ended		Fiscal Year-to-Date Ended	
	June 30, 2006	June 29, 2007	June 30, 2006	June 29, 2007
	(in thousands, except per share amounts)			
Numerator:				
Net income	$ 19,084	$ 29,685	$ 64,332	$ 98,673
Denominator:				
Weighted-average shares outstanding (basic)	106,238	109,692	105,262	108,898
Potential common shares from options to purchase Class A common stock and Class B common stock	5,745	4,004	6,184	4,491
Weighted-average shares outstanding (diluted)	111,983	113,696	111,446	113,389
Basic earnings per share	**$ 0.18**	**$ 0.27**	**$ 0.61**	**$ 0.91**
Diluted earnings per share	**$ 0.17**	**$ 0.26**	**$ 0.58**	**$ 0.87**

A total of 1,581,240 and 1,790,872 options were excluded from the calculation of potential common shares for the third quarter of fiscal 2006 and the third quarter of fiscal 2007, respectively, because their inclusion would have been anti-dilutive. A total of 1,671,801 and 1,434,147 options were excluded from the calculation of potential common shares for the fiscal year-to-date periods ended June 30, 2006 and June 29, 2007, respectively, because their inclusion would have been anti-dilutive.

Cash Equivalents and Investments

We have investments in money market funds, United States government agency securities, auction rate certificates, variable rate demand notes and municipal debt securities. We account for these instruments under the provisions of Statement of Financial Accounting Standards No. 115, *Accounting for Certain Investments in Debt and Equity Securities*. Investments that have original maturities of 90 days or less from the date of purchase are classified as cash equivalents; investments that have original maturities between 91 days and one year from the date of purchase are classified as short-term investments; and investments that have maturities of more than one year from the date of purchase are classified as long-term investments. Auction rate certificates and variable rate demand notes which have original maturities greater than one year are classified as short-term investments based on our ability and intent to sell these instruments within one year from the date of purchase. All of our investments are classified as available-for-sale and are recorded at fair market value, except for an investment in equity securities that is accounted for under the cost method, on the accompanying condensed consolidated balance sheet. Unrealized gains or losses from these investments are reported as a component of other comprehensive income and realized gains or losses are reported as a component of other income, net.

Stock-Based Compensation

We account for stock-based compensation under the provisions of Statement of Financial Accounting Standards No. 123(R), *Share-Based Payment* (SFAS 123R). SFAS 123R requires measurement of all employee stock-based awards using a fair-value method and recording of related compensation expense in the consolidated financial statements over the requisite service period. Further, as required under SFAS 123R, we estimate forfeitures for share based awards that are not expected to vest. In the third quarter of fiscal 2007, we recorded stock-based compensation expense of $5.1 million under the fair-value provisions of SFAS 123R, compared to $4.7 million in the third quarter of fiscal 2006. For the fiscal year-to-date period ended June 29, 2007, we recorded stock-based compensation expense of $14.8 million, compared to $14.9 million for the fiscal year-to-date period ended June 30, 2006. See Note 4 “Stockholders’ Equity and Stock-Based Compensation” for further discussion.

Income Taxes

We recognize our quarterly provision for income taxes based on our estimated full year projected effective tax rate. We estimate our effective tax rate based on projections of our income before income taxes for the full fiscal year. In the period that we file our annual tax returns, we true up our provision for income taxes to reflect any difference between our estimated provision and our filed tax return. In the third quarter of fiscal 2007, we determined that we had incorrectly estimated the amount of tax-free interest income that we expect for the full year of fiscal 2007. As a result, we adjusted our provision for income taxes in the third quarter of fiscal 2007 by $1.4 million related to the first two quarters of fiscal 2007. We concluded that the impact of this adjustment was not material to the third quarter of fiscal 2007 or any prior quarters.

Gain on Settlements

Gain on settlements includes payments received related to the resolution of disputes with integrated circuit (IC) manufacturers from which we typically do not earn royalties. In contrast, amounts attributable to the resolution of royalty disputes from licensees that specifically represent unpaid royalties are recorded as licensing revenue in the period payment is received, if all other revenue recognition criteria have been met. In the third quarter of fiscal 2007, we recognized $0.4 million as gain on settlement in connection with the resolution of disputes with two IC manufacturers regarding the violation of the terms of their licensing agreements with us. For the fiscal year-to-date period ended June 29, 2007, we have recognized $1.9 million as gain on settlement related to the resolution of disputes with three IC manufacturers.

Comprehensive Income

Comprehensive income includes net income, foreign currency translation adjustments and unrealized losses on available-for-sale securities which are reflected as a component of stockholders’ equity. The components of comprehensive income, net of tax, were as follows:

	Fiscal Quarter Ended		Fiscal Year-to-Date Ended	
	June 30, 2006	June 29, 2007	June 30, 2006	June 29, 2007
	(in thousands)			
Net income	$19,084	$29,685	$ 64,332	$ 98,673
Other comprehensive income (loss):				
Foreign currency translation adjustment	3,002	3,355	2,033	8,109
Unrealized losses on available-for-sale securities, net of tax	(101)	(135)	(101)	(262)
Comprehensive income	$21,985	$32,905	$ 66,264	$ 106,520

Withholding and Sales Tax

Licensing revenue is recognized gross of withholding taxes that are remitted by our licensees directly to their local tax authorities. Withholding taxes were $2.5 million and $2.7 million in the third quarter of fiscal 2006 and 2007, respectively. Withholding taxes were $7.3 million and $9.4 million in the fiscal year-to-date period ended June 30, 2006 and June 29, 2007, respectively. Sales tax is accounted for on a net basis and is excluded from revenues.

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2. Composition of Certain Financial Statement Captions

Cash, Cash Equivalents, and Investments

Cash, cash equivalents, and investments as of September 29, 2006 and June 29, 2007 consisted of the following:

	September 29, 2006	June 29, 2007
	(in thousands)	
Cash and cash equivalents:		
Cash	$ 108,653	$122,256
Cash equivalents:		
Money market funds	224,331	196,186
U.S. government agency securities	30,553	7,467
Cash and cash equivalents	363,537	325,909
Investments:		
U.S. government agency securities	17,011	115,727
Auction rate certificates	62,850	83,600
Variable rate demand notes	48,950	55,000
Municipal debt securities	25,466	35,474
Equity securities	794	794
Total investments	155,071	290,595
Cash, cash equivalents and investments	$ 518,608	$616,504

Our investment portfolio which is recorded as cash equivalents, short-term investments, and long-term investments as of June 29, 2007 is as follows:

	Maturity					
	90 Days or Less		91 Days to One Year		Greater than One Year	
	Fair Value	Net Unrealized Loss	Fair Value	Net Unrealized Loss	Fair Value / Cost	Net Unrealized Loss
	(in thousands)					
Money market funds	$196,186	$ —	$ —	$ —	$ —	$ —
U.S. government agency securities	7,467	(2)	49,584	(38)	66,143	(103)
Variable rate demand notes	—	—	55,000	—	—	—
Municipal debt securities	—	—	22,364	(31)	13,110	(35)
Auction rate certificates	—	—	83,600	—	—	—
Equity securities	—	—	—	—	794	—
Cash equivalents and investments	$203,653	$ (2)	$210,548	$ (69)	$ 80,047	$ (138)

Equity securities have been accounted for under the cost method and though it does not have any maturity, we have classified it as a long-term investment based on our ability and intent to hold the investment for more than one year.

We review our investment portfolio for indicators of impairment. This evaluation requires significant judgment to identify events or circumstances that would likely have a significant adverse effect on the fair value of our investments. Total investment securities had net unrealized losses of $0.2 million, which consisted of gross unrealized losses of $0.7 million and gross unrealized gains of $0.5 million as of June 29, 2007. An analysis of the securities in an unrealized loss position revealed that the total potential other-than-temporary impairment exposure was less than $0.1 million. Based on our evaluation of the impairment indicators, and because we have the ability and intent to hold these investments until a recovery of fair value, which may be maturity, we do not consider any of our investments to be other-than-temporarily impaired as of June 29, 2007.

Accounts Receivable

Accounts receivable consists of the following:

	September 29, 2006	June 29, 2007
	(in thousands)	
Trade accounts receivable, licensing	$ 13,648	$11,016
Trade accounts receivable, products and services	8,949	11,647
Amounts receivable related to joint licensing programs	2,037	2,048
Other accounts receivable	640	1,409
	25,274	26,120
Less: Allowance for doubtful accounts	(1,724)	(1,099)
Accounts receivable, net of allowance	$ 23,550	$25,021

Inventories

Inventories are stated at the lower of cost (first-in, first-out) or market, adjusted for excess and obsolete items, and consist of the following:

	September 29, 2006	June 29, 2007
	(in thousands)	
Raw material	$ 4,339	$ 4,023
Work in process	1,437	2,580
Finished goods	5,328	7,488
Inventories	$ 11,104	$14,091

Goodwill and Intangible Assets

Following is a summary of goodwill and intangible assets:

	September 29, 2006	June 29, 2007
	(in thousands)	
Amortized intangible assets:		
Patents	$ 4,435	$21,087
Acquired technology	3,745	6,293
Other intangibles	11,428	12,353
	19,608	39,733
Less: Accumulated amortization	(4,654)	(6,705)
Intangible assets, net	$ 14,954	$33,028
Non-amortized intangible assets:		
Goodwill	$ 23,188	$41,908

Amortization expense associated with our intangible assets was $0.5 million and $1.0 million in the third quarters of fiscal 2006 and 2007, respectively, and is included in cost of licensing, cost of product sales, and selling, general and administrative expenses in the accompanying condensed consolidated statements of operations. Amortization expense associated with our intangible assets was $1.5 million and $2.1 million for the fiscal year-to-date periods ended June 30, 2006 and June 29, 2007, respectively. The increase in goodwill from September 29, 2006 to June 29, 2007 was due to the acquisition of Brightside Technologies Inc. (Brightside), as well as fluctuations in foreign currency exchange rates. Our fiscal 2007 impairment test of goodwill, which was performed in the third quarter of fiscal 2007, resulted in no impairment charge.

Accounts Payable and Accrued Liabilities

Accounts payable and accrued liabilities consist of the following:

	September 29, 2006	June 29, 2007
	(in thousands)	
Accounts payable	$ 4,581	$ 5,397
Accrued royalties	11,054	30,615
Amounts payable to joint licensing program partners	26,749	24,038
Accrued compensation and benefits	23,241	25,119
Accrued professional fees	3,629	3,743
Current portion of litigation settlement (see Note 5)	2,502	2,456
Other accrued liabilities	7,580	11,855
Accounts payable and accrued liabilities	$ 79,336	$103,223

Accrued royalties includes approximately $10.5 million and $29.8 million at September 29, 2006 and June 29, 2007, respectively, in royalties related to the license of certain patents under a license agreement with an unrelated third party. In the third quarter of fiscal 2006, we evaluated whether the patents licensed to us under the license agreement covered all of the products and technologies for which we had historically been paying royalties to the patent licensor. Based on our evaluation, we determined that under the license agreement we may not owe royalties to the patent licensor on all the products and technologies for which we had historically been paying. In the third quarter of fiscal 2006, we notified the patent licensor that going forward we intended to pay royalties only for products and technologies that we believe are covered by the patents licensed under the license agreement, and subsequently, we have been paying the patent licensor royalties on this basis. In the second quarter of fiscal 2007, the patent licensor informed us that it disagreed with our interpretation of the license agreement. While we are trying to resolve this matter with the patent licensor, there continues to be uncertainty regarding the outcome. As a result, we have continued to accrue royalty expense in a manner consistent with our historical payments.

3. Segment Information

Operating Segments

Our chief operating decision maker is our Chief Executive Officer (CEO). While the CEO evaluates results in a number of different ways, historically the primary basis for which the allocation of resources and financial results has been assessed has been by examining our business in two operating segments: the technology licensing segment and the products and services segment. The technology licensing segment licenses our technologies, trademarks and know-how to manufacturers of consumer electronics products and software developers. The products and services segment provides professional products to movie theatres and to the recording, broadcast, cable and video post-production industries. Additionally, this segment provides services to film production and distribution companies, cinemas and broadcasters.

In an effort to improve our ability to scale our organization and effectively apply our strategy across our markets, in the third quarter of fiscal 2007 we decided to reorganize our business from two operating segments into a functional organizational model. As a result, there will be a products and technology group responsible for research, engineering, product development, manufacturing and technology and there will be a sales and marketing group responsible for all sales, marketing, business development and field operations. The world-wide corporate support functions will continue to support the overall needs of the business. The change will take effect in the fourth quarter of fiscal 2007. We are currently evaluating the new structure as it relates to Statement of Financial Accounting Standards No. 131, *Disclosures about Segments of an Enterprise and Related Information*.

Accounting policies for each of the operating segments are the same as those used on a consolidated basis. Our reportable segment information for the fiscal quarters and fiscal year-to-date periods ended June 30, 2006 and June 29, 2007 is as follows:

	Revenue			
	Fiscal Quarter Ended		Fiscal Year-to-Date Ended	
	June 30, 2006	June 29, 2007	June 30, 2006	June 29, 2007
	(in thousands)			
Technology licensing	$ 69,138	$ 94,795	$ 221,303	$ 283,812
Products and services	24,512	24,818	68,096	69,253
Total revenue	$ 93,650	$119,613	$ 289,399	$ 353,065

	Gross Margin			
	Fiscal Quarter Ended		Fiscal Year-to-Date Ended	
	June 30, 2006	June 29, 2007	June 30, 2006	June 29, 2007
	(in thousands)			
Technology licensing	$ 63,130	$ 86,317	$ 201,517	$ 257,525
Products and services	11,636	13,736	30,429	36,264
Total gross margin	$ 74,766	$100,053	$ 231,946	$ 293,789

	Reconciliation to Income before Provision for Income Taxes and Controlling Interest			
	Fiscal Quarter Ended		Fiscal Year-to-Date Ended	
	June 30, 2006	June 29, 2007	June 30, 2006	June 29, 2007
	(in thousands)			
Total segment gross margin	$ 74,766	$100,053	$ 231,946	$ 293,789
Operating expenses	(47,585)	(59,934)	(139,011)	(158,066)
Other income, net	4,020	5,759	12,313	17,118
Total income before provision for income taxes and controlling interest	$ 31,201	$ 45,878	$ 105,248	$ 152,841

We do not track capital expenditures or assets by reportable segment. Consequently, it is not practical to show this information.

Geographic Data

Revenue by geographic region, which was determined based on the location of our licensees for licensing revenue, the location of our direct customers or distributors for product sales, and the location where services were performed for service revenue, was as follows:

	Revenue by Geographic Region			
	Fiscal Quarter Ended		Fiscal Year-to-Date Ended	
	June 30, 2006	June 29, 2007	June 30, 2006	June 29, 2007
	(in thousands)			
United States	$29,639	$ 43,553	$ 79,735	$ 100,081
International	64,011	76,060	209,664	252,984
Total revenue	$93,650	$119,613	$289,399	$ 353,065

The concentration of our revenue from individual countries or geographic regions was as follows:

	Fiscal Quarter Ended		Fiscal Year-to-Date Ended	
	June 30, 2006	June 29, 2007	June 30, 2006	June 29, 2007
	(in thousands)			
United States	*32%*	*36%*	*28%*	*28%*
Japan	*18%*	*18%*	*22%*	*21%*
Europe	*19%*	*17%*	*20%*	*20%*
Taiwan	*12%*	*11%*	*10%*	*11%*
China	*10%*	*8%*	*10%*	*11%*
Other	*9%*	*10%*	*10%*	*9%*

In the third quarter of fiscal 2007, revenue from our two largest licensing segment customers represented $13.0 million and $12.8 million, or 11%, of total revenue for each customer. For the fiscal year-to-date period ended June 29, 2007, revenue from our largest customer represented $35.3 million or 10%, of total revenue. No other customers represented over 10% of revenue for the fiscal year-to-date period ended June 29, 2007. In the third quarter of fiscal 2006, revenue from our largest licensing segment customer represented $9.8 million, or 10%, of total revenue, and no customer accounted for more than 10% of total revenue for the fiscal year-to-date period ended June 30, 2006.

Long-lived tangible assets, net of accumulated depreciation, by geographic region were as follows:

	Long-Lived Tangible Assets by Geographic Region	
	September 29, 2006	June 29, 2007
	(in thousands)	
United States	$ 55,236	$58,239
International	21,759	23,218
Total long-lived tangible assets, net of accumulated depreciation	$ 76,995	$81,457

Long-lived tangible assets, which consist of property, plant and equipment net of accumulated depreciation, held in the United Kingdom were $21.0 million and $22.1 million at September 29, 2006 and June 29, 2007, respectively.

4. Stockholders' Equity and Stock-Based Compensation

Secondary Offering

On May 15, 2007, we filed a registration statement with the Securities and Exchange Commission relating to the public offering and sale of 8,000,000 shares of our Class A common stock by an affiliate of Ray Dolby, the founder, chairman of our Board of Directors, and, together with certain affiliates, the largest stockholder of the Company. The offering was priced at $32.00 per share and all 8,000,000 shares were sold on May 30, 2007. We did not receive any proceeds from the sale of the shares. We incurred approximately $0.7 million of expenses related to the sale of the shares for legal, accounting and registration fees which were recorded to selling, general and administrative expenses. We agreed to indemnify the underwriters against certain potential liabilities under the Securities Act of 1933 related to the offering and the registration statement.

Stock-Based Compensation

We utilize stock-based awards as a form of compensation for employees, officers, directors and non-employee consultants. Stock-based compensation expense was $4.7 million and $5.1 million for the third quarter of fiscal 2006 and 2007, respectively, and $14.9 million and $14.8 million for the fiscal year-to-date periods ended June 30, 2006 and June 29, 2007, respectively.

We recognized $4.5 million and $6.0 million in tax benefits related to stock-based compensation arrangements in the third quarter of fiscal 2006 and 2007, respectively and $13.6 million and $23.5 million in tax benefits related to stock-based compensation arrangements in the fiscal year-to-date periods ended June 30, 2006 and June 29, 2007, respectively.

We have issued stock-based awards in the form of stock options, stock appreciation rights, shares issued under our employee stock purchase plan and stock grants. Below is a summary of the different types of stock-based awards issued under our stock plans:

Stock Options. We have granted stock options to our employees, officers and directors under our 2005 Stock Plan and our 2000 Stock Incentive Plan. We utilize a Black-Scholes option pricing model to determine the fair value of employee stock options at the date of grant. The fair value of our stock-based awards was estimated using the following weighted-average assumptions:

	Fiscal Quarter Ended		Fiscal Year-to-Date Ended	
	June 30, 2006	June 29, 2007	June 30, 2006	June 29, 2007
Expected term (in years)	6.25	5.09	6.23	5.71
Expected stock price volatility	50.4%	40.1%	50.1%	43.5%
Risk-free interest rate	5.2%	4.6%	4.6%	4.6%
Dividend yield	—	—	—	—

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Stock-based compensation expense is recorded net of estimated forfeitures. In the third quarter of fiscal 2007, we utilized an estimated forfeiture rate of 5.6%.

The following table summarizes information about stock options issued to officers, directors, employees and non-employee consultants under our 2000 Stock Incentive Plan and 2005 Stock Plan:

	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life	Aggregate Intrinsic Value
	(in thousands)		(in years)	(in thousands)
Options outstanding at September 29, 2006	8,881	$ 5.47		
Grants	1,921	29.52		
Exercises	(2,598)	2.79		
Forfeitures and expirations	(364)	10.69		
Options outstanding at June 29, 2007	7,840	12.00	7.18	$ 183,647
Options vested and expected to vest at June 29, 2007	7,215	11.45	7.09	$ 172,948
Options exercisable at June 29, 2007	3,358	3.49	5.69	$ 107,193

The weighted-average fair value of stock options on the date of grant was $12.90 and $14.86 for the third quarter of fiscal 2006 and 2007, respectively, and $10.11 and $13.95 for the fiscal year-to-date period ended June 30, 2006 and June 29, 2007, respectively. Aggregate intrinsic value is based on the closing price of our common stock on June 29, 2007 of $35.41 and excludes the impact of options that were not in-the-money.

5. Legal Proceedings

In March 1997, an unrelated third party filed a lawsuit against us alleging breach of a written agreement. In April 2002, we settled the dispute and agreed to pay a total of $30.0 million, without interest, in ten equal annual installments of $3.0 million per year beginning in June 2002. We recorded this liability at its present value of $24.2 million on the consolidated balance sheet using a discount rate of 5.125%, which approximated our incremental cost of borrowing rate. Interest related to this liability is recorded quarterly and is included in other income, net on the accompanying condensed consolidated statements of operations. Other than such payments, neither party has any material obligations as a result of the settlement. We made an annual $3.0 million payment in June 2007. As of June 29, 2007, we had $12.0 million remaining to be paid under this settlement.

In addition, we are involved in various legal proceedings from time to time arising from the normal course of business activities, including claims of alleged infringement of intellectual property rights, commercial, employment and other matters. In our opinion, resolution of these proceedings is not expected to have a material adverse effect on our operating results or financial condition. However, it is possible that an unfavorable resolution of one or more such proceedings could materially affect our future operating results or financial condition in a particular period.

6. Business Combinations

In April 2007, we acquired all outstanding shares of Brightside a provider of high-dynamic range (HDR) technology. The technology acquired through this acquisition focuses on enabling the capture, distribution, and display of more vibrant video on LCD TV sets. We acquired Brightside to expand our technology portfolio and to increase our expertise in imaging technologies. The acquisition was accounted for as a business combination as described in Statement of Financial Accounting Standards No. 141, *Business Combinations.* The financial results of Brightside, excluding those that are eliminated in consolidation, have been included in our consolidated financial statements since April 2007. Supplemental pro forma disclosure was deemed not necessary due to the immateriality of the financial statements.

The aggregate cost of the acquisition, net of acquired cash, was $30.5 million and was allocated as follows:

	Total Purchase Price Allocation
	(in thousands)
Goodwill	$ 16,072
Patents	15,900
Developed technology	2,500
Other intangible assets	100
Acquired liabilities, net	(4,121)
Total purchase price	$ 30,451

7. Contractual Obligations and Commitments

The following table presents a summary of our contractual obligations and commitments as of June 29, 2007:

	Payments Due by Period				
	Remainder of Fiscal 2007	Fiscal 2008 to 2009	Fiscal 2010 to 2011	After Fiscal 2011	Total
			(in thousands)		
Long-term debt (1)	$ 380	$ 3,180	$ 3,538	$ 4,467	$11,565
Operating leases (2)	994	6,786	6,334	9,680	23,794
Payments on litigation settlement (3)	—	6,000	6,000	—	12,000
Total	**$ 1,374**	**$ 15,966**	**$ 15,872**	**$ 14,147**	**$47,359**

(1) We maintain three term loans through our consolidated affiliates Dolby Properties, LLC, Dolby Properties Burbank, LLC and Dolby Properties United Kingdom, LLC, for financing commercial and real property at various locations in which we are the primary tenant.

(2) Operating lease payments include future minimum rental commitments, including those payable to our principal stockholder, for non-cancelable operating leases of office space as of June 29, 2007.

(3) In April 2002, we settled a dispute with an unrelated third party and agreed to pay a total of $30.0 million in ten equal annual installments of $3.0 million per year beginning in June 2002. Refer to Note 5 “Legal Proceedings” for further discussion.

Other Cash Obligations. Under the terms of the agreement to acquire all outstanding shares of our subsidiary, Cinea in September 2003, we have future payment obligations that equal approximately 5% to 8% of the revenue generated from products incorporating certain technologies we acquired in the transaction though 2022. As of June 29, 2007, no additional purchase consideration had been paid and no liability is reflected on our balance sheet.

8. Recently Issued Accounting Standards

In June 2006, the FASB issued FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* (FIN 48). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise’s financial statements in accordance with FASB Statement of Financial Accounting Standards No. 109, *Accounting for Income Taxes*. This Interpretation defines the minimum recognition threshold a tax position is required to meet before being recognized in the financial statements. FIN 48 is effective for fiscal years beginning after December 15, 2006. We plan to adopt FIN 48 in the first quarter of fiscal 2008. We are currently evaluating the effect that the adoption of FIN 48 will have on our financial position and results of operations.

In September 2006, the Securities and Exchange Commission issued Staff Accounting Bulletin No. 108, *Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements* (SAB 108). SAB 108 provides interpretive guidance on how to evaluate the materiality of an uncorrected misstatement in the current year financial statements using both an income statement approach (the rollover approach) and a balance sheet approach (the iron curtain approach). The rollover approach quantifies a misstatement based on the amount of the error originating in the current year income statement while the iron curtain approach quantifies a misstatement based on the effects of correcting the cumulative misstatement existing in the balance sheet at the end of the current year. SAB 108 is effective for fiscal years ending after November 15, 2006. We plan to adopt SAB 108 in the fourth quarter of fiscal 2007. We are currently evaluating the effect that the adoption of SAB 108 will have on our financial position or results of operations.

In February 2007, the FASB issued Statement of Financial Accounting Standards No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities, including an amendment of FASB Statement No. 115* (SFAS 159). SFAS 159 permits companies to choose to measure many financial instruments and certain other items at fair value that are not currently required to be measured at fair value and establishes presentation and disclosure requirements designed to facilitate comparisons between companies that choose different measurement attributes for similar types of assets and liabilities. The provisions of SFAS 159 become effective as of the beginning of our 2009 fiscal year. We are currently evaluating the impact that SFAS 159 will have on our financial statements.

ITEM 2 – MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis should be read in conjunction with our condensed consolidated financial statements and the related notes that appear elsewhere in this Form 10-Q. These discussions contain forward-looking statements reflecting our current expectations that involve risks and uncertainties. In some cases, you can identify forward-looking statements by terminology such as "may," "will," "should," "expects," "plans," "anticipates," "believes," "estimates," "predicts," "potential," "continue" or the negative of these terms or other comparable terminology. Forward-looking statements include, but are not limited to: demand for and future revenues from the sale of consumer electronics products incorporating our technologies, including traditional and next–generation DVD players; growth opportunities in the consumer electronics market; opportunities to incorporate our technologies in markets outside the traditional consumer electronics market or to deliver technology solutions in areas beyond sound; the impact of inclusion of certain of our technologies in audio standards; the rate of adoption of and sales of next–generation DVD players; diversification of sources of licensing revenue; demand for and future revenues from incorporation of our technologies in personal computers; increase in sales of our products and demand for consumer electronics products containing our technologies in emerging economies; concentration of manufacturing of consumer electronic products containing our technologies in emerging economies and the associated challenges in royalty collection and intellectual property enforcement; our ability to scale our organization and effectively apply our strategy across our markets; pricing strategies for our digital cinema product and competitive pricing pressures for our cinema products; the pace of the movie industry's transition to digital cinema and our expected revenue associated with the transition; the expected timing of revenue and cost recognition for a number of digital cinema systems and our expected product sales and product services gross margins; our expected selling, general and administrative expenses and research and development expenses for the remaining quarter of fiscal 2007; our expected effective tax rate for the remaining quarter of fiscal 2007; our critical accounting policies, including those regarding revenue recognition, allowance for doubtful accounts, accounting for goodwill, accounting for income taxes, personal holding company matters and stock-based compensation; calculations of royalties due to our licensors; statements regarding the sufficiency of our cash reserves; and our expected rate of return on investments. Actual results may differ materially from those discussed in these forward-looking statements due to a number of factors, including: the rate of growth of the markets for consumer electronics that include our technologies; whether PC manufacturers will continue to include additional DVD software applications on personal computers that include Windows Vista Home Premium Edition or Ultimate Edition; whether sales of personal computers with the Home Premium Edition or the Ultimate Edition will be strong; whether our technologies are selected for and remain part of audio standards; the rate of deployment and adoption of next–generation DVD players; the extent to which our expectations regarding new licensing markets are realized; the extent to which consumer electronics manufacturers concentrate their production in emerging economies that present royalty collection and intellectual property enforcement challenges; the extent to which consumers in emerging economies elect to purchase products containing our technologies; the effectiveness of our transition to a functional organizational model; the extent to which professionals using our equipment continue to demand innovative technology solutions developed by us; the pace of the movie industry's transition to digital cinema; our ability to tailor our traditional model of selling to respond to market trends; whether our competitors are able to develop and sell alternative digital cinema technologies to our customers; the accuracy of our identification of critical accounting policies and the accuracy of the assumptions we make in implementing such policies; the accuracy of our estimates regarding our taxable income and cash needs for the next twelve months; the accuracy of our calculations of royalties due to our licensors; fluctuations in interest rates; and risks set forth in the section entitled "Risk Factors" in Part II, Item 1A of this Quarterly Report on Form 10-Q and elsewhere in this filing. Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance or achievements. Moreover, neither we nor any other person assumes responsibility for the accuracy and completeness of these forward-looking statements. We are under no duty to update any of the forward-looking statements after the date of this Quarterly Report on Form 10-Q to conform our prior statements to actual results. The periods presented herein consist of our third quarters of fiscal 2006 and 2007 and the fiscal year-to-date periods ended June 30, 2006 and June 29, 2007. Our fiscal year-to-date periods ended June 30, 2006 and June 29, 2007, both consisted of 39 weeks. Our 2007 fiscal year consists of 52 weeks and ends on September 28, 2007. The results for the fiscal quarter and fiscal year-to-date period ended June 29, 2007 are not necessarily indicative of the results to be expected for any subsequent quarterly or annual financial period, including the fiscal year ending September 28, 2007.

Overview

Dolby Laboratories develops and delivers innovative products and technologies that make the entertainment experience more realistic and immersive. Since Ray Dolby founded Dolby Laboratories in 1965, we have been at the forefront of delivering sound technologies that assist the entertainment creation process and enhance the entertainment experience. Today, Dolby technologies are standard in a wide range of entertainment platforms. For example, Dolby products are widely used in movie theatres around the world and our technologies are used in virtually all DVD players and DVD playback software for personal computers. In addition, Dolby Digital is mandated in all North American digital televisions and digital set-top boxes that include Advanced Television Systems Committee (ATSC) television tuners and is widely included in high-definition set-top boxes used for European high-definition television broadcasts.

Historically, we have conducted our business in two operating segments: licensing our technologies to manufacturers of consumer electronics products and software developers, and selling our professional products and related services.

In an effort to improve our ability to scale our organization and effectively apply our strategy across our markets, in the third quarter of fiscal 2007 we decided to reorganize our business from two operating segments into a functional organizational model. As a result, there will be a products and technology group responsible for research, engineering, product development, manufacturing and technology and there will be a sales and marketing group responsible for all sales, marketing, business development and field operations. The world-wide corporate support functions will continue to support the overall needs of the business. The change will take effect in the fourth quarter of fiscal 2007.

In our technology licensing segment, we work with manufacturers of integrated circuits (ICs) to help them incorporate our technologies into their ICs. These manufacturers then sell ICs to product manufacturers that license our technologies for incorporation in products such as DVD players, DVD recorders, audio/video receivers, television sets, set-top boxes, video game consoles, portable audio and video players, personal computers, in-car entertainment systems and other consumer electronics products. We also license our technologies to software developers who implement our technologies for use in personal computer software products. Our licensing arrangements typically entitle us to receive a specified royalty for every product shipped by product manufacturers or software developer licensees that incorporate our technologies. We do not receive royalties from IC manufacturers. We also collect fees for administering joint licensing programs (commonly referred to as “patent pools”) on behalf of third parties. In fiscal 2005, 2006 and the fiscal year-to-date period ended June 29, 2007 our licensing revenue represented 75%, 77% and 80% of our total revenue, respectively.

In our products and services segment, we design, manufacture and sell audio products for the motion picture, broadcast, music and video game industries to improve sound quality, provide surround sound and increase the efficiency of sound storage and distribution. The majority of our professional product revenue is derived from sales of cinema processors, which movie theatres use to process film soundtracks, and to a lesser extent, from sales of broadcast products, which broadcasters use to distribute content encoded with our technologies. Our services revenue is primarily generated by service agreements with motion picture production companies who utilize our services and equipment. Our sound engineers work alongside filmmakers, television broadcasters, music producers and video game designers to help them use our products to create and reproduce the sound they envision. Our sound engineers also provide training, system design expertise and on-site technical expertise to cinema operators to help them configure their theatres and sound equipment to ensure that movie soundtracks are replayed with consistent high-quality sound. In our digital cinema content preparation service unit we act as a technical agent for our clients, following the content from start to finish, providing the compression mastering and distribution media preparation, distribution and verification services.

We believe that our long history of developing innovative technology solutions for the entertainment industry and our well-established relationships with industry participants provide us with opportunities to deliver technology solutions in areas beyond sound. In recent years we have expanded our business to offer technologies to facilitate delivery of digital entertainment, including digital cinema technologies for processing digital moving images and content protection. In addition, we are exploring other areas where we may be able to develop and deliver technologies that enrich the entertainment experience, including technologies for imaging and display and mobile devices.

On April 25, 2007 we acquired all outstanding shares of Brightside Technologies Inc. (Brightside), a privately held provider of high-dynamic range image technology. The technology acquired through this acquisition focuses on enabling the capture, distribution, and display of more vibrant video on LCD TV sets, as well as front-projection and rear-projection TVs.

We are a global organization. We have licensed our technologies to manufacturers in approximately 35 countries, including countries in North America, Europe and Asia. In fiscal 2005, 2006 and the fiscal year-to-date period ended June 29, 2007, revenue from licensees outside the United States represented 76%, 77% and 74% of our licensing revenue, respectively. Our licensees distribute products incorporating our technologies throughout the world. We sell our professional products and services in over 50 countries. In fiscal 2005, 2006 and the fiscal year-to-date period ended June 29, 2007, revenue from sales outside the United States represented 61%, 64% and 62% of our professional products sales and services revenue, respectively. Most of our revenue is derived from transactions denominated in United States dollars.

Management Discussion Regarding Opportunities, Challenges and Risks

Licensing revenue constitutes the majority of our total revenue, representing 75%, 77% and 80% of total revenue in fiscal 2005, 2006 and the fiscal year-to-date period ended June 29, 2007, respectively. We categorize our licensing revenue into the following markets:

- Consumer electronics (CE) market – primarily comprised of DVD players, DVD recorders, audio/video receivers and home-theatres-in-a-box.
- Personal computer (PC) market – primarily comprised of software DVD players and DVD authoring applications.
- Broadcast market – primarily comprised of televisions and television set-top boxes.
- Gaming market – primarily comprised of video game consoles.
- Automotive market – comprised of in-car entertainment products.
- Licensing services – revenue from joint licensing program administration performed by our subsidiary Via Licensing.

Historically, the consumer electronics market, which is driven primarily by revenue attributable to DVD player sales, has been our largest market, generating just over 50% of our licensing revenue in fiscal 2005 and approximately 45% of our licensing revenue in fiscal 2006. We expect next-generation DVD players for high-definition content to be a growth opportunity in the consumer electronics market. Our Dolby Digital, Dolby Digital Plus and TrueHD technologies have been selected as mandatory audio standards in the High-Definition Digital Versatile Disc (HD-DVD) format. Dolby Digital has been selected as a mandatory audio standard and Dolby Digital Plus and TrueHD have been selected as optional audio standards in the Blu-ray Disc format. However, the release and consumer adoption of next-generation DVD players has been slower than expected due, in part, to the competing HD-DVD and Blu-ray Disc formats. Consequently, our ability to generate significant royalties from incorporation of our technology in next-generation DVD players has been delayed. Even assuming resolution of the competing disc format conflict, the rate of consumer adoption of next-generation DVD players is uncertain and may be slower than past growth rates of traditional DVD players. Furthermore, as the market for traditional DVD players continues to mature, the industry has moved towards lower-end Chinese-made DVD players, which we believe poses challenges in royalty collection and intellectual property enforcement in China.

We are continuing to diversify our sources of licensing revenue by actively promoting the incorporation of our technologies for use in growing markets outside of our traditional consumer electronics market, such as personal computers, broadcast, gaming and automotive. As a result, we expect that revenue from our consumer electronics market will decrease as a percentage of licensing revenue in fiscal 2007.

The personal computing market, which represented over 25% of our licensing revenue in fiscal 2005 and just over 30% in fiscal 2006, has been primarily driven by demand for software DVD players and to a lesser extent, DVD authoring applications. Historically, PC manufacturers have frequently included DVD playback functionality as part of the software applications included in their products. Microsoft recently introduced its Windows Vista operating system. Two of the six editions of this operating system, the Windows Vista Home Premium Edition and the Windows Vista Ultimate Edition, include Dolby technologies which help enable DVD playback functionality and DVD authoring capabilities. To date, sales of personal computers for the consumer market shipped with the Home Premium Edition have been strong. In addition, many major PC manufacturers continue to include additional branded software applications with DVD playback capabilities and other features that PC manufacturers have selected for inclusion and which are not provided in the Microsoft operating systems.

This contributed to an increase in licensing revenue from our PC market in the third quarter of fiscal 2007 and we expect revenue from our PC market to increase as a percentage of licensing revenue for fiscal 2007. In the future, PC manufacturers may elect to exclude additional DVD software applications on personal computers that include the Windows Vista Home Premium Edition or Windows Vista Ultimate Edition. Additionally, it is unclear at what pace business customers will migrate from their current operating systems to the Windows Vista operating systems and how such adoption will impact sales of software DVD players for business PCs.

The broadcast market, which is primarily driven by demand for Dolby Digital in televisions and set-top boxes, represented approximately 10% of our licensing revenue in fiscal 2005 and just over 10% in fiscal 2006. The broadcast market has benefited in recent years from the transition from analog televisions to digital televisions, including high definition television (HDTV). We expect that revenue from our broadcast market will increase as a percentage of licensing revenue in fiscal 2007. Revenue generated from the gaming and automotive markets has primarily been driven by demand for Dolby Digital and ATRAC technology in video game consoles and Dolby Digital in in-car entertainment systems.

Any future growth in the PC, broadcast, gaming and automotive markets may not fully offset a potential decline in the growth of revenue generated from our consumer electronics market.

Our technologies are incorporated in consumer electronics and digital entertainment products throughout the world. We expect that sales of products incorporating our technologies in emerging economies, such as China and India, will increase in the future as consumers in these geographical markets have more disposable income available for increased purchases of entertainment products, although there can be no assurance that this will occur. We also expect that manufacturers from lower-cost manufacturing countries, including China, will increase production of consumer electronics and digital entertainment products in the future to satisfy this increased demand. Associated with opportunities of doing business in these emerging economies, such as China, are unique risks that have and will continue to affect our operating results, such as manufacturers failing to report or underreporting product shipments. In an effort to better serve our licensees and address these risks we have expanded our presence in Asia, with offices in Taiwan, Shenzhen and Seoul and a product testing center in the Shanghai Waigaoqiao Free Trade Zone.

Revenue from the sale of our products and services represented 25%, 23% and 20% of total revenue in fiscal 2005, 2006 and the fiscal year-to-date period ended June 29, 2007, respectively. We are committed to developing technologies for use by professionals in the entertainment industry. We believe that filmmakers, broadcasters, music producers and video game designers will continue to push for technology solutions to help create, distribute and play back rich, high quality sounds and images. As a result, we believe that major advances in sound, imaging and other technologies for the recording, delivery and playback of entertainment likely will be introduced first in products designed for use by professionals.

Sales of our professional products and services tend to fluctuate based on the underlying trends in the motion picture and broadcast industries. For example, when box office receipts for the motion picture industry increase, we have typically seen sales of our professional cinema products increase as well, as cinema owners are more likely to build new theatres and upgrade existing theatres with our more advanced cinema products when they are doing well financially. Conversely, when box office receipts are down cinema owners tend to scale back on plans to upgrade their systems or build new theatres. In the broadcast industry, consumer demand for high-quality broadcasts can drive broadcasters to purchase our professional broadcast products. For example, broadcasters seeking to deliver content to consumers in Dolby Digital 5.1 surround sound positively affected sales of our professional broadcast products in fiscal 2006.

Our services revenue, both in the United States and internationally, is also tied to the strength of the motion picture production industry and, in particular, to the number of films being made by studios and independent filmmakers. The number of films that are produced can be affected by a number of factors, including strikes and work-stoppages within the motion picture industry as well as by the tax incentive arrangements that many foreign governments provide filmmakers to promote local filmmaking.

In recent years we have developed a digital cinema system which allows for the storage and playback of digital content in theatres. Helping the motion picture industry transition to digital cinema continues to be a major initiative in our products and services segment. Digital cinema offers the motion picture industry possible means to achieve substantial cost savings in printing and distributing movies, to combat piracy, and to enable movies to be played repeatedly without degradation in image and audio quality. It also provides additional revenue opportunities for cinema operators, as concerts and sporting events already in digital format could be broadcast live via satellite to digitally-equipped theatres. We have made significant investments in our digital cinema initiative, and if our digital cinema systems are not widely deployed, our future prospects in digital cinema will be limited and our business could be materially and adversely affected.

The cinema industry is still in the early stages of the adoption of digital cinema for the distribution and exhibition of movies. A number of competitors offer competing products for digital cinema, some of which are priced lower than our products. At least one competitor has a significantly greater installed base of its competing digital cinema products than we do which could limit our eventual share of the digital cinema product market. We expect that as the market for digital cinema grows we will face more competitive pricing pressures than we have traditionally experienced for cinema products. As a result, we have had to implement pricing strategies which will have an adverse impact on our product sales gross margins in the future.

Furthermore, if the market for digital cinema develops more slowly than we anticipate or if we do not identify opportunities and successfully execute our initiatives to participate in the emerging digital cinema market, our significant investment in digital cinema technology may not yield the returns we anticipate and our business could be adversely affected.

In recent years, our products and services segment has grown more slowly than our technology licensing segment. In addition, the profit margin for our products and services segment has been lower than our technology licensing segment and is expected to remain so. Future initiatives associated with digital cinema in this competitive market also may adversely affect our gross margin.

Critical Accounting Policies

The discussion and analysis of our financial condition and results of operations are based on our condensed consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America, or U.S. GAAP. The preparation of these financial statements in accordance with U.S. GAAP requires us to utilize accounting policies and make certain estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingencies as of the date of the financial statements and the reported amounts of revenue and expenses during a fiscal period. The SEC considers an accounting policy to be critical if it is both important to a company's financial condition and results of operations and it requires significant judgment and estimates on the part of management in its application. We have discussed the selection and development of the critical accounting policies with the audit committee of our board of directors, and the audit committee has reviewed our related disclosures in this Form 10-Q. Although we believe that our judgments and estimates are appropriate and correct, actual results may differ from those estimates.

The following are our critical accounting policies because we believe they are both important to the portrayal of our financial condition and results of operations and require critical management judgments and estimates about matters that are uncertain. If actual results or events differ materially from those contemplated by us in making these estimates, our reported financial condition and results of operation for future periods could be materially affected. See "Risk Factors" for certain matters bearing risks on our future results of operations.

Revenue Recognition

We evaluate revenue recognition for transactions to sell products and services and to license technology, trademarks and know-how using the criteria set forth by the SEC in Staff Accounting Bulletin 104, *Revenue Recognition* (SAB 104). For revenue transactions that involve software or software-related products, such as certain fees we earn from integrated software vendors (ISVs), certain product sales and certain other transactions with licensees, we recognize revenue under the guidance established by Statement of Position No. 97-2, *Software Revenue Recognition* (SOP 97-2). Both SAB 104 and SOP 97-2 state that revenue is recognized when each of the following criteria is met: persuasive evidence of an arrangement exists, delivery has occurred or services have been rendered, the seller's price to the buyer is fixed or determinable, and collectibility is probable.

Licensing. Our licensing revenue is primarily derived from royalties paid to us by licensees of our intellectual property rights, including patents, trademarks and know-how. Royalties are recognized when all revenue recognition criteria have been met. We make judgments as to collectibility based on the licensee's recent payment history, the existence of a standby letter-of-credit between the licensee's financial institution and our financial institution, or an evaluation of the licensee's creditworthiness. In cases where collectibility is not probable, we recognize revenue upon receipt of cash, provided that all other revenue recognition criteria have been met.

We generate the majority of our licensing revenue through our licensing contracts with original equipment manufacturers (system licensees) and independent software vendors. Our revenue recognition policies for each of these arrangements are summarized below.

Licensing to system licensees. We license our technologies to system licensees who manufacture consumer electronic devices and, in return, the system licensee pays us a royalty for each unit shipped that incorporates our technologies. Royalties from system licensees are generally recognized upon receipt of a royalty report from the licensee and when all other revenue recognition criteria have been met.

Licensing to independent software vendors. We license our technologies for resale to independent software vendors and, in return, the software vendor pays us a royalty for each unit of software distributed that incorporates our technologies. Royalties from ISVs are generally recognized upon receipt of a royalty report from the licensee and when all other revenue recognition criteria have been met.

Product Sales and Services. Our revenue from the sale of products is recognized when the risk of ownership has transferred to our customer as provided under the terms of the governing purchase agreement, typically when the product has been shipped to the customer, and all the other revenue recognition criteria have been met. Generally, these purchase agreements provide that the risk of ownership is transferred to the customer when the product is shipped. Services are recognized as the services related to a given project are completed and all other revenue recognition criteria have been met.

Multiple-Element Arrangements. We enter into arrangements that include multiple elements such as hardware, software, maintenance and other services. Revenue from these arrangements is allocated based on the fair value of each element. The allocated revenue for each element is recognized when all revenue recognition criteria for that element has been met. If we cannot objectively determine the fair value of any undelivered element included in a multiple-element arrangement, we defer revenue until all elements are delivered and/or services have been performed, or until we can objectively determine the fair value of all remaining undelivered elements. When the undelivered element is support, revenue for the entire arrangement is bundled and recognized ratably over the support period. When our products have been delivered as part of a multiple-element arrangement, but the revenue associated with that product is deferred because the related revenue recognition criteria have not been met, we also defer the related inventory costs for the delivered items in accordance with Accounting Research Bulletin No. 43, *Restatement and Revision of Accounting Research Bulletins*.

Allowance for Doubtful Accounts

We continually monitor customer payments and maintain a reserve for estimated losses resulting from our customers' inability to make required payments. In determining the reserve, we evaluate the collectibility of our accounts receivable based upon a variety of factors. In cases where we are aware of circumstances that may impair a specific customer's ability to meet its financial obligations, we record a specific allowance against amounts due, thereby reducing the net recognized receivable to the amount reasonably believed to be collectible. For all other customers, we recognize allowances for doubtful accounts based on our actual historical write-off experience in conjunction with the length of time the receivables are past due, customer creditworthiness, geographic risk and the current business environment. Actual future losses from uncollectible accounts may differ from our estimates and may have a material effect on our consolidated statements of operations and our financial condition. Our allowance for doubtful accounts totaled $1.1 million at June 29, 2007. An incremental change of 1% in our allowance for doubtful accounts as a percentage of trade accounts receivables would have a $0.1 million increase or decrease in our operating results.

Goodwill

We account for goodwill in accordance with Statement of Financial Accounting Standards No. 142, *Goodwill and Other Intangible Assets* (SFAS 142). As required by SFAS 142, we perform an impairment test on recorded goodwill by comparing the estimated fair value of each of our reporting units to the carrying value of the assets and liabilities of each unit, including goodwill. The fair value of each of our reporting units is determined by using a discounted cash-flow model which considers a number of factors, including estimated future cash-flows, risks facing us and our current market capitalization. If the carrying value of the assets and liabilities of the reporting units, including goodwill, were to exceed our estimation of the fair value of the reporting units, we would record an impairment charge in an amount equal to the excess of the carrying value of goodwill over the implied fair value of the goodwill. Our fiscal 2007 impairment test of goodwill, which was performed in the third quarter of fiscal 2007, resulted in no impairment charge. Fluctuations in our fair value, which may result from changes in economic conditions, our results of operations and other factors, relative to the carrying value, could result in impairment charges in future periods.

Accounting for Income Taxes

In preparing our consolidated financial statements, we are required to make estimates and judgments that affect our accounting for income taxes. This process includes estimating actual current tax exposure together with assessing temporary differences resulting from differing treatment of items for tax and accounting purposes. These differences, including differences in the timing of recognition of stock-based compensation expense, result in deferred tax assets and liabilities, which are included in our consolidated balance sheets. We also assess the likelihood that our deferred tax assets will be recovered from future taxable income and, to the extent that we believe that recovery is not likely, we have established a valuation allowance.

Significant judgment is required in determining the provision for income taxes, deferred tax assets and liabilities and the valuation allowance against our deferred tax assets. Our financial position and results of operations may be materially impacted if actual results significantly differ from these estimates or the estimates are adjusted in future periods.

Personal Holding Company Tax Matters. For United States federal income tax purposes, a corporation is generally considered to be a "personal holding company" under the United States Internal Revenue Code if (i) at any time during the last half of its taxable year more than 50% of its stock by value is owned, directly or indirectly, by virtue of the application of certain stock ownership attribution rules set forth in the Internal Revenue Code for purposes of applying the personal holding company rules, by five or fewer individuals and (ii) at least 60% of its adjusted ordinary gross income, as defined for United States federal income tax purposes, is "personal holding company income." Personal holding company income is generally passive income, including royalty income, subject to certain exceptions such as qualifying software royalties. A personal holding company is subject to an additional tax on its undistributed after-tax income, calculated at the statutory tax rate, which is currently 15%. Since the personal holding company tax is imposed only on undistributed income, a personal holding company can avoid or mitigate liability for the tax, but not interest or penalties, by paying a dividend to its stockholders.

During fiscal 2006 and the fiscal year-to-date period ended June 29, 2007, more than 50% of the value of our stock was held by Ray Dolby and stockholders considered affiliated with him pursuant to the stock ownership attribution rules applicable to personal holding companies. We expect this will continue to be the case in the foreseeable future. In addition, a significant portion of our income is from licensing fees, which may constitute personal holding company income. Currently, however, less than 60% of Dolby Laboratories' adjusted ordinary gross income is personal holding company income. Given our current sources of revenue, we believe that neither we nor any of our subsidiaries is currently liable for personal holding company tax.

Stock-Based Compensation

We account for stock-based compensation under the provisions of Statement of Financial Accounting Standards No. 123(R), *Share-Based Payment* (SFAS 123R). SFAS 123R requires measurement of all employee stock-based compensation awards using a fair-value method and recording of such expense in the consolidated financial statements over the requisite service period. In the third quarter of fiscal 2007, we recorded stock-based compensation expense of $5.1 million under the fair-value provisions of SFAS 123R, compared to $4.7 million in the third quarter of fiscal 2006. In the fiscal year-to-date period ended June 29, 2007 we recorded stock-based compensation expense of $14.8 million, compared to $14.9 million in the year-to-date period ended June 30, 2006. See Note 4 "Stockholders' Equity and Stock-Based Compensation" for further discussion.

Results of Operations

Revenue

	Fiscal Quarter Ended		Change		Fiscal Year-to-Date Ended		Change	
	June 30, 2006	June 29, 2007	$	%	June 30, 2006	June 29, 2007	$	%
			($ in thousands)					
Revenue:								
Licensing	$69,138	$ 94,795	$25,657	37%	$221,303	$283,812	$62,509	28%
Percentage of total revenue	*74%*	*79%*			*77%*	*80%*		
Product sales	18,862	17,191	(1,671)	(9)%	50,574	47,870	(2,704)	(5)%
Percentage of total revenue	*20%*	*14%*			*17%*	*14%*		
Production services	5,650	7,627	1,977	35%	17,522	21,383	3,861	22%
Percentage of total revenue	*6%*	*7%*			*6%*	*6%*		
Total revenue	**$93,650**	**$119,613**	**$25,963**	**28%**	**$289,399**	**$353,065**	**$63,666**	**22%**

Licensing. The $25.7 million, or 37%, increase in licensing revenue from the third quarter of fiscal 2006 to the third quarter of fiscal 2007 was primarily due to increased revenue from our personal computer market and broadcast market. The increase in revenue from our PC market was primarily driven by continued growth in shipments of notebook computers, the release of Microsoft Vista, in particular, the Microsoft Vista Home Premium and Ultimate Editions which contain Dolby technologies, as well as the continued inclusion of additional software DVD player applications by PC manufacturers. The increase in revenue from our broadcast market has been driven by growth in sales of digital televisions and cable and satellite set-top boxes that incorporate our technologies.

The $62.5 million, or 28%, increase in licensing revenue from the fiscal year-to-date period ended June 30, 2006 to the fiscal year-to-date period ended June 29, 2007 was primarily due to increased revenue from our personal computer market and broadcast market and, to a lesser extent, our consumer electronics market.

Product Sales. The $1.7 million, or 9%, decrease in our product sales revenue from the third quarter of fiscal 2006 to the third quarter of fiscal 2007 was principally attributable to a decrease in sales of our cinema products. In the third quarter of fiscal 2006, sales of cinema products were favorably impacted by orders from several customers in anticipation of an announced price increase. We have not announced a price increase for our cinema products this year, and as a result, did not see a similar affect in the third quarter of fiscal 2007.

The $2.7 million, or 5%, decrease in our products sales revenue from the fiscal year-to-date period ended June 30, 2006 to the fiscal year-to-date period ended June 29, 2007 was due to a decrease in both cinema and broadcast products from the comparable period of last year. These decreases were due to the acceleration of orders of cinema products by several customers in fiscal 2006 in anticipation of a price increase, as mentioned above, and sales of broadcast products in advance of the 2006 World Cup soccer tournament.

Services. The $2.0 million, or 35%, increase in service revenue from the third quarter of fiscal 2006 to the third quarter of fiscal 2007 and the $3.9 million, or 22%, increase from the fiscal year-to-date period ended June 30, 2006 to the fiscal year-to-date period ended June 30, 2007 was principally attributable to an increase in film services, particularly services on original films, including digital films.

Gross Margin

	Fiscal Quarter Ended		Fiscal Year-to-Date Ended	
	June 30, 2006	June 29, 2007	June 30, 2006	June 29, 2007
Gross margin:				
Licensing gross margin percentage	*91%*	*91%*	*91%*	*91%*
Product sales margin percentage	*46%*	*53%*	*41%*	*49%*
Production services gross margin percentage	*52%*	*61%*	*55%*	*60%*
Total gross margin percentage	**80%**	**84%**	**80%**	**83%**

Licensing Gross Margin. We license intellectual property to our customers that may be internally developed, acquired by us or licensed from other parties. Our cost of licensing consists principally of royalty obligations to third parties for the licensing of intellectual property rights that we sublicense as part of our licensing arrangements with our customers. Our cost of licensing also includes amortization expenses associated with purchased intangible assets.

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Cost of licensing for the third quarter of fiscal 2007 and the fiscal year-to-date period ended June 29, 2007 was $8.5 million and $26.3 million, respectively, which includes approximately $7.3 million and $21.9 million, respectively, in royalty expense related to the license of certain patents under a license agreement with an unrelated third party. In the third quarter of fiscal 2006, we evaluated whether the patents licensed to us under the license agreement covered all of the products and technologies for which we had historically been paying royalties to the patent licensor. Based on our evaluation, we determined that under the license agreement we may not owe royalties to the patent licensor on all the products and technologies for which we had historically been paying. In the third quarter of fiscal 2006, we notified the patent licensor that going forward we intended to pay royalties only for products and technologies that we believe are covered by the patents licensed under the license agreement, and subsequently, we have been paying the patent licensor royalties on this basis. In the second quarter of fiscal 2007, the patent licensor informed us that it disagreed with our interpretation of the license agreement. While we are trying to resolve this matter with the patent licensor, there continues to be uncertainty regarding the outcome. As a result, we have continued to accrue royalty expense in a manner consistent with our historical payments. Accrued royalties for unpaid amounts related to this patent licensor from the third quarter of fiscal 2006 to the third quarter of fiscal 2007 were approximately $29.8 million at June 29, 2007.

Product Sales Gross Margin. Cost of product sales primarily consists of material costs related to the products sold, applied labor and manufacturing overhead and, to a lesser extent, amortization of certain intangible assets. In the third quarter of fiscal 2006, an increase in our reserves related to certain products, negatively impacted product sales gross margin. The increase in product sales gross margin from 46% in the third quarter of fiscal 2006 to 53% in the third quarter of fiscal 2007 was primarily due to a decrease in these charges compared to the same period of last year. Upon satisfying certain obligations, we expect to recognize revenue and associated costs related to a number of digital cinema systems that are currently deferred. We expect to recognize these transactions in fiscal 2008, and we expect that upon the eventual recognition, our product sales gross margins will be adversely impacted because these products were sold at a significantly lower margin than our other professional products.

In the third quarter of fiscal 2005 we entered into a collaboration agreement with Walt Disney Pictures and Television under which we deployed digital cinema systems in selected theatres throughout the U.S. We funded the majority of the equipment and installation costs related to this deployment, of which the majority was recorded in the fourth quarter of fiscal 2005 and the first quarter of fiscal 2006. Cost of product sales for the fiscal year-to-date period ended June 30, 2006 includes a $6.0 million charge recorded in connection with this collaboration agreement. The increase in product sales gross margin from 41% for the fiscal year-to-date period ended June 30, 2006 to 49% for the fiscal year-to-date period ended June 29, 2007 was primarily due to this charge.

Services Gross Margin. Cost of services primarily consists of the payroll and benefits costs of employees performing our professional services, the cost of outside consultants and reimbursable expenses incurred on behalf of customers. Cost of services for the fiscal year-to-date period ended June 30, 2006 includes a $0.8 million charge recorded in the first quarter of fiscal 2006 related to services provided in connection with the digital cinema collaboration with Walt Disney Pictures and Television discussed above. The increase in services gross margin from the fiscal year-to-date period ended June 30, 2006 to the fiscal year-to-date period ended June 29, 2007 was primarily due to this charge. An increase in the number of movies and increase in virtual print fees also contributed to a higher gross margin.

Operating Expenses

	Fiscal Quarter Ended		Change		Fiscal Year-to-Date Ended		Change	
	June 30, 2006	June 29, 2007	$	%	June 30, 2006	June 29, 2007	$	%
				($ in thousands)				
Operating expenses:								
Selling, general and administrative	$38,477	$48,430	$ 9,953	26%	$113,598	$128,266	$14,668	13%
Percentage of total revenue	*41%*	*40%*			*39%*	*36%*		
Research and development	9,108	11,854	2,746	30%	25,413	31,650	6,237	25%
Percentage of total revenue	*10%*	*10%*			*9%*	*9%*		
Gain on settlements	—	(350)	(350)	n/a	—	(1,850)	(1,850)	n/a
Percentage of total revenue	—	*n/a*			—	*n/a*		
Total operating expenses	**$47,585**	**$59,934**	**$12,349**	**26%**	**$139,011**	**$158,066**	**$19,055**	**14%**

Selling, General and Administrative. Selling, general and administrative expense consists primarily of personnel and personnel-related expenses, professional service fees and facility costs for our sales, marketing and administrative functions. The $10.0 million, or 26%, increase in selling, general and administrative expenses from the third quarter of fiscal 2006 to the third quarter of fiscal 2007 was primarily due to an increase in personnel expenses and related occupancy and travel expenses. These increases were primarily driven by increases in headcount, bonus expense due to our financial performance exceeding our targets and annual pay increases for existing employees. Selling, general and administrative expenses also increased due to increases in professional consulting fees, as well as an increase in bad debt expense. We expect to continue to incur increased levels of selling, general and administrative expenses through the remainder of fiscal 2007 as we continue to increase headcount and expand our sales and marketing capabilities.

The $14.7 million, or 13%, increase in selling, general and administrative expenses from the fiscal year-to-date period ended June 30, 2006 to the fiscal year-to-date period ended June 29, 2007 was primarily due to the same reasons discussed above with respect to the third quarter of fiscal 2007.

Research and Development. Research and development expense consists primarily of compensation and benefits related costs for personnel responsible for the research and development of new technologies and products. The $2.7 million, or 30%, increase in research and development expense from the third quarter of fiscal 2006 to the third quarter of fiscal 2007 was primarily driven by an increase in personnel expenses due to an increase in headcount, largely attributable to the acquisition of Brightside, as well as increases in bonus expense and annual pay increases for existing employees.

The $6.2 million, or 25%, increase in research and development expenses from the fiscal year-to-date period ended June 30, 2006 to the fiscal year-to-date period ended June 29, 2007 was primarily driven by an increase in personnel expenses due to increases in headcount, bonus expense and annual pay increases for existing employees. In addition, there were increases in engineering costs related to a variety of research projects, such as imaging, including 3-D and high-dynamic range technologies, and next-generation broadcast platforms.

Gain on Settlements. Gain on settlements includes payments received related to the resolution of disputes with IC manufacturers from which we typically do not earn royalties. In contrast, amounts attributable to the resolution of royalty disputes from licensees that specifically represent unpaid royalties are recorded as licensing revenue in the period payment is received, if all other revenue recognition criteria have been met. In the third quarter of fiscal 2007, we recognized $0.4 million as gain on settlement in connection with the resolution of disputes with two IC manufacturers regarding the violation of the terms of their licensing agreements with us.

Other Income, Net

	Fiscal Quarter Ended		Change		Fiscal Year-to-Date Ended		Change	
	June 30, 2006	June 29, 2007	$	%	June 30, 2006	June 29, 2007	$	%
	($ in thousands)							
Interest income	$ 4,671	$ 6,592	$1,921	41%	$ 13,383	$ 19,216	$5,833	44%
Interest expense	(477)	(825)	(348)	73%	(1,327)	(1,751)	(424)	32%
Other income (expense), net	(174)	(8)	166	95%	257	(347)	(604)	n/a
Other income, net	**$ 4,020**	**$ 5,759**	**$1,739**	**43%**	**$ 12,313**	**$ 17,118**	**$4,805**	**39%**

Other income, net, primarily consists of interest income earned on cash, cash equivalent and investment balances, offset by interest expense on outstanding balances on our facility debt obligations. Also included are gains and losses on interest rate swap agreements associated with our facility debt obligations and foreign exchange rate fluctuations. The increase in other income of $1.7 million, or 43% from the third quarter of fiscal 2006 to the third quarter of fiscal 2007 was due to an increase in interest income driven by the investment of our available cash into short-term and long-term investments, as well as higher total cash, cash equivalents and investment balances driven by cash generated from operations.

Income Taxes

	Fiscal Quarter Ended		Fiscal Year-to-Date Ended	
	June 30, 2006	June 29, 2007	June 30, 2006	June 29, 2007
	($ in thousands)			
Income taxes:				
Provision for income taxes	$11,778	$15,839	$39,916	$53,067
Effective tax rate	*38%*	*35%*	*38%*	*35%*

Our effective tax rate is based upon a projection of annual fiscal year results. Our effective tax rate in the third quarter of fiscal 2006 was 38%, compared to 35% for the third quarter of fiscal 2007 and 38% for the fiscal year-to-date period ended June 30, 2006, compared to 35% for the fiscal year-to-date period ended June 29, 2007. The decrease in our effective tax rate from the third quarter of fiscal 2006 to the third quarter of fiscal 2007 was due primarily to the increase in projected tax-exempt interest income. In the third quarter of fiscal 2007, we determined that we had incorrectly estimated the amount of tax-free interest income that we expect for the full year of fiscal 2007. As a result, we adjusted our provision for income taxes in the third quarter of fiscal 2007 by $1.4 million related to the first two quarters of fiscal 2007. We concluded that the impact of this adjustment was not material to the third quarter of fiscal 2007 or any prior quarters.

The change in our effective tax rate for the fiscal year-to-date period ended June 29, 2006 to the fiscal year-to-date period ended June 29, 2007 was due primarily to a taxable gain on the transfer of intellectual property from a foreign subsidiary in the second quarter of fiscal 2006, an increase in tax deductions related to disqualifying dispositions of incentive stock options, an increase in the projected tax-exempt interest income and an increase in research and development tax credits resulting from a change in the tax law. This change in tax law reinstated the research and development tax credits for periods prior to fiscal 2007.

Liquidity and Capital Resources

The following table presents selected financial information for the fiscal quarters ended on the dates indicated:

	September 29, 2006	June 29, 2007
	(in thousands)	
Cash and cash equivalents	$ 363,537	$325,909
Short-term investments	122,162	210,548
Long-term investments	32,909	80,047
Accounts receivable, net	23,550	25,021
Accounts payable and accrued liabilities	79,336	103,223
Working capital (a)	479,778	545,183

	June 30, 2006	June 29, 2007
	(in thousands)	
Cash flows from operating activities (fiscal year-to-date)	86,420	105,477
Capital expenditures (fiscal year-to-date) (b)	5,697	6,945
Cash flows from investing activities (fiscal year-to-date)	156,791	172,048
Cash flows from financing activities (fiscal year-to-date)	16,521	25,657

(a) Working capital consists of total current assets less total current liabilities.

(b) Capital expenditures primarily consist of purchases of office equipment, building fixtures, computer hardware and software, leasehold improvements and production and test equipment.

As of June 29, 2007, we had cash and cash equivalents of $325.9 million, compared to $363.5 million at September 29, 2006. In addition, at June 29, 2007 we had short-term and long-term investments of $290.6 million, compared to $155.1 million at September 29, 2006. During the second quarter of fiscal 2007, we determined that certain immaterial corrections were needed to properly classify variable rate demand notes (VRDNs) as short-term investments rather than cash and cash equivalents, which resulted in a reduction of cash and cash equivalents of $49.0 million and a corresponding increase in short-term investments of the same amount as of September 29, 2006. The decrease in cash and cash equivalents of $37.6 million from September 29, 2006 to June 29, 2007 was primarily due to cash used in investing activities of $172.0 million primarily due to net purchases of available-for-sale securities, partially offset by cash generated from operating and financing activities of $131.1 million.

Cash flow from operating activities for the fiscal year-to-date period ending June 29, 2007 was primarily driven by net income of $98.7 million. Net income included non-cash expenses of $25.3 million related to stock-based compensation expense and depreciation and amortization for the fiscal year-to-date period ended June 29 2007. Cash flows from operating activities were partially reduced by $18.5 million of excess tax benefits upon the exercise of stock options. We believe that our cash, cash equivalents and potential cash flow from operating activities will be sufficient to satisfy our cash requirements through at least the next 12 months.

Cash used in investing activities was $172.0 million for fiscal year-to-date period ended June 29, 2007, which was primarily due to net purchases of available-for-sale securities of $134.2 million, and the acquisition of Brightside for $30.2 million. In addition, capital expenditures were $6.9 million for the period.

Cash provided by financing activities was $25.7 million for fiscal year-to-date period ended June 29, 2007. Cash provided by financing activities was primarily driven by proceeds and excess tax benefits from the exercise of stock options, as well as the issuance of common stock related to our Employee Stock Purchase Plan.

Personal Holding Company Tax Matters

If we or any of our subsidiaries were to become liable for personal holding company tax, we expect that it is likely that instead of paying the personal holding company tax, we would elect to pay a dividend to our stockholders in an amount equal to all or a significant part of our undistributed personal holding company income. We expect that we would pay such a dividend out of our available working capital, which could significantly decrease our cash, unless we sought additional financing for this purpose. Any such financing might not be available on terms acceptable to us or at all. If instead of paying a dividend we elect to pay the tax, this could significantly increase our consolidated tax expense. We expect we would pay any such tax out of our available working capital, which could also significantly decrease our cash, unless we sought additional financing. For an explanation of personal holding company tax, refer to our “Critical Accounting Policies – Accounting for Income Taxes” for further explanation of matters related to personal holding tax.

ITEM 3 – QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Interest Rate Sensitivity

Cash, Cash Equivalents and Investments. As of June 29, 2007, we had cash and cash equivalents of $325.9 million, which consisted of cash, highly liquid money market funds and United States government agency securities with original maturities of 90 days or less. In addition, we had short-term and long-term investments of $290.6 million, which consisted primarily of United States government agency securities, variable rate discount notes and municipal debt with original maturities greater than 90 days. Many of these investments are subject to fluctuations in interest rates, which could impact our results. At June 29, 2007 the average investment maturity of our investment portfolio was less than 6 months. Based on our investment portfolio balance as of June 29, 2007, a hypothetical change in interest rates of 1% would have approximately a $1.8 million impact, and a change of 0.5% would have approximately a $0.9 million impact on the carrying value of our portfolio. Furthermore, a hypothetical change in interest rates of 1% would have approximately a $4.1 million impact, and a change of 0.5% would have approximately a $2.1 million impact on interest income over a one-year period.

Interest Rate Swap Agreements. We have entered into interest rate swap agreements to manage our exposure to interest rate changes on our facility debt obligations. The swap agreements involve the exchange of fixed and variable interest rate payments without exchanging the notional principal amount. Gains and losses associated with the swap agreements are included in other income, net, in our condensed consolidated statements of operations.

We do not utilize financial instruments for trading or other speculative purposes, nor do we utilize leveraged financial instruments.

Foreign Currency Exchange Risk

We maintain sales, marketing and business operations in foreign countries, most significantly in the United Kingdom. Consequently, we have exposure to adverse changes in exchange rates associated with our foreign business operations. While most of our revenue is derived from transactions denominated in United States dollars, nearly all of our costs from our foreign operations are derived from transactions denominated in the functional currency of that foreign location. As a result, our operating income is subject to exposure from changes in exchange rates. For example, the average exchange rate for fiscal 2006 of the British pound sterling to the United States dollar was approximately 1.8 United States dollars for one British pound sterling. We estimate that if the average exchange rate for the British pound sterling had been 10% higher or lower, it would have had an impact of approximately $2.8 million on our operating income during fiscal 2006. In addition, we are in the process of expanding our foreign operations, specifically in Asia, which will increase our exposure to changes in foreign currency exchange rates.

In fiscal 2005, we began selling more products in United States dollars from our United Kingdom branch and maintained the receipts in a United States dollar account in the United Kingdom. The functional currency of our United Kingdom branch is the British pound sterling. Therefore, we were required to remeasure balances that were in currencies other than the functional currency and recognize the impact of these foreign exchange rate fluctuations in our results of operations. As the United States dollar cash balances grew throughout fiscal 2005, our results of operations became exposed to foreign exchange gains and losses. In the first quarter of fiscal 2006, we converted much of the balance into British pound sterling, thereby significantly mitigating the exposure from fluctuations in foreign exchange rates on our statement of operations. We periodically convert cash balances denominated in United States dollars at our United Kingdom branch into British pound sterling to mitigate this exposure.

ITEM 4 – CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

We maintain “disclosure controls and procedures,” as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934 (the “Exchange Act”), that are designed to ensure that information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in Securities and Exchange Commission rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. In designing and evaluating our disclosure controls and procedures, management recognized that disclosure controls and procedures, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the disclosure controls and procedures are met. Additionally, in designing disclosure controls and procedures, our management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible disclosure controls and procedures. The design of any disclosure controls and procedures also is based in part upon 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.

Subject to the limitations noted above, our management, with the participation of our Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the design and operation of our disclosure controls and procedures as of the end of the fiscal period covered by this Quarterly Report on Form 10-Q. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that, as of such date, our disclosure controls and procedures were effective to meet the objective for which they were designed and operate at the reasonable assurance level.

Changes in Internal Control Over Financial Reporting

There were no changes in our internal control over financial reporting during the fiscal quarter ended June 29, 2007, that have materially affected or are reasonably likely to affect, our internal control over financial reporting.

PART II – OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

We are involved in various legal proceedings from time to time arising from the normal course of business activities, including claims of alleged infringement of intellectual property rights, commercial, employment and other matters. In our opinion, resolution of these proceedings is not expected to have a material adverse effect on our operating results or financial condition. However, it is possible that an unfavorable resolution of one or more such proceedings could materially affect our future operating results or financial condition in a particular period.

ITEM 1A. RISK FACTORS

A restated description of the risk factors associated with our business is set forth below. This description includes any material changes to and supersedes the description of the risk factors associated with our business previously disclosed in Part I, Item 1A of our Annual Report on Form 10-K for our fiscal year ended September 29, 2006. The following risk factors and other information included in this Quarterly Report on Form 10-Q should be carefully considered. The risks and uncertainties described below are not the only ones we face. Additional risks and uncertainties not presently known to us or that we presently deem less significant may also impair our business operations. If any of the following risks actually occur, our business operating results and financial condition could be materially adversely affected.

Our business and prospects depend on the strength of our brand, and if we do not maintain and strengthen our brand, our business will be materially harmed.

Maintaining and strengthening the "Dolby" brand is critical to maintaining and expanding both our products and services business and our technology licensing business, as well as to our ability to enter new markets for our sound and other technologies. Our continued success depends, in part, on our reputation for providing high quality products, services and technologies across a wide range of entertainment industries, including the consumer electronics products industry. If we fail to promote and maintain the Dolby brand successfully on either the products and services or the licensing sides of our business, our business and prospects will suffer. Moreover, we believe that the likelihood that our technologies will be adopted as industry standards in various markets and for various applications depends, in part, upon the strength of our brand, because professional organizations and industry participants are more likely to accept, as an industry standard, technologies developed by a well-respected and well-known brand. Maintaining and strengthening our brand will depend heavily on our ability to continue to develop innovative technologies for the entertainment industry and to continue to provide high quality products and services, which we may not do successfully.

We do not expect sales of traditional consumer DVD players to sustain their past growth rates. To the extent that sales of DVD players and home theatre systems level off or decline, or alternative technologies in which we do not participate replace DVDs as a dominant medium for consumer video entertainment, our licensing revenue will be adversely affected.

Growth in our revenue over the past several years has been the result, in large part, of the rapid growth in sales of DVD players and home theatre systems incorporating our technologies. However, as the markets for DVD players mature, we do not expect sales of traditional consumer DVD players to sustain their past growth rates. To the extent that sales of DVD players and home theatre systems level off or decline, our licensing revenue will be adversely affected. Additionally, the release and consumer adoption of next-generation DVD players has been delayed. There are currently two potential, incompatible formats for next-generation high-definition disc format proposed, and consumers may not react favorably to having to make a choice between formats. The delay in the release and consumer adoption of the next-generation disc format, as well as the inability of traditional DVD players to sustain their past growth rates, could adversely affect our licensing revenue. Even assuming resolution of the competing disc format conflict, the rate of consumer adoption of next-generation DVD players is uncertain and may be slower than past growth rates of traditional DVD players. In addition, if new technologies are developed for use with DVDs or new technologies are developed that substantially compete with or replace DVDs as a dominant medium for consumer video entertainment, and if we are unable to develop and successfully market technologies that are incorporated into or compatible with those new technologies, our business, operating results and prospects will be adversely affected.

We depend on the sale by our licensees of products that incorporate our technologies, and a reduction in those sales would adversely affect our licensing revenue.

We derive most of our revenue from the licensing of our technologies to consumer electronics product manufacturers. We derived 73%, 75% and 79% of our total revenue from our technology licensing business in fiscal 2004, 2005 and 2006, respectively. We do not manufacture consumer electronics products ourselves and our licensing revenue is dependent on sales by our licensees of products that incorporate our technologies. We cannot control these manufacturers' product development or commercialization efforts or predict their success. In addition, our license agreements, which typically require manufacturers of consumer electronics products and software developers to pay us a specified royalty for every electronics product shipped that incorporates our technologies, do not require these manufacturers to include our technologies in any specific number or percentage of units, and only a few of these agreements guarantee us a minimum aggregate licensing fee. Accordingly, if our licensees sell fewer products incorporating our technologies, or otherwise face significant economic difficulties, our revenue will decline. Moreover, we have a widespread presence in markets for electronics products, such as the consumer electronics product market, which includes DVD players, audio/video receivers and other home theatre consumer electronics products, and, as a result, there is little room for us to further penetrate such markets. Lower sales of products incorporating our technologies could occur for a number of reasons. Changes in consumer tastes or trends, or changes in industry standards, may adversely affect our licensing revenue. Increasing market saturation, durability of products in the marketplace, competing products and alternate consumer entertainment options could adversely affect demand for new products incorporating our technologies. In addition, our licensees, for whatever reason, may not choose to or may not be able to incorporate our technologies into their products in the future.

We face risks in conducting business in emerging economies, such as China, particularly due to the limited recognition and enforcement of intellectual property and contractual rights in these countries.

We believe that various trends will continue to increase our exposure to the risks of conducting business in emerging economies. For example, we expect consumer electronics product manufacturing in emerging economies, such as China, to continue to increase due to the availability of lower manufacturing costs as compared to in other industrial countries and an industry shift by discount retailers towards lower-end DVD player offerings. We also believe that our sales of professional products and production services in emerging economies will expand in the future to the extent that the use of digital surround sound technologies increases in these countries, including in movies and broadcast television. We further expect that the sale of products incorporating our technologies will increase in emerging economies to the extent that consumers there become more affluent. We face many risks associated with operating in these emerging economies, in large part, due to limited recognition and enforcement of contractual and intellectual property rights. As a result, we may experience difficulties in enforcing our intellectual property rights in these emerging economies, where intellectual property rights are not as respected as they are in the United States, Japan and Europe. We believe that it is critical that we strengthen existing relationships and develop new relationships with entertainment industry participants world-wide to increase our ability to enforce our intellectual property and contractual rights without relying solely on the legal systems in the countries in which we operate. If we are unable to develop, maintain and strengthen these relationships, our revenue from these countries could be adversely affected.

Our future success depends, in part, upon the growth of new and existing markets for our technologies and our ability to develop and adapt our technologies for those markets. If those markets do not grow or we are not able to develop successful products for them, our business prospects could be limited.

We expect that the future growth of our licensing revenue will depend, in part, upon the growth of, and our successful participation in, new opportunities for our technologies, including:

- Next-generation DVD;
- Digital television and radio broadcasting;
- HDTV;

- Personal computer technology;
- Video game consoles and video games;
- Home DVD recording;
- In-car entertainment systems;
- Personal audio and video players, including internet music applications;
- Broadband internet;
- Imaging; and
- Mobile devices.

Our ability to penetrate these markets depends on increased consumer demand for products that contain our technologies, which may not occur. Any failure of such markets to develop or consumer demand to grow would have a material adverse effect on our business and prospects. For example, in the PC market, equipment manufacturers are experiencing pricing pressure and, as a result, may elect to exclude DVD playback functionality from their products, thereby, requiring an additional cost to add this capability, which may affect demand for our technology. Whether our revenue from digital broadcast networks and broadband internet services increases depends upon the expansion of digital broadcast technologies and broadband internet as a medium of entertainment, which may not occur. In addition, even when our technologies are adopted as industry standards for a particular market, such market may not fully develop. In such case, our success depends not only on whether our technologies are adopted as industry standards for such market, but also on the development of that market, which may not occur. Demand for our technologies in any of these developing markets may not continue to grow, and a sufficiently broad base of consumers and professionals may not adopt or continue to use these technologies. In addition, our ability to generate revenue from these markets may be limited to the extent that service providers in these markets choose to provide select technologies and entertainment for little or no cost, such as many of the services provided in connection with broadband internet services. Moreover, some of these markets are ones in which we have not previously participated and, because of our limited experience, we may not be able to adequately adapt our business and our technologies to the needs of customers in these fields.

If we fail to deliver innovative technologies in response to changes in the entertainment industry, our business could decline.

The markets for our professional products and the markets for consumer electronics products using our licensed technologies are characterized by rapid change and technological evolution. We will need to expend considerable resources on research and development, or acquisitions, in the future in order to continue to design and deliver enduring, innovative entertainment products and technologies. Despite our efforts, we may not be able to develop, or acquire, and effectively market new products, technologies and services that adequately or competitively address the needs of the changing marketplace. For example, we cannot assure that Dolby Volume, Dolby's new volume leveling solution designed to address the annoyances of inconsistent loudness, or Dolby 3D Digital Cinema, Dolby's new 3D digital cinema solution, will address the needs of the marketplace, be effectively marketed or be successful technologies. In addition, we may not correctly identify new or changing market trends at an early enough stage to capitalize on market opportunities. At times such changes can be dramatic, such as the shift from VHS tapes to DVDs for consumer playback of movies in homes and elsewhere. Our future success depends to a great extent on our ability to develop, or acquire, and deliver innovative technologies that are widely adopted in response to changes in the entertainment industry and that are compatible with the technologies or products introduced by other entertainment industry participants.

Our operating results may fluctuate depending upon the timing of when we receive royalty reports from our licensees and of the satisfaction of our revenue recognition criteria.

Our quarterly operating results may fluctuate depending upon the timing of when we receive royalty reports from our licensees and of the satisfaction of our revenue recognition criteria. We recognize license revenue only after we receive royalty reports from our licensees regarding the shipment of their products that incorporate our technologies.

As a result, the timing of our revenue depends upon the timing of our receipt of those reports. In addition, it is not uncommon for royalty reports to include positive or negative corrective or retroactive royalties that cover extended periods of time. Furthermore, there have been times in the past when we have recognized an unusually large amount of licensing revenue from a licensee in a given quarter because not all of our revenue recognition criteria were met in prior periods. This can result in a large amount of licensing revenue from a licensee being recorded in a given quarter that is not necessarily indicative of the amounts of licensing revenue to be received from that licensee in future quarters, thus causing fluctuations in our operating results. For example, in the fourth quarter of fiscal 2006 and second quarter of fiscal 2007 we recognized approximately $6.7 million and $7.7 million, respectively, in licensing revenue from two separate licensees related to royalties on shipments in prior periods.

If our products and technologies fail to be adopted as industry standards, our business prospects could be limited and our operating results could be adversely affected.

The entertainment industry depends upon industry standards to ensure the compatibility of its content across a wide variety of entertainment systems and products. Accordingly, we make significant efforts to design our products and technologies to address capabilities, quality and cost considerations so that they either meet, or, more importantly, are adopted as, industry standards across the broad range of entertainment industry markets in which we participate, as well as the markets in which we hope to compete in the future, including digital cinema. To have our products and technologies adopted as industry standards, we must convince a broad spectrum of professional organizations throughout the world, as well as our major customers and licensees who are members of such organizations, to adopt them as such and to ensure that other industry standards are consistent with our products and technologies. If our technologies are not adopted or do not remain as industry standards, our business, operating results and prospects could be materially and adversely affected. We expect that meeting, maintaining and establishing industry standard technologies will continue to be critical to our business in the future. In addition, the market for broadcast technologies has traditionally been heavily based upon industry standards, often set by governments or other regulatory bodies, and we expect this to continue to be the case in the future. If our technologies are not chosen as industry standards for broadcasting in particular geographic areas, this could adversely affect our ability to compete in these markets.

It may be more difficult for us, in the future, to have our technologies adopted as individual industry standards to the extent that entertainment industry participants collaborate on the development of industry standard technologies.

Increasingly, standards-setting organizations are adopting or establishing technology standards for use in a wide range of consumer electronics products. As a result, it is more difficult for individual companies to have their technologies adopted wholesale as an informal industry standard. We call this type of standard a "de facto" industry standard, meaning that the standard is not explicitly mandated by any industry standards-setting body but is nonetheless widely adopted. In addition, increasingly there are a large number of companies, including ones that typically compete against one another, involved in the development of new technologies for use in consumer entertainment products. As a result, these companies often license their collective intellectual property rights as a group, making it more difficult for any single company to have its technologies adopted widely as a de facto industry standard or to have its technologies adopted as an exclusive, explicit industry standard for consumer electronics products.

Even if our technologies are adopted as an industry standard for a particular market, market participants may not widely adopt our technologies.

Even when a standards-setting body mandates our technologies for a particular market, which we call an "explicit" industry standard, our technologies may not be the sole technologies adopted for that market as an industry standard. Accordingly, our operating results depend upon participants in that market choosing to adopt our technologies instead of competitive technologies that also may be acceptable under such standard. For example, the continued growth of our revenue from the broadcast market will depend upon both the continued adoption of digital television generally and the choice to use our technologies where it is an optional industry standard.

Our licensing of industry standard technologies can be subject to limitations that could adversely affect our business and prospects.

When a standards-setting body mandates our technologies as explicit industry standards, we generally must agree to license such technologies on a fair, reasonable and non-discriminatory basis, which could limit our control over the use of these technologies. In these situations, we must often limit the royalty rates we charge for these technologies, which could adversely affect our gross margins. Furthermore, we may be unable to limit to whom we license such technologies, and may be unable to restrict many terms of the license. From time to time we may be subject to claims that our licenses of our industry standard technologies may not conform to the requirements of the standards-setting body. Private parties have raised this type of issue with us in the past. Allegations such as these could be asserted in private actions seeking monetary damages and injunctive relief, or in regulatory actions. Claimants in such cases could seek to restrict or change our licensing practices or our ability to license our technologies in ways that could injure our reputation and otherwise materially and adversely affect our business, operating results and prospects.

Third parties from whom we license technologies may challenge our calculation of the royalties we owe them for inclusion of their technologies in our products and licensed technologies, which could adversely affect our operating results, business and prospects.

In some cases, primarily in connection with the licensing of our Dolby Digital technologies, the products we sell and the technologies we license to our customers include intellectual property that we have licensed from third parties. Our agreements with these third parties generally require us to pay them royalties for that use, and give the third parties the right to audit our calculation of those royalties. A third party may disagree with our interpretation of the terms of a license agreement or, as a result of an audit, a third party could challenge the accuracy of our calculation. We are currently involved in a license agreement dispute with a third party patent licensor.

A successful challenge by a third party could increase the amount of royalties we have to pay to the third party, decrease our gross margin and adversely affect our operating results. Such a challenge could result in the termination of the license agreement which would impair our ability to continue to use and re-license intellectual property from that third party which, in turn, could adversely affect our business and prospects.

Inaccurate licensee royalty reporting and unauthorized use of our intellectual property could materially adversely affect our operating results.

Our licensing revenue is generated primarily from consumer electronics product manufacturers and software developers who license our technologies and incorporate them in their products. Under our existing arrangements, these licensees typically pay us a specified royalty for every product they ship that incorporates our technologies. We rely on our licensees to accurately report the number of units shipped that incorporate our technologies. We calculate our license fees, prepare our financial reports, projections and budgets, and direct our sales and product development efforts based on these reports we receive from our licensees. However, it is often difficult for us to independently determine whether or not our licensees are reporting shipments accurately. This is especially true with respect to software incorporating our technologies because software can be copied relatively easily and we oftentimes do not have easy ways to determine how many copies have been made. Most of our license agreements permit us to audit our licensees' records, but audits are generally expensive and time consuming and initiating audits could harm our customer relationships. In the past, licensees, particularly in emerging economies, such as China, have understated or failed to report the number of products incorporating our technologies that they shipped, and we have not been able to collect and recognize revenue to which we were entitled. We expect that we will continue to experience understated and non-reporting by licensees, which could adversely affect our operating results. Conversely, to the extent that our licensees overstate the number of products incorporating our technologies, or report the products under the wrong categories, negative corrections could result in reductions of royalty revenue in subsequent periods. In addition, some of our licensees may begin to more closely scrutinize their past or future licensing statements which may result in an increased receipt of negative corrective statements.

We also have often experienced, and expect to continue to experience, problems with non-licensee consumer electronics product manufacturers and software developers, particularly in emerging economies, such as China, incorporating our technologies or incorporating our technologies and trademarks into their products without our authorization and without paying us any licensing fees. This unauthorized use of our intellectual property could adversely affect our operating results.

Our licensing revenue depends in large part upon semiconductor manufacturers incorporating our technologies into integrated circuits, or ICs, for sale to our electronics product licensees and if, for any reason, our technologies are not incorporated in these ICs or fewer ICs are sold that incorporate our technologies, our operating results would be adversely affected.

Our licensing revenue from consumer electronics product manufacturers depends in large part upon the availability of integrated circuits, or ICs, that implement our technologies. IC manufacturers incorporate our technologies into these ICs, which are then incorporated in consumer electronics products. We do not manufacture these ICs, but rather depend on IC manufacturers to develop, produce and then sell them to licensed consumer electronics product manufacturers. We do not control the IC manufacturers' decisions whether or not to incorporate our technologies into their ICs, and we do not control their product development or commercialization efforts nor predict their success. As a result, if these IC manufacturers are unable or unwilling, for any reason, to implement our technologies into their ICs, or if, for any reason, they sell fewer ICs incorporating our technologies, our operating results will be adversely affected.

Our inability to deploy our digital cinema products in significant numbers in the early stages of the transition to digital cinema, coupled with the price of our products, could limit our future prospects in the digital cinema market and could materially and adversely affect our business.

The cinema industry is still in the early stages of the adoption of digital cinema for the distribution and exhibition of movies. A number of competitors offer competing products for digital cinema, some of which are priced lower than our products. At least one competitor has a significantly greater installed base of its competing digital cinema products than we do, which could limit our eventual share of the digital cinema product market and materially and adversely affect our operating results. We expect that as the market for digital cinema grows we will face more competitive pricing pressures than we have traditionally experienced for cinema products. As a result, we may have to implement pricing strategies which could have an adverse impact on our product sales gross margins in the future.

If the market for digital cinema develops more slowly than expected, our future prospects could be limited and our business could be materially and adversely affected.

If the industry cannot agree on one or more business models for digital cinema, the broad adoption of digital cinema will be delayed. The conversion of movie theatres from film to digital cinema will require significant expenditures, and we cannot predict how quickly digital cinema will become widely adopted. At present only a limited number of movie theatres have been converted to digital cinema, and we expect the conversion of theatres to digital cinema technologies, if it occurs, to be a long-term process due to both technological and financial obstacles. If the market for digital cinema develops more slowly than expected, or if there is significant and sustained resistance by the motion picture industry or cinema operators to this technology or the cost of implementation, we may not realize significant returns on our investments in digital cinema technology, which could materially and adversely affect our operating results.

If we do not identify opportunities and successfully execute our initiatives to participate in the emerging digital cinema market, our future prospects could be limited and our business could be adversely affected.

The cinema industry is in the early stages of the adoption of digital cinema for the distribution and exhibition of movies. Industry participants continue to discuss business models to facilitate adoption of digital cinema by allocating the costs among industry participants, and the business models that ultimately emerge may vary from country to country. Participating in some of the models under discussion may require us to depart from our traditional model of selling our professional products pursuant to one-time contracts, and could expose us to various risks we have not faced in the past. For example, we have participated in one model by deploying, at our expense, fully integrated digital cinema systems and seeking payment from motion picture distributors for films presented on the systems. If we do not identify, and successfully execute on, the business models that provide an opportunity to generate revenues from our digital cinema products and services, our future prospects in this market will be limited and our business could be materially and adversely affected.

If our digital cinema initiatives do not perform to expectations, our reputation may suffer and demand for our digital cinema products and services may not develop.

As we participate in digital cinema initiatives, if we or our equipment do not perform to expectations, our relationships with cinema industry participants may be adversely affected and our reputation may suffer, affecting the demand for our digital cinema products and services. Any negative publicity or significant problems with our digital cinema initiatives could materially and adversely affect our relationships in the cinema industry or the perception of our brand.

If we are unable to expand our business into non-sound technologies, our future growth could be limited.

Our future growth will depend, in part, upon our expansion into areas beyond sound technologies. For example, in addition to our digital cinema initiative, we are exploring other areas that facilitate delivery of digital entertainment, such as technologies for processing digital moving images and content protection. We will need to spend considerable resources on research and development or acquisitions in the future in order to deliver innovative non-sound technologies. Our April 2007 acquisition of Brightside Technologies Inc. (Brightside), a development-stage technology company focused on enabling the capture, distribution, and display of more vibrant video on LCD TV sets, as well as front-projection and rear-projection TVs, is an example of our efforts to expand into areas beyond sound technologies. However, we have limited experience in non-sound technology markets and, despite our efforts, we cannot predict whether we will be successful in developing, or acquiring and marketing non-sound products, technologies and services. We will face significant risks in successfully integrating businesses that we acquire, such as Brightside, into our business.

In addition, many of the non-sound technology markets are relatively new and may not develop as we currently anticipate. Moreover, although we believe that many of the technological advances we may develop or acquire for digital cinema may have applicability in other areas, such as broadcasting or consumer electronics products, we may not ever be able to achieve these anticipated benefits in these other markets. A number of competitors and potential competitors may develop non-sound technologies similar to those that we develop, or acquire, some of which may provide advantages over our products, technologies and services. Some of these competitors have much greater experience and expertise in the non-sound fields we may enter. The non-sound products, technologies and services we expect to market may not achieve or sustain market acceptance, may not meet industry needs, and may not be accepted as industry standards. If we are unsuccessful in selling non-sound products, technologies and services, the future growth of our business may be limited. In addition, our efforts to enter or strengthen our positions in non-sound markets may be tied to the success of specific programs.

Acquisition activities could result in operating difficulties, dilution to our stockholders and other harmful consequences.

We have evaluated, and expect to continue to evaluate, a wide array of possible strategic transactions, including acquisitions. For example, in April 2007 we acquired Brightside, a development-stage technology company focused on enabling the capture, distribution, and display of more vibrant video on LCD TV sets, as well as front-projection and rear-projection TVs. We consider these types of transactions in connection with our efforts to expand our business beyond sound technologies to other technologies related to the delivery of digital entertainment. Although we cannot predict whether or not we will complete any such acquisition or other transactions in the future, any of these transactions could be material in relation to our market capitalization, financial condition or results of operations. The process of integrating an acquired company, business or technology may create unforeseen difficulties and expenditures. The areas where we may face risks in integrating acquired businesses, including in connection with our acquisition of Brightside, include:

- Diversion of management time and focus from operating our business to acquisition integration challenges;
- Cultural challenges associated with integrating employees from acquired businesses into our organization, including cultural and logistical challenges;
- Retaining employees from businesses we acquire;
- The need to implement or improve internal controls, procedures and policies appropriate for a public company at businesses that prior to the acquisition lacked effective controls, procedures and policies;
- Possible write-offs or impairment charges resulting from acquisitions;
- Unanticipated or unknown liabilities relating to acquired businesses; and
- The need to integrate acquired businesses' accounting, management information, manufacturing, human resources and other administrative systems to permit effective management.

Foreign acquisitions involve unique risks in addition to those mentioned above, including those related to integration of operations across different geographies, cultures and languages, currency risks and risks associated with the particular economic, political and regulatory environment in specific countries. Also, the anticipated benefit of our acquisitions may not materialize. Future acquisitions could result in potentially dilutive issuances of our equity securities, the incurrence of debt, contingent liabilities or amortization expenses, or write-offs of goodwill, any of which could harm our operating results or financial condition. Future acquisitions may also require us to obtain additional equity or debt financing, which may not be available on favorable terms or at all. Moreover, acquisitions may have an adverse impact on our financial condition and results of operations, including a potential adverse impact on our gross margins.

Pricing pressures on the electronics product manufacturers who incorporate our technologies into their products could limit the licensing fees we charge for our technologies, which could adversely affect our revenues.

The markets for the consumer electronics products in which our technologies are incorporated are intensely competitive and price sensitive. Retail prices for consumer electronics products that include our sound technology, such as DVD players and home theatre systems, have decreased significantly, and we expect prices to continue to decrease for the foreseeable future. In response, manufacturers have sought to reduce their product costs, which can result in downward pressure on the licensing fees we charge our customers who incorporate our technologies into the consumer electronics products that they sell. A decline in the licensing fees we charge could materially and adversely affect our operating results.

If the sale of consumer electronics products incorporating our technologies does not grow in emerging markets, our ability to increase our licensing revenue may be limited.

We also expect that growth in our licensing revenue will depend, in part, upon the growth of sales of consumer electronics products incorporating our technologies in emerging economies, as consumers in these markets have more disposable income and are increasingly purchasing entertainment products with surround sound capabilities. However, if our licensing revenue from the use of our technologies in these new markets or geographic areas does not expand, our prospects could be adversely affected.

We face significant competition in various markets, and if we are unable to compete successfully, our business will suffer.

The markets for entertainment industry technologies are highly competitive, and we face competitive threats and pricing pressure in our markets. Competitors on the professional side of our business include Avica, DTS, Doremi, EVS, GDC, Kodak, Microsoft, NEC, Panastereo, Qube, QuVis, Sony and UltraStereo. Competitors on the consumer side of our business include Coding Technologies, DTS, Fraunhofer Institute for Integrated Circuits, Philips, Microsoft, RealNetworks, Sony, SRS Labs, DivX, Inc., and Thomson. In addition, other companies may become competitors in the future. Some people may perceive the quality of sound produced by some of our competitors' technologies to be equivalent or superior to that produced by ours. In addition, some of our current and/or future competitors may have significantly greater financial, technical, marketing and other resources than we do, or may have more experience or advantages in the markets in which they compete. For example, Microsoft and RealNetworks may have an advantage over us in the market for internet technologies because of their greater experience and presence in that market. In addition, some of our current or potential competitors, such as Microsoft and RealNetworks, may be able to offer integrated system solutions in markets for sound or non-sound entertainment technologies, including audio, video and rights management technologies related to personal computers or the internet, which could make competing technologies that we develop unnecessary. By offering an integrated system solution, these potential competitors also may be able to offer competing technologies at lower prices than our technologies, which could adversely affect our operating results. Further, many of the consumer electronics products that include our sound technologies also include sound technologies developed by our competitors. As a result, we must continue to invest significant resources in research and development in order to enhance our technologies and our existing products and services and introduce new high-quality products and services to meet the wide variety of such competitive pressures. Our business will suffer if we fail to do so successfully.

Our relationships with entertainment industry participants are particularly important to our products and services and our technology licensing businesses, and if we fail to maintain such relationships our business could be materially harmed.

If we fail to maintain and expand our relationships with a broad range of participants throughout the entertainment chain, including motion picture studios, broadcasters, video game designers, music producers and manufacturers of consumer electronics products, our business and prospects could be materially harmed. Relationships have historically played an important role in the entertainment industries that we serve, both on the professional and consumer sides of our business. For example, our products and services business is particularly dependent upon our relationships with the major motion picture studios and broadcasters, and our technology licensing business is particularly dependent upon our relationships with consumer electronics product manufacturers, software developers and integrated circuit, or IC, manufacturers. If we fail to maintain and strengthen these relationships, these entertainment industry participants may be more likely not to purchase and use our products, services and technologies, or create content incorporating our technologies, which could materially harm our business and prospects. In addition to directly providing substantially all of our revenue, these relationships are also critical to our ability to have our technologies adopted as industry standards. In addition, if major industry participants form strategic relationships that exclude us, whether on the products and services side or the licensing side of our business, our business and prospects could be materially adversely affected.

We have limited or no patent protection for our technologies in particular countries, including China and India, which could limit our ability to grow our business in these markets.

We have a relatively limited number of issued patents in particular countries, including China and India. For example, in China we have only limited patent protection, especially with respect to our Dolby Digital technologies. In India, we have no issued patents. Consequently, growing our licensing revenue in these emerging countries will depend on our ability to obtain patent rights in these counties for existing and new technologies, which is uncertain. Moreover, because of the limitations of the legal systems in many of these countries, the effectiveness of patents obtained or that may in the future be obtained, if any, is likewise uncertain.

We face diverse risks in our international business, which could adversely affect our operating results.

We are dependent on international sales for a substantial amount of our total revenue. For fiscal 2004, 2005 and 2006, royalties from licensees outside the United States were 80%, 76% and 77% of our licensing revenue, respectively, and our sales outside the United States were 59%, 61% and 64% of our professional products and service revenue, respectively. We expect that international and export sales will continue to represent a substantial portion of our revenue for the foreseeable future. This future revenue will depend to a large extent on the continued use and expansion of our technologies in entertainment industries worldwide. Increased worldwide use of our technologies is also an important factor in our future growth.

Due to our reliance on sales to customers outside the United States, we are subject to the risks of conducting business internationally, including:

- Our ability to enforce our contractual and intellectual property rights, especially in those foreign countries that do not respect and protect intellectual property rights to the same extent as do the United States, Japan and European countries, which increases the risk of unauthorized, and uncompensated, use of our technology;
- United States and foreign government trade restrictions, including those which may impose restrictions on importation of programming, technology or components to or from the United States;
- Foreign government taxes, regulations and permit requirements, including foreign taxes that we may not be able to offset against taxes imposed upon us in the United States, and foreign tax and other laws limiting our ability to repatriate funds to the United States;
- Foreign labor laws, regulations and restrictions;
- Changes in diplomatic and trade relationships;

- Difficulty in staffing and managing foreign operations;
- Fluctuations in foreign currency exchange rates and interest rates, including risks related to any interest rate swap or other hedging activities we undertake;
- Political instability, natural disasters, war or events of terrorism; and
- The strength of international economies.

The licensing of patents constitutes a significant source of our revenue. If we are unable to replace expiring patents with new patents or proprietary technologies, our revenue could decline.

We hold patents covering much of the technology that we license to consumer electronics product manufacturers, and our licensing revenue is tied in large part to the life of those patents. Our right to receive royalties related to our patents terminates with the expiration of the last patent covering the relevant technologies. However, many of our licensees choose to continue to pay royalties for continued use of our trademarks and know-how even after the licensed patents have expired, although at a reduced royalty rate. Accordingly, to the extent that we do not continue to replace licensing revenue from technologies covered by expiring patents with licensing revenue based on new patents and proprietary technologies, our revenue could decline.

As of June 29, 2007, we had 1,012 individual issued patents and 1,501 pending patent applications in nearly 35 jurisdictions throughout the world. Our issued patents are scheduled to expire at various times through July 2027. Of these, 8 patents are scheduled to expire in the remainder of calendar year 2007, 19 patents are scheduled to expire in calendar year 2008 and 5 patents are scheduled to expire in calendar year 2009. We derive our licensing revenue principally from our Dolby Digital technologies. Patents relating to our Dolby Digital technologies generally expire between 2009 and 2017, and patents relating to our Dolby Digital Plus technologies, an extension of Dolby Digital, expire between 2019 and 2022. In addition, the remaining patents relating to Dolby Digital Live technologies, an extension of Dolby Digital, are scheduled to expire in 2021.

We are, and may in the future be, subject to intellectual property rights claims, which are costly to defend, could require us to pay damages and could limit our ability to use particular technologies in the future.

Companies in the technology and entertainment industries own large numbers of patents, copyrights, trademarks and trade secrets and frequently enter into litigation based on allegations of infringement or other violations of intellectual property rights. We have faced such claims in the past and we expect to face similar claims in the future.

Any intellectual property claims, with or without merit, could be time-consuming, expensive to litigate or settle and could divert management resources and attention. In the past we have settled claims relating to infringement allegations and agreed to make payments in connection with such settlements. We expect that similar claims will be asserted against us in the future in the ordinary course of our business. An adverse determination in any intellectual property claim could require that we pay damages or stop using technologies found to be in violation of a third party's rights and could prevent us from offering our products and services to others. In order to avoid these restrictions, we may have to seek a license for the technology. This license may not be available on reasonable terms, could require us to pay significant royalties and may significantly increase our operating expenses. The technologies also may not be available for license to us at all. As a result, we may be required to develop alternative non-infringing technologies, which could require significant effort and expense. If we cannot license or develop technologies for any infringing aspects of our business, we may be forced to limit our product and service offerings and may be unable to compete effectively. In addition, at times in the past, we have chosen to defend our licensees from third-party intellectual property infringement claims even where such defense was not contractually required, and we may choose to take on such defense in the future. Any of these results could harm our brand, our operating results and our financial condition. In addition, from time to time we are engaged in disputes regarding the licensing of our intellectual property rights, including matters related to our royalty rates and other terms of our licensing arrangements. These types of disputes can be asserted by our customers or prospective customers or by other third parties as part of negotiations with us or in private actions seeking monetary damages or injunctive relief, or in regulatory actions. In the past, licensees have threatened to initiate litigation against us regarding our licensing royalty rate practices, including potential antitrust claims. Damages and requests for injunctive relief asserted in claims like these could be material, and could have a significant impact on our business. Any disputes with our customers or potential customers or other third parties could adversely affect our business, results of operations and prospects.

Our ability to develop proprietary technology in markets in which "open standards" are adopted may be limited, which could adversely affect our ability to generate revenue.

Standards-setting bodies, such as those for digital cinema technologies, may require the use of so-called "open standards," meaning that the technologies necessary to meet those standards are publicly available. The use of open standards may reduce our opportunity to generate revenue, as open standards technologies are based upon non-proprietary technology platforms in which no one company maintains ownership over the dominant technologies.

Events and conditions in the motion picture and broadcast industries may affect sales of our professional products and production services.

Sales of our professional products and production services tend to fluctuate based on the underlying trends in the motion picture industry. For example, when box office receipts for the motion picture industry increase, we have typically seen sales of our professional products increase as well, as cinema owners are more likely to build new theatres and upgrade existing theatres with our more advanced cinema products when they are doing well financially. Conversely, when box office receipts are down cinema owners tend to scale back on plans to upgrade their systems or build new theatres. Our professional product sales are also subject to fluctuations based on events and conditions in the theatre industry generally that may or may not be tied to box office receipts in particular periods. For example, the growth in piracy of motion pictures adversely affects the construction of new screens, the renovation of existing theatres and the continued production of new motion pictures. Technological advances and the conversion of motion pictures into digital formats have made it easier to create, transmit and "share" high-quality unauthorized copies of motion pictures, including on pirated DVDs and on the internet. In 2005, events within the U.S. cinema industry, including recent restructuring and consolidations, and a decline in box office sales appear to have delayed purchasing decisions by exhibitors. The launch of new digital services by broadcasters also influences the sale of our professional products. On the other hand, our production services revenue, both in the United States and internationally, is tied to the number of films being made by studios and independent filmmakers. A number of factors can affect the number of films that are produced, including strikes and work stoppages within the motion picture industry, as well as by the tax incentive arrangements that many foreign governments provide filmmakers to promote local filmmaking.

We may be unable to significantly expand our current professional product sales in the cinema industry because our professional products are already used by the vast majority of major cinema operators and major motion picture studios in the United States and much of the rest of the world. If the cinema industry does not expand, or if it contracts, the demand for our professional products will be adversely affected.

Our ability to further penetrate the market for motion picture sound technologies is limited because of the widespread use of our current professional products by major motion picture content creators, distributors and cinema operators. As a result, our future revenue from our professional products for the cinema industry will depend, in part, upon events and conditions in that industry—specifically, the continued production and distribution of motion pictures, and the construction of new theatres and the renovation of existing theatres, using our products and services. For example, in the late 1990s cinema operators in the United States built a large number of new cinema megaplexes. This initially resulted in increased sales of our cinema processors, but also resulted in an oversupply of screens in some markets. This oversupply led to significant declines in new theatre construction in the United States in the early 2000s, resulting in a corresponding decline in sales of our cinema processors. As a result, future growth in sales of our existing cinema products may be limited, and may decrease in the future, as the number of new cinemas being built and the number of existing cinemas without our products continues to decline.

The demand for our current professional products and production services could decline if the film industry broadly adopts digital cinema.

If the film industry broadly adopts digital cinema, the demand for our current professional products and production services could decline. Such a decline in our products and services business could also adversely affect our technology licensing business, because the strength of our brand and our ability to use professional developments to advance our consumer licensing technologies would be impaired. If, in such circumstances, we are unable to adapt our professional products and production services or introduce new products for the market for digital cinema successfully, our business could be materially adversely affected.

Fluctuations in our quarterly and annual operating results may significantly affect the value of our stock.

A number of factors, many of which are outside our control, may cause or contribute to significant fluctuations in our quarterly and annual revenue and operating results. These fluctuations may make financial planning and forecasting more difficult. In addition, these fluctuations may result in unanticipated decreases in our available cash, which could negatively impact our business and prospects. As discussed more fully below, these fluctuations also could increase the volatility of our stock price. Factors that may cause or contribute to fluctuations in our operating results and revenue include:

- Fluctuations in demand for our products and for the consumer electronics products of our licensees;
- Fluctuations in the timing of royalty reports we receive from our licensees, including late, sporadic or inaccurate reports;
- Sporadic payments we may be able to recover from companies utilizing our technologies without licenses;
- Corrections to licensees' reports received in periods subsequent to those in which the original revenue was reported;
- Introduction or enhancement of products, services and technologies by us, our licensees and our competitors, and market acceptance of these new or enhanced products, services and technologies;
- Rapid, wholesale changes in technology in the entertainment industries in which we compete;
- Events and conditions in the motion picture industry, including box office receipts that affect the number of theatres constructed, the number of movies produced and exhibited, the general popularity of motion pictures and strikes by motion picture industry participants;
- The financial resources of cinema operators available to buy our products or to equip their theatres to accommodate upgraded or new technologies;
- Consolidation by participants in the markets in which we compete, which could result among other things in pricing pressure;
- The amount and timing of our operating costs and capital expenditures, including those related to the expansion of our business, operations and infrastructure;
- Variations in the time-to-market of our technologies in the entertainment industries in which we operate;
- Seasonal electronics product shipment patterns by our consumer electronics product licensees and seasonal product purchasing patterns by customers of our professional products;
- The impact of, and our ability to react to, interruptions in the entertainment distribution chain, including as a result of work stoppages at our facilities, our customers' facilities and other points throughout the entertainment distribution chain;
- Changes in business cycles that affect the markets in which we sell our products and services or the markets for consumer electronics products incorporating our technologies;
- Adverse outcomes of litigation or governmental proceedings, including any foreign, federal, state or local tax assessments or audits;
- Costs of litigation and intellectual property protection; and

- Seasonal demand for production services in the motion picture industry, which could result in reduced revenue.

One or more of the foregoing or other factors may cause our operating expenses to be disproportionately higher or lower or may cause our revenue and operating results to fluctuate significantly in any particular quarterly or annual period. Results from prior periods are thus not necessarily indicative of the results of future periods.

Some of our customers are also our current or potential competitors, and if those customers were to choose to use their competing technologies rather than ours, our business and operating results would be adversely affected.

We face competitive risks in situations where our customers are also current or potential competitors. For example, Sony is a significant licensee customer and is a significant purchaser of our professional products and production services, but Sony is also a competitor with respect to some of our professional and consumer technologies. To the extent that our customers choose to utilize competing technologies they have developed or in which they have an interest, rather than use our technologies, our business and operating results could be adversely affected.

Surround sound technologies could be treated as a commodity in the future, which could adversely affect our business, operating results and prospects.

We believe that the success we have had licensing our surround sound technologies to consumer electronics product manufacturers is due, in part, to the strength of our brand and the perception that our technologies provide a high-quality solution for surround sound. However, as applications that incorporate surround sound technologies become increasingly prevalent, we expect more competitors to enter this field with other solutions. Furthermore, to the extent that competitors' solutions are perceived, accurately or not, to provide the same advantages as our technologies, at a lower or comparable price, there is a risk that sound encoding technologies such as ours will be treated as commodities, resulting in loss of status of our technologies, decline in their use, and significant pricing pressure. To the extent that our audio technologies become a commodity, rather than a premium solution, our business, operating results and prospects could be adversely affected.

Licensing some of our technologies in joint licensing programs, or "patent pools," is a different business model for us, and we may face many challenges in conducting this business.

In fiscal 2002, we began licensing some of our patents through our wholly-owned subsidiary Via Licensing Corporation in joint licensing programs, or "patent pools," with other companies in an effort to ensure that our technologies are compatible with other technologies in the entertainment industry and to promote our technologies as industry standards. These patent pools allow product manufacturers streamlined access to selected foundational technologies and are comprised of a group of patents held by a number of companies, including us in some cases, and administered by Via Licensing. If we do not identify new or changing market trends and technologies at an early enough stage to capitalize on market opportunities for joint licensing programs, we may not continue to be successful with this business model. Also, to the extent that Dolby technologies are included in patent pools, we have less control over the licensing of those technologies through the patent pools compared to licensing through our traditional business model in which we license our patents as bundles of technologies and interact directly with our customers. In addition, we may have less control over the application and quality control of our technologies included in these pools.

The loss of or interruption in operations of one or more of our key suppliers could materially delay or stop the production of our professional products and impair our ability to generate revenue.

Our reliance on outside suppliers for some of the key materials and components we use in manufacturing our professional products involves risks, including limited control over the price, timely delivery and quality of such components. We have no agreements with our suppliers to ensure continued supply of materials and components. Although we have identified alternate suppliers for most of our key materials and components, any required changes in our suppliers could cause material delays in our production operations and increase our production costs. In addition, our suppliers may not be able to meet our future production demands as to volume, quality or timeliness. Moreover, we rely on sole source suppliers for some of the components that we use to manufacture our professional products, including specific charged coupled devices, light emitting diodes and digital signal processors. These sole source suppliers may become unable or unwilling to deliver these components to us at an acceptable cost or at all, which could force us to redesign those specific products. Our inability to obtain timely delivery of key components of acceptable quality, any significant increases in the prices of components, or the redesign of our professional products could result in material production delays, increased costs and reductions in shipments of our products, any of which could increase our operating costs, harm our customer relationships or materially and adversely affect our business and operating results.

Revenue from our professional products may suffer if our production processes encounter problems or if we are not able to match our production capacity to fluctuating levels of demand.

Our professional products are highly complex, and production difficulties or inefficiencies can interrupt production, resulting in our inability to deliver products on time in a cost effective manner, which could harm our competitive position. If production is interrupted at one of our two manufacturing facilities, we may not be able to shift production to the other facility on a timely basis, and customers may purchase products from our competitors. A shortage of manufacturing capacity for our professional products could adversely affect our operating results and damage our customer relationships. We generally cannot quickly adapt our manufacturing capacity to rapidly changing market conditions. Likewise, we may be unable to respond to fluctuations in customer demand. At times we underutilize our manufacturing facilities as a result of reduced demand for some of our professional products. Any inability to respond to fluctuations in customer demand for our professional products may adversely affect our gross margins.

Our professional products, from time to time, experience quality problems that can result in decreased sales and higher operating expenses.

Our professional products are complex and sometimes contain undetected software or hardware errors, particularly when first introduced or when new versions are released. In addition, our professional products are sometimes combined with or incorporated into products from other vendors, sometimes making it difficult to identify the source of a problem. These errors could result in a loss of or delay in market acceptance of our professional products or cause delays in delivering them and meeting customer demands, any of which could reduce our revenue and raise significant customer relations issues. In addition, if our professional products contain errors we could be required to replace or reengineer them, which would increase our costs. Moreover, if any such errors cause unintended consequences, we could face claims for product liability. Although we generally attempt to contractually limit liability for defective products to the cost of repairing or replacing these products, if these contract provisions are not enforced, or are unenforceable for any reason, or if liabilities arise that are not effectively limited, we could incur substantial costs in defending and settling product liability claims.

Awareness of our brand depends to a significant extent upon decisions by our customers to display our trademarks on their products, and if our customers do not display our trademarks on their products, our ability to increase our brand awareness may be harmed.

Because we engage in relatively little direct brand advertising, the promotion of our brand depends upon entertainment industry participants displaying our trademarks on their products that incorporate our technologies, such as film prints and consumer electronics products. Although we do not require our customers to place our brand on their products, we actively encourage them to do so. For example, we rely on consumer electronics product manufacturers that license our technologies to display our trademarks on their products in order to promote our brand. If our customers choose for any reason not to display our trademarks on their products, our ability to maintain or increase our brand awareness may be harmed, which would have an adverse effect on our business and prospects. In addition, if we fail to maintain high quality standards for our professional products, or if we fail to maintain high quality standards for the products that incorporate our technologies through the quality-control certification process that we require of our licensees, the strength of our brand could be adversely affected.

Licensee products that incorporate our technologies, from time to time, experience quality problems that could damage our brand, decrease revenues and increase operating expenses.

Licensee products that incorporate our technologies often are complex and sometimes contain undetected software or hardware errors, particularly when first introduced or when new versions are released. In addition, those products are often combined with, or incorporated into, products from other companies, sometimes making it difficult to identify the source of a problem. Any negative publicity or negative impact relating to these product problems could adversely affect the perception of our brand. In addition, these errors could result in loss of, or delay in, market acceptance of those products or Dolby technologies, or cause delays in delivering them and meeting customer demands, any of which could reduce our revenue and raise significant customer relations issues. Although we generally attempt to contractually limit our liability for our licensees' defective products, we may elect to help reengineer those products, which could adversely affect our operating results.

A loss of one or more of our key customers or licensees in any of our markets could adversely affect our operating results.

From time to time, one or a small number of our customers or licensees may represent a significant percentage of our professional products and services or licensing revenue. Although we have agreements with many of these customers, these agreements typically do not require any minimum purchases or minimum royalty fees and do not prohibit customers from purchasing products and services from competitors. A decision by any of our major customers or licensees not to use our technologies, or their failure or inability to pay amounts owed to us in a timely manner, or at all, whether due to strategic redirections or adverse changes in their businesses or for other reasons, could have a significant effect on our operating results.

We are subject to various environmental laws and regulations that could impose substantial costs upon us and may adversely affect our business, operating results and financial condition.

Some of our operations use substances regulated under various federal, state, local and international laws governing the environment, including those governing the discharge of pollutants into the air and water, the management, disposal and labeling of hazardous substances and wastes and the cleanup of contaminated sites. We could incur costs, fines and civil or criminal sanctions, third-party property damage or personal injury claims, or could be required to incur substantial investigation or remediation costs, if we were to violate or become liable under environmental laws. Liability under environmental laws can be joint and several and without regard to comparative fault. The ultimate costs under environmental laws and the timing of these costs are difficult to predict.

We also face increasing complexity in our product design as we adjust to new and future requirements relating to the materials composition of our products. For example, restrictions on lead and other hazardous substances that apply to specified electronic products put on the market in the European Union became effective as of July 1, 2006 and similar requirements related to marking of electronic products became effective in China as of March 1, 2007. We have redesigned our products in order to be able to continue to offer them for sale within the European Union. For some products, substituting particular components containing regulated hazardous substances is more difficult or costly, and additional redesign efforts could result in production delays. Selected electronic products that we maintain in inventory may be rendered obsolete if not in compliance with the new environmental laws, which could negatively impact our ability to generate revenue from those products.

We also expect that our operations, whether manufacturing or licensing, will be affected by other new environmental laws and regulations on an ongoing basis. Although we cannot predict the ultimate impact of any such new laws and regulations, they will likely result in additional costs or decreased revenue, and could require that we redesign or change how we manufacture our products, any of which could have a material adverse effect on our business.

Any inability to protect our intellectual property rights could reduce the value of our products, services and brand.

Our business is dependent upon our patents, trademarks, trade secrets, copyrights and other intellectual property rights. We derived 73%, 75% and 77% of our total revenue from licensing revenue in the fiscal years 2004, 2005 and 2006, respectively. Effective intellectual property rights protection, however, may not be available under the laws of every country in which our products and services and those of our licensees are distributed. Also, the efforts we have taken to protect our proprietary rights may not be sufficient or effective. Any significant impairment of our intellectual property rights could harm our business or our ability to compete. In addition, protecting our intellectual property rights is costly and time consuming. We have taken steps in the past to enforce our intellectual property rights and expect to continue to do so in the future. However, it may not be practicable or cost effective for us to enforce our intellectual property rights fully, particularly in particular countries or where the initiation of a claim might harm our business relationships. For example, we have many times experienced, and expect to continue to experience, problems with consumer electronics product manufacturers incorporating our technologies into their products without our authorization. If we are unable to successfully identify and stop unauthorized use of our intellectual property, we could experience increased operational and enforcement costs, which could adversely affect our financial condition and results of operations. We generally seek patent protection for our innovations. It is possible, however, that some of these innovations may not be protectable. In addition, given the costs of obtaining patent protection, we may choose not to protect particular innovations that later turn out to be important. Moreover, we have limited or no patent protection in particular foreign jurisdictions. For example, in China we have only limited patent protection, especially with respect to our Dolby Digital technologies, and in India we have no issued patents. Furthermore, there is always the possibility, despite our efforts, that the scope of the protection gained will be insufficient or that an issued patent may later be found to be invalid or unenforceable. Moreover, we seek to maintain select intellectual property as trade secrets. These trade secrets could be compromised by third parties, or intentionally or accidentally by our employees, which would cause us to lose the competitive advantage resulting from them.

It is possible that we may be treated as a personal holding company, which could adversely affect our operating results and financial condition.

The Internal Revenue Service may assert that we or any of our subsidiaries are currently, or previously have been, liable for personal holding company tax, plus interest and penalties, if applicable. In addition, we and our subsidiaries may be liable for personal holding company tax in the future. For United States federal income tax purposes, a corporation is generally considered to be a "personal holding company" under the United States Internal Revenue Code if (i) at any time during the last half of its taxable year more than 50% of its stock by value is owned, directly or indirectly, by virtue of the application of certain stock ownership attribution rules set forth in the Internal Revenue Code for purposes of applying the personal holding company rules, by five or fewer individuals and (ii) at least 60% of its adjusted ordinary gross income, as defined for United States federal income tax purposes, is "personal holding company income." Personal holding company income is generally passive income, including royalty income, subject to particular exceptions such as qualifying software royalties. A personal holding company is subject to an additional tax on its undistributed after-tax income, calculated at the statutory tax rate, which is currently 15%. Since the personal holding company tax is imposed only on undistributed income, a personal holding company can avoid or mitigate liability for the tax, but not interest or penalties, by paying a dividend to its stockholders.

More than 50% of the value of our stock is held by Ray Dolby and stockholders considered affiliated with him pursuant to the stock ownership attribution rules applicable to personal holding companies. We expect this will continue to be the case in the foreseeable future. In addition, a significant portion of our income is from licensing fees, which may constitute personal holding company income. Currently, however, less than 60% of Dolby Laboratories' adjusted ordinary gross income is personal holding company income.

However, the Internal Revenue Service may assert that we or one of our subsidiaries are currently, or previously have been, liable for personal holding company tax, plus interest and penalties, if applicable. In addition, we or our subsidiaries may be liable for personal holding company tax in the future. The treatment of select items of our income and the income of our subsidiaries, for purposes of the personal holding company tax, may be subject to challenge. In the event that we or any of our subsidiaries is determined to be a personal holding company, or for prior taxable years, to have been a personal holding company, we or our subsidiary could be liable for additional taxes, and possibly interest and penalties, based on the undistributed income and the tax rate in effect at that time, but only if we or our subsidiary, as the case may be, decides not to fully abate the tax by the payment of a dividend, although such a dividend will not eliminate interest and penalties. In addition, we believe that there exists a meaningful risk that in the relatively near future the mix of our revenue will change so that more of our adjusted ordinary gross income may be classified as personal holding company income. In such event, it is possible that we or one of our subsidiaries could become liable for the personal holding company tax, assuming the ownership test continues to be met. In that case, we or our subsidiary, as the case may be, may be required to pay additional tax in the event we or the subsidiary decides not to fully abate the tax by the payment of a dividend. Because no claim or assessment has been made against us with respect to personal holding company taxes, we are unable to quantify the amount of any additional taxes, and possibly interest and penalties, for which we may be liable in the future for past periods or the amount of the dividend that we may pay to abate the tax. Furthermore, we are unable to quantify the amount of personal holding company tax that we may be liable for or the dividend that we may elect to pay for future periods as such amounts, if any, would be based upon the application of the rules discussed above to the results of our future operations. We have explored options to reduce our exposure and the exposure of our subsidiaries to the personal holding company tax in the future, as well as continue to actively monitor our current exposure.

If we or any of our subsidiaries were to pay personal holding company tax (and possibly interest and penalties), this could significantly increase our consolidated tax expense and adversely affect our operating results. In addition, if the statutory tax rate increases in the future, the amount of any personal holding company tax we or any of our subsidiaries may have to pay could increase significantly, further impairing our operating results. In that regard, the statutory tax rate, which is currently 15%, is scheduled to return to ordinary income tax rate levels for tax years beginning on or after January 1, 2011. If we are deemed to be a personal holding company and, instead of paying the personal holding company tax, we elect to pay a dividend to our stockholders in an amount equal to all or a significant part of our undistributed personal holding company income, we may consume a significant amount of cash resources and be unable to retain or generate working capital. This would adversely affect our financial condition. As a result, if we pay such a dividend, we may decide to seek additional financing, although that financing may not be available to us when and as required on commercially reasonable terms, if at all.

Failure to comply with applicable current and future government regulations could have a negative effect on our business.

Our operations and business practices are subject to federal, state and local government laws and regulations, as well as international laws and regulations, including those relating to consumer and other safety-related compliance for electronic equipment, as well as compulsory license requirements as a prerequisite to being included as part of the industry standards, such as the United States HDTV standard. Any failure by us to comply with the laws and regulations applicable to us or our products could result in our inability to sell those products, additional costs to redesign products to meet such laws and regulations, fines or other administrative actions by the agencies charged with enforcing compliance and, possibly, damages awarded to persons claiming injury as the result of our non-compliance. Changes in or enactment of new statutes, rules or regulations applicable to us could have a material adverse effect on our business.

The loss of members of our management team could substantially disrupt our business operations.

Our success depends to a significant degree upon the continued individual and collective contributions of our management team. A limited number of individuals have primary responsibility for managing our business, including our relationships with key customers and licensees. We have key executives and senior technical people who have been with us for a number of years, including over 150 employees who have been with us for over 10 years. These individuals, as well as the rest of our management team and key employees, are at-will employees, and we do not maintain any key-person life insurance policies. Losing the services of any key member of our team, whether from retirement, competing offers or other causes, could prevent us from executing our business strategy, cause us to lose key customer or licensee relationships, or otherwise materially affect our operations.

We rely on highly skilled personnel, and if we are unable to retain or motivate key personnel or hire qualified personnel, we may not be able to maintain our operations or grow effectively.

Our performance is largely dependent on the talents and efforts of highly skilled individuals. Our future success depends on our continuing ability to identify, hire, develop, motivate and retain highly skilled personnel for all areas of our organization. In this regard, we currently plan to hire a number of employees throughout fiscal 2007 in response to our growth and our current initiatives. We have maintained a rigorous, highly selective and time-consuming hiring process, which we believe has significantly contributed to our success to date, but has made it more difficult for us to hire a sufficient number of qualified employees. As we grow, our hiring process may prevent us from hiring the personnel we need in a timely manner. In addition, we are aware that some of our competitors have directly targeted our employees. If we are unable to hire and train a sufficient number of qualified employees or retain and motivate existing employees, our existing operations may suffer and we may be unable to grow effectively.

If we fail to maintain proper and effective internal controls, our ability to produce accurate financial statements could be impaired, which could adversely affect our operating results, our ability to operate our business and our investors' views of us.

We have a complex business organization that is international in scope. Ensuring that we have adequate internal financial and accounting controls and procedures in place to help ensure that we can produce accurate financial statements on a timely basis is a costly and time-consuming effort that needs to be re-evaluated frequently. On an ongoing basis, we document, review and, if appropriate, improve our internal controls and procedures in connection with Section 404 of the Sarbanes-Oxley Act, which requires annual management assessments of the effectiveness of our internal controls over financial reporting and a report by our independent auditors addressing these assessments. Both we and our independent auditors periodically test our internal controls in connection with the Section 404 requirements and could, as part of that documentation and testing, identify areas for further attention or improvement. Implementing any appropriate changes to our internal controls may require specific compliance training of our directors, officers and employees, entail substantial costs in order to modify our existing accounting systems, and take a significant period of time to complete. Such changes may not, however, be effective in maintaining the adequacy of our internal controls, and any failure to maintain that adequacy, or consequent inability to produce accurate financial statements on a timely basis, could increase our operating costs and could materially impair our ability to operate our business. In addition, investors' perceptions that our internal controls are inadequate or that we are unable to produce accurate financial statements may seriously affect our stock price.

For the foreseeable future, Ray Dolby or his affiliates will be able to control the selection of all members of our board of directors, as well as virtually every other matter that requires stockholder approval, which will severely limit the ability of other stockholders to influence corporate matters.

At June 29, 2007, Ray Dolby and his affiliates owned 100 shares of our Class A common stock and 60,000,000 shares of our Class B common stock. As of June 29, 2007, Ray Dolby and his affiliates, including his family members, had voting power over approximately 98% of our outstanding Class B common stock, which in the aggregate represented approximately 91% of the combined voting power of our outstanding Class A and Class B common stock. Under our certificate of incorporation, holders of Class B common stock are entitled to ten votes per share while holders of Class A common stock are entitled to one vote per share. Generally, shares of Class B common stock automatically convert into shares of Class A common stock upon transfer of such Class B common stock, other than transfers to certain specified persons and entities, including the spouse and descendents of Ray Dolby and the spouses and domestic partners of such descendents. Because of this dual class structure, Ray Dolby, his affiliates, and his family members and descendents will, for the foreseeable future, have significant influence over our management and affairs, and will be able to control virtually all matters requiring stockholder approval, including the election of directors and significant corporate transactions such as mergers or other sales of our company or assets, even if they come to own considerably less than 50% of the total number of outstanding shares of our Class A and Class B common stock. Ray Dolby, his affiliates, his family members and descendents will maintain this control even if in the future they come to own considerably less than 50% of the total number of outstanding shares of our Class A and Class B common stock. Moreover, these persons may take actions in their own interests that you or our other stockholders do not view as beneficial. Absent a transfer of Class B common stock that would trigger an automatic conversion as described above, there is no threshold or time deadline at which the shares of Class B common stock will automatically convert into shares of Class A common stock. Assuming conversion of all shares of Class B common stock held by persons not affiliated with Ray Dolby into shares of Class A common stock, so long as Ray Dolby and his affiliates, his family members and descendents continue to hold shares of Class B common stock representing approximately 10% or more of the total number of outstanding shares of our Class A and Class B common stock, they will hold a majority of the combined voting power of the Class A and Class B common stock.

Future sales of shares by insiders could cause our stock price to decline.

If our founder, officers, directors or employees sell, or indicate an intention to sell, substantial amounts of our Class A common stock in the public market, including shares of Class A common stock issuable upon conversion of shares of Class B common stock, the trading price of our Class A common stock could decline. As of June 29, 2007, we had a total of 109,891,394 shares of Class A and Class B common stock outstanding. Of these shares, 31,625,000 shares of Class A common stock were sold in our initial public offering by us and the selling stockholders, and an additional 8,000,000 shares of Class A common stock were sold in a secondary offering in May 2007 by our principal stockholder.

As of June 29, 2007, our directors and executive officers beneficially held 60,580,797 shares of Class B common stock, 6,299 shares of Class A common stock, vested options to purchase 843,122 shares of Class B common stock and vested options to purchase 116,748 shares of Class A common stock. We expect that any sale of our Class A common stock by our directors and executive officers would be subject to compliance with Rule 144 under the Securities Act.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

Sales of Unregistered Securities

In the fiscal quarter ended June 29, 2007, we issued an aggregate of 546,670 shares of our Class B common stock to certain employees, officers and directors upon the exercise of options awarded under our 2000 Stock Incentive Plan and since June 30, 2007 through July 18, 2007, we issued an aggregate of 81,540 shares of our Class B common stock to certain employees and officers upon the exercise of options awarded under our 2000 Stock Incentive Plan. We received aggregate proceeds of $1.1 million in the fiscal quarter ended June 29, 2007, and $0.2 million in the period since June 30, 2007 through, July 18, 2007 as a result of the exercise of these options. We believe these transactions were exempt from the registration requirements of the Securities Act in reliance on Rule 701 thereunder as transactions pursuant to compensatory benefit plans and contracts relating to compensation as provided under Rule 701. As of July 18, 2007 options to purchase an aggregate of 4,429,880 shares of our Class B common stock remain outstanding. All issuances of shares of our Class B common stock pursuant to the exercise of these options will be made in reliance on Rule 701. All option grants made under the 2000 Stock Incentive Plan were made prior to the effectiveness of our initial public offering. No further option grants will be made under our 2000 Stock Incentive Plan.

None of the foregoing transactions involved any underwriters, underwriting discounts or commissions, or any public offering.

Each share of our Class B common stock is convertible into one share of our Class A common stock at any time at the option of the holder or upon the affirmative vote of the holders of a majority of the shares of Class B common stock. In addition, each share of Class B common stock shall convert automatically into one share of Class A common stock upon any transfer, except for certain transfers described in our amended and restated certificate of incorporation.

ITEM 6. EXHIBITS

Exhibit Number	Description
31.1	Certification by the Chief Executive Officer Pursuant to Rule 13a-14(a) or 15d-14(a) under the Securities Exchange Act of 1934 as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification by the Chief Financial Officer Pursuant to Rule 13a-14(a) or 15d-14(a) under the Securities Exchange Act of 1934 as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1 ‡	Certification by the Chief Executive Officer and the Chief Financial Officer Pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

‡ Furnished herewith

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SIGNATURES

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

Date: August 1, 2007

DOLBY LABORATORIES, INC.

By: /s/ Kevin J. Yeaman

Kevin J. Yeaman
Chief Financial Officer
(Principal Financial and Accounting Officer and Duly Authorized Officer)

INDEX TO EXHIBITS

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32.1 ‡	Certification by the Chief Executive Officer and the Chief Financial Officer Pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

‡ Furnished herewith

Exhibit 31.1

CERTIFICATION

I, N. W. Jasper, Jr., certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Dolby Laboratories, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15(d)-15(f)) for the registrant and have:

   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurances regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 1, 2007

/s/ N.W. Jasper, Jr.

N. W. Jasper, Jr.
Principal Executive Officer

Exhibit 31.2

CERTIFICATION

I, Kevin J. Yeaman, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Dolby Laboratories, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15(d)-15(f)) for the registrant and have:
   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
   (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurances regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
   (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
   (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 1, 2007

/s/ Kevin J. Yeaman
Kevin J. Yeaman
Principal Financial Officer

Exhibit 32.1

**CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of Dolby Laboratories, Inc. (the “Company”) on Form 10-Q for the fiscal quarter ended June 29, 2007, as filed with the Securities and Exchange Commission (the “Report”), N.W. Jasper, Jr., President and Chief Executive Officer of the Company, and Kevin J. Yeaman, Chief Financial Officer of the Company, respectively, do each hereby certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

- The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- The information in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: August 1, 2007

/s/ N.W. Jasper, Jr.
N.W. Jasper, Jr.
President and Chief Executive Officer

/s/ Kevin J. Yeaman
Kevin J. Yeaman
Chief Financial Officer