

Dolby Laboratories, Inc.  
Form DEF 14A  
January 17, 2006

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

**SCHEDULE 14A INFORMATION**

**Proxy Statement Pursuant to Section 14(a) of the**  
**Securities Exchange Act of 1934**

Filed by the Registrant

Filed by a party other than the Registrant

Check the appropriate box:

Preliminary Proxy Statement

**Confidential, For Use of the Commission Only (as permitted by Rule 14a-6(e)(2))**

Definitive Proxy Statement

Definitive Additional Materials

Soliciting Material Pursuant to § 240.14a-12

**DOLBY LABORATORIES, INC.**

(Name of Registrant as Specified in Its Charter)

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(Name of Person(s) Filing Proxy Statement, if Other than the Registrant)

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- No fee required.
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**Dolby Laboratories, Inc.**  
**100 Potrero Avenue**  
**San Francisco, CA 94103-4813**  
**(415) 558-0200**

January 17, 2006

Dear Stockholder:

You are cordially invited to attend the Annual Meeting of Stockholders of Dolby Laboratories, Inc. that will be held on February 14, 2006, at 10:30 a.m., Pacific Standard Time, at the executive offices of Dolby Laboratories, Inc. located at 100 Potrero Avenue, San Francisco, CA 94103-4813.

Details regarding admission to the Annual Meeting of Stockholders and the business to be conducted are described in the accompanying Notice of Annual Meeting and Proxy Statement. Included with the Proxy Statement is a copy of our 2005 Annual Report to Stockholders.

Your vote is important. Whether or not you plan to attend the Annual Meeting of Stockholders, we hope you will vote as soon as possible. You may vote over the internet, as well as by telephone or by mailing a proxy or voting instruction form. Voting over the internet, by telephone or by written proxy will ensure your representation at the Annual Meeting of Stockholders regardless of whether or not you attend in person. Please review the instructions on the proxy or voting instruction form regarding each of these voting options.

Thank you for your ongoing support of Dolby Laboratories, Inc.

Sincerely yours,

/s/ Bill Jasper

Bill Jasper

*President and Chief Executive Officer*

**DOLBY LABORATORIES, INC.**

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**Notice of Annual Meeting of Stockholders**

**to be held on February 14, 2006**

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To the Stockholders of Dolby Laboratories, Inc.:

The Annual Meeting of Stockholders (the "Annual Meeting") of Dolby Laboratories, Inc., a Delaware corporation (the "Company"), will be held at the Company's executive offices located at 100 Potrero Avenue, San Francisco, CA 94103-4813, on Tuesday, February 14, 2006, at 10:30 a.m., Pacific Standard Time, for the following purposes:

1. To elect five directors to serve until the 2007 Annual Meeting of Stockholders or until their successors are duly elected and qualified;
2. To consider and vote upon a proposal to amend and restate the Company's 2005 Stock Plan to permit certain future awards under the plan to qualify as performance-based compensation under Section 162(m) of the Internal Revenue Code and to permit the granting of performance cash bonus awards under the plan;
3. To ratify the appointment of KPMG LLP as the Company's independent registered public accounting firm for our fiscal year ending September 29, 2006; and
4. To transact such other business as may properly come before the Annual Meeting and any postponement or adjournment of the Annual Meeting.

The foregoing items of business are more fully described in the Proxy Statement accompanying this Notice. We are not aware of any other business to come before the Annual Meeting.

Only stockholders of record as of the close of business on January 9, 2006 and their proxies are entitled to notice of and to vote at the Annual Meeting and any postponements, adjournments or continuations thereof.

All stockholders are cordially invited to attend the Annual Meeting in person. Any stockholder attending the Annual Meeting may vote in person even if such stockholder returned a proxy. Please note, however, that if your shares are held of record by a broker, bank or other nominee and you wish to vote at the Annual Meeting, you must obtain a proxy issued in your name from the record holder. **You will need to bring proof of ownership of Company stock to enter the Annual Meeting.**

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By Order of the Board of Directors

/s/ Mark S. Anderson  
Mark S. Anderson  
*Secretary*

January 17, 2006

**WHETHER OR NOT YOU EXPECT TO ATTEND THE ANNUAL MEETING, WE ENCOURAGE YOU TO READ THIS PROXY STATEMENT AND SUBMIT YOUR PROXY OR VOTING INSTRUCTIONS AS PROMPTLY AS POSSIBLE IN ORDER TO ENSURE YOUR REPRESENTATION AT THE ANNUAL MEETING. YOU MAY SUBMIT YOUR PROXY OR VOTING INSTRUCTIONS FOR THE ANNUAL MEETING BY COMPLETING, SIGNING, DATING AND RETURNING YOUR PROXY OR VOTING INSTRUCTION FORM IN THE PRE-ADDRESSED ENVELOPE PROVIDED, OR, IN MOST CASES, BY USING THE TELEPHONE OR THE INTERNET. FOR SPECIFIC INSTRUCTIONS ON HOW TO VOTE YOUR SHARES, PLEASE REFER TO THE SECTION ENTITLED QUESTIONS AND ANSWERS ABOUT THE PROXY MATERIALS AND THE ANNUAL MEETING IN THIS PROXY STATEMENT AND THE INSTRUCTIONS ON THE PROXY OR VOTING INSTRUCTION FORM. EVEN IF YOU HAVE GIVEN YOUR PROXY, YOU MAY STILL VOTE IN PERSON IF YOU ATTEND THE ANNUAL MEETING. PLEASE NOTE, HOWEVER, THAT IF YOUR SHARES ARE HELD OF RECORD BY A BROKER, BANK OR OTHER NOMINEE AND YOU WISH TO VOTE AT THE ANNUAL MEETING, YOU MUST OBTAIN A PROXY ISSUED IN YOUR NAME FROM THE RECORD HOLDER.**

**Dolby Laboratories, Inc.**

**100 Potrero Avenue**

**San Francisco, CA 94103-4813**

**(415) 558-0200**

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**PROXY STATEMENT**

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The Board of Directors of Dolby Laboratories, Inc., a Delaware corporation ( we, us, Dolby or the Company ), is soliciting proxies in the accompanying form to be used at the Annual Meeting of Stockholders of the Company to be held at the Company s executive offices located at 100 Potrero Avenue, San Francisco, CA 94103-4813, on Tuesday, February 14, 2006, at 10:30 a.m., Pacific Standard Time, and any postponement, adjournment or continuation thereof (the Annual Meeting ).

This Proxy Statement and the accompanying notice and form of proxy are first being mailed to stockholders on or about January 17, 2006.

**QUESTIONS AND ANSWERS ABOUT  
THE PROXY MATERIALS AND THE ANNUAL MEETING**

**What proposals will be voted on at the Annual Meeting?**

Three proposals will be voted on at the Annual Meeting:

The election of directors;

The amendment and restatement of the Company s 2005 Stock Plan; and

The ratification of the appointment of KPMG LLP as the Company s independent registered public accounting firm for our fiscal year ending September 29, 2006.

**What are the Board s recommendations?**

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Our Board unanimously recommends that you vote:

FOR election of each of the nominated directors;

FOR amendment and restatement of the Company's 2005 Stock Plan; and

FOR ratification of the appointment of KPMG LLP as the Company's independent registered public accounting firm for our fiscal year ending September 29, 2006.

### **Will there be any other items of business on the agenda?**

We do not expect any other items of business because the deadline for stockholder proposals and nominations has already passed. Nonetheless, in case there is an unforeseen need, the accompanying proxy gives discretionary authority to the persons named on the proxy with respect to any other matters that might be brought before the Annual Meeting. Those persons intend to vote that proxy in accordance with their best judgment.

### **What constitutes a quorum?**

As of the close of business on January 9, 2006 (the Record Date), there were 34,510,769 shares of our Class A Common Stock outstanding and 70,323,492 shares of our Class B Common Stock outstanding. Each share of Class A Common Stock is entitled to one vote, and each share of Class B Common Stock is entitled to



ten votes, on all matters being considered at the Annual Meeting. We refer to our Class A Common Stock and Class B Common Stock collectively as our Common Stock. The presence at the Annual Meeting, in person or by proxy, of the holders of a majority of the voting power of the Common Stock outstanding on the Record Date will constitute a quorum. Both abstentions and broker non-votes are counted for the purpose of determining the presence of a quorum.

### **Who is entitled to vote?**

Stockholders of record at the close of business on the Record Date may vote at the Annual Meeting. Each holder of our Class A Common Stock is entitled to one vote for each share of Class A Common Stock held as of the Record Date, and each holder of our Class B Common Stock is entitled to ten votes for each share of Class B Common Stock held as of the Record Date. The Class A Common Stock and Class B Common Stock are voting as a single class on all matters described in these proxy materials for which your vote is being solicited.

### **What is the difference between holding shares as a stockholder of record and as a beneficial owner?**

*Stockholder of Record.* If your shares are registered directly in your name with Dolby's transfer agent, Computershare Trust Company, N.A., you are considered, with respect to those shares, the stockholder of record. Dolby sent directly to stockholders of record the Proxy Statement, Annual Report and proxy card.

*Beneficial Owner.* If your shares are held in a stock brokerage account or by a bank or other nominee, you are considered the beneficial owner of shares held in street name. Your broker, bank or nominee, who is considered with respect to those shares the stockholder of record, forwarded the Proxy Statement and Annual Report, together with a voting instruction form, to you. As the beneficial owner, you have the right to direct your broker, bank or nominee how to vote your shares by completing the voting instruction form. Under the rules of the New York Stock Exchange ( NYSE ), brokers are prohibited from giving proxies to vote on equity compensation plans unless the beneficial owner of such shares has given voting instructions on the matter. This means that if your broker is the record holder of your shares, you must give voting instructions to your broker with respect to Proposal 2 if you want your broker to vote your shares on the matter.

### **How do I vote?**

You may vote using any of the following methods:

**By Mail** Stockholders of record of Dolby Common Stock may submit proxies by completing, signing and dating their proxy cards and mailing them in the accompanying pre-addressed envelopes. If you return your signed proxy but do not indicate your voting preferences, your shares will be voted on your behalf FOR the election of the nominated directors, FOR the amendment and restatement of the Company's 2005 Stock Plan and FOR the ratification of KPMG LLP as the Company's independent registered public accounting firm for fiscal 2006. Dolby stockholders who hold shares beneficially in street name may provide voting instructions by mail by completing, signing and dating the voting instruction forms provided by their brokers, banks or nominees and mailing them in the accompanying pre-addressed envelopes.

**By Internet** Stockholders of record of Dolby Common Stock with internet access may submit proxies by following the Vote by Internet instructions on their proxy cards. Most Dolby stockholders who hold shares beneficially in street name may provide voting instructions by accessing the web site specified on the voting instruction forms provided by their brokers, banks or nominees. Please

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check the voting instruction form for internet voting availability. Please be aware that if you submit voting instructions over the internet, you may incur costs such as telephone and internet access charges for which you will be responsible.

By Telephone Stockholders of record of Dolby Common Stock who live in the United States or Canada may submit proxies by following the Vote by Phone instructions on their proxy cards. Most

Dolby stockholders who hold shares beneficially in street name and live in the United States or Canada may provide voting instructions by phone by calling the number specified on the voting instruction forms provided by their brokers, banks or nominees. Please check the voting instruction form for telephone voting availability.

In person at the Annual Meeting Shares held in your name as the stockholder of record may be voted in person at the Annual Meeting. Shares held beneficially in street name may be voted in person only if you obtain a legal proxy from the broker, bank or nominee that holds your shares giving you the right to vote the shares. *Even if you plan to attend the Annual Meeting, we recommend that you also submit your proxy or voting instructions by mail, or by telephone, or the internet so that your vote will be counted if you later decide not to attend the Annual Meeting.*

#### **Can I change my vote or revoke my proxy?**

If you are a stockholder of record, you may revoke your proxy at any time prior to the vote at the Annual Meeting. If you submitted your proxy by mail, you must file with the Secretary of the Company a written notice of revocation or deliver, prior to the vote at the Annual Meeting, a valid, later-dated proxy. If you submitted your proxy by telephone or the internet, you may revoke your proxy with a later telephone or internet proxy, as the case may be. Attendance at the Annual Meeting will not have the effect of revoking a proxy unless you give written notice of revocation to the Secretary before the proxy is exercised or you vote by written ballot at the Annual Meeting. If you are a beneficial owner, you may vote by submitting new voting instructions to your broker, bank or nominee, or, if you have obtained a legal proxy from your broker, bank or nominee giving you the right to vote your shares, by attending the meeting and voting in person.

#### **How are votes counted?**

In the election of directors, you may vote FOR all of the nominees or your vote may be WITHHELD with respect to one or more of the nominees. For the other items of business, you may vote FOR, vote AGAINST or ABSTAIN. If you ABSTAIN, the abstention has the same effect as a vote AGAINST. If you provide specific instructions, your shares will be voted as you instruct. If you sign your proxy card with no further instructions, your shares will be voted in accordance with the recommendations of the Board ( FOR all of the nominees to the Board, FOR the amendment of the Company's 2005 Stock Plan, FOR ratification of KPMG LLP as the Company's independent registered public accounting firm, and in the discretion of the proxy holders on any other matters that properly come before the Annual Meeting).

#### **What vote is required to approve each item?**

In the election of directors, the five persons receiving the highest number of FOR votes at the Annual Meeting will be elected. All other proposals require the affirmative FOR vote of a majority of the voting power of the shares present and voting at the Annual Meeting in person or by proxy. If you hold your shares beneficially in street name and do not provide your broker or nominee with voting instructions, your shares may constitute broker non-votes. Generally, broker non-votes occur on a matter when a broker is not permitted to vote on that matter without instructions from the beneficial owner and instructions are not given. In tabulating the voting result for any particular proposal, shares that constitute broker non-votes are not considered entitled to vote on that proposal. Thus, broker non-votes will not affect the outcome of any matter being voted on at the Annual Meeting, assuming that a quorum is obtained. Abstentions have the same effect as votes against the matter. Under the rules of the NYSE, brokers are prohibited from giving proxies to vote on equity compensation plans unless the beneficial owner of such shares has given voting instructions on the matter. This means that if your broker is the record holder of your shares, you must give voting instructions to your broker with respect to Proposal 2 if you want your broker to vote your shares on that matter.

#### **Is cumulative voting permitted for the election of directors?**

No. You may not cumulate your votes for the election of directors.

**How are proxies solicited?**

Employees, officers and directors of the Company may solicit proxies. We will reimburse brokerage houses and other custodians, nominees and fiduciaries for their reasonable out-of-pocket expenses for forwarding proxy and solicitation material to the beneficial owners of Common Stock.

**Date of Our Fiscal Year End.**

This Proxy Statement provides information about the matters to be voted on at the Annual Meeting and additional information about Dolby and its executive officers and directors. Some of the information is provided as of the end of fiscal 2005 and some information is provided as of a more current date. Each of our fiscal years ends on the last Friday of September. Our fiscal 2005 ended on September 30, 2005 and our fiscal 2004 ended on September 24, 2004.

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**PROPOSAL 1**
**ELECTION OF DIRECTORS****Nominees**

The Board of Directors proposes the election of five directors of the Company, each to serve until the next annual meeting of stockholders or until his successor is duly elected and qualified. All of the nominees have been recommended for nomination by the Nominating and Governance Committee of the Board of Directors and all of them are currently serving as directors of the Company. All nominees were elected by the stockholders at last year's annual meeting.

Each person nominated for election has agreed to serve if elected, and management has no reason to believe that any nominee will be unavailable to serve. If any nominee is unable or declines to serve as director at the time of the Annual Meeting, an event that the Company does not currently anticipate, proxies will be voted for any nominee designated by the Board of Directors to fill the vacancy. Unless otherwise instructed, the proxy holders will vote the proxies received by them FOR the nominees named below.

Names of the nominees and certain biographical information about them as of the Record Date are set forth below:

| <u>Name</u>                            | <u>Age</u> | <u>Position with the Company</u>                | <u>Director Since</u> |
|--|------------|---|-----------------------|
| Ray Dolby <sup>(1)</sup>               | 72         | Founder and Chairman of the Board               | 1967                  |
| Bill Jasper <sup>(1)(2)</sup>          | 58         | President, Chief Executive Officer and Director | 2003                  |
| Peter Gotcher <sup>(2)(3)(4)(5)</sup>  | 46         | Director  | 2003                  |
| Sanford Robertson <sup>(3)(4)(5)</sup> | 74         | Director  | 2003                  |
| Roger Siboni <sup>(3)(4)(5)</sup>      | 51         | Director  | 2004                  |

- (1) Member of the Outside Director Compensation Committee  
(2) Member of the Stock Plan Committee  
(3) Member of the Audit Committee  
(4) Member of the Compensation Committee  
(5) Member of the Nominating and Governance Committee

**Ray Dolby**, founder and chairman of Dolby Laboratories, was born in Portland, Oregon and grew up on the San Francisco peninsula. From 1949 through 1952 he worked on audio and instrumentation projects at Ampex Corporation, where from 1952 through 1957, as a student, he was mainly responsible for the development of the electronic aspects of the Ampex video tape recording system. He received his B.S. in electrical engineering from Stanford University in 1957 and, as a Marshall Scholar, left Ampex to pursue further studies at Cambridge University in England. He received a Ph.D. degree in physics from Cambridge in 1961.

In 1963, Dolby took up a two-year appointment as a United Nations technical advisor in India, then returned to England in 1965 to found Dolby Laboratories in London. In 1976 he established further offices, laboratories and manufacturing facilities in California. He holds more than 50

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United States patents and has written papers on video tape recording, long wavelength X-ray analysis and noise reduction.

Honors and Awards Audio Engineering Society: Fellow and Past President; Silver Medal; Gold Medal. British Kinematograph Sound and Television Society: Fellow; Science and Technology Award. Society of Motion Picture and Television Engineers: Fellow; Samuel L. Warner Memorial Award; Alexander M. Poniatoff Gold Medal; Progress Medal; Honorary Member. Academy of Motion Picture Arts and Sciences:

Science and Engineering Award; Oscar Award. National Academy of Television Arts and Sciences: Emmy Award. National Academy of Recording Arts and Sciences: Grammy Award. United States: National Medal of Technology. United Kingdom: Honorary O.B.E.

**Bill Jasper**, our President and Chief Executive Officer, joined Dolby Laboratories in February 1979 and has also served as a director since June 2003. Mr. Jasper served in a variety of positions prior to becoming President in May 1983, including as our Vice President, Finance and Administration and Executive Vice President. Mr. Jasper is a member of the Audio Engineering Society and the Society of Motion Picture and Television Engineers and an at-large member of the Academy of Motion Picture Arts and Sciences. He serves as chairman of the board of directors of FOCUS Enhancements and as a member of the board of trustees of Saint Mary's College of California. Mr. Jasper holds a B.S. degree in industrial engineering from Stanford University and a M.B.A. from the University of California at Berkeley.

**Peter Gotcher** has served as a director since June 2003. Mr. Gotcher is an independent investor. Mr. Gotcher was a venture partner with Redpoint Ventures, a private investment firm, from September 1999 to January 2003. Prior to joining Redpoint Ventures, Mr. Gotcher was a venture partner with Institutional Venture Partners, a private investment firm, from 1997 to September 1999. Prior to joining Institutional Venture Partners, Mr. Gotcher founded and served as the president, chief executive officer and chairman of the board of Digidesign from 1984 to 1995. Digidesign was acquired by Avid Technology, a media software company, in 1995 and Mr. Gotcher served as the general manager of Digidesign and executive vice president of Avid Technology from January 1995 to May 1996. Mr. Gotcher serves on the boards of directors of several private companies. Mr. Gotcher holds a B.A. degree in English literature from the University of California at Berkeley.

**Sanford Robertson** has served as a director since June 2003. Mr. Robertson has been a partner of Francisco Partners, a technology buyout fund, since 1999. Prior to founding Francisco Partners, Mr. Robertson was the founder and chairman of Robertson, Stephens & Co., a technology investment bank formed in 1978 and sold to BankBoston in 1998. Since the sale, Mr. Robertson has been a technology investor and advisor to several technology companies. Mr. Robertson was also the founder of Robertson, Colman, Siebel & Weisel, later renamed Montgomery Securities, another technology investment bank. Mr. Robertson also serves on the board of directors of Pain Therapeutics and salesforce.com. Mr. Robertson holds a B.B.A. and a M.B.A. from the University of Michigan.

**Roger Siboni** has served as a director since July 2004. Mr. Siboni served as the chairman of the board of directors of E.piphany, Inc., a provider of customer interaction software, from December 1999 until E.piphany, Inc. was acquired by SSA Global Technologies, Inc. in September 2005. Mr. Siboni also served as president and chief executive officer of E.piphany from August 1998 to July 2003. From July 1996 to August 1998, Mr. Siboni was deputy chairman and chief operating officer of KPMG Peat Marwick LLP, a member firm of KPMG International, an accounting and consulting firm. From July 1993 to June 1996, Mr. Siboni was managing partner of the KPMG Peat Marwick LLP's information, communication and entertainment practice. Mr. Siboni also serves on the boards of directors of Cadence Design Systems and FileNET. Mr. Siboni holds a B.S. degree in business administration from the University of California at Berkeley.

There are no family relationships among any of our directors or executive officers. Our Bylaws permit our Board of Directors to establish by resolution the authorized number of directors, and five directors are currently authorized. Our Board of Directors currently consists of five members.

*The Board of Directors recommends a vote **FOR** election as director of each of the nominees set forth above.*



## **Compensation of Directors**

We pay each of our non-employee directors \$30,000 per year for their services as members of our Board of Directors. In addition, Mr. Siboni receives \$20,000 for his services as chairman of our Audit Committee. We also reimburse our non-employee directors for reasonable travel expenses in connection with attendance at Board and committee meetings. Board members do not receive additional compensation for attending Board and committee meetings.

Under our 2005 Stock Plan, new non-employee directors appointed to the Board receive an initial option to purchase 20,000 shares of our Class A Common Stock, which vests over three years at a rate of one-third upon each anniversary of grant date as long as the director continues to serve on the applicable vesting date.

In addition, our non-employee directors receive automatic grants of options under our 2005 Stock Plan. Specifically, on July 15, 2005, we granted options to purchase 10,000 shares of Class A Common Stock to each of Messrs. Gotcher, Robertson and Siboni at an exercise price of \$22.75 per share. One-third of the shares covered by these options vest on each of the first three anniversaries of the grant date as long as the director continues to serve on the applicable vesting date. Following each annual meeting of our stockholders beginning with the Annual Meeting, non-employee directors who have been directors for at least six months will receive an option to purchase 10,000 shares of our Class A Common Stock, with one-third of the shares covered by these options vesting on each of the first three anniversaries of the grant date as long as the director continues to serve on the applicable vesting date. These options will become fully vested and exercisable immediately prior to a change in control of the Company.

Directors who are employees of the Company do not receive any compensation for their service on the Board of Directors.

## **Board Meetings and Committees**

The Board of Directors held eight meetings during fiscal 2005. Each of our directors attended at least 75% of the aggregate number of meetings held by the Board of Directors and of the committees on which such director served during fiscal 2005.

The independent members of the Board also meet in executive session without management present on a regular basis. The chairs of the committees rotate as Presiding Director of these executive sessions on an annual basis. Mr. Robertson, the chair of the Nominating and Governance Committee, is the Presiding Director until January 2006, then the chair of the Audit Committee will act as the Presiding Director until January 2007, at which time the chair of the Compensation Committee will act as the Presiding Director until January 2008.

Our Board of Directors has an Audit Committee, a Compensation Committee, a Nominating and Governance Committee, an Outside Director Compensation Committee and a Stock Plan Committee, each of which has the composition and responsibilities described below.

### *Audit Committee*

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The current members of the Audit Committee are Peter Gotcher, Sanford Robertson and Roger Siboni, each of whom is a non-employee member of our Board of Directors. Mr. Siboni is the chairman of our Audit Committee. The Audit Committee held twelve meetings during fiscal 2005. Our Board has determined that each member of our Audit Committee meets the requirements for independence under the current requirements of the NYSE and the Securities and Exchange Commission ( SEC ) rules and regulations. The Board of Directors has also determined that each of Messrs. Gotcher, Robertson and Siboni meet the requirements for financial literacy under the applicable rules and regulations of the NYSE and SEC, and are Audit Committee financial experts as defined in SEC rules. The Audit Committee is responsible for, among other things:

Monitoring the integrity of our financial statements and our compliance with legal and regulatory requirements as they relate to financial statements or accounting matters;

Selecting and hiring our independent auditors, and approving the audit and non-audit services to be performed by our independent auditors;

Evaluating the qualifications, performance and independence of our independent auditors;

Evaluating the performance of our internal audit function;

Reviewing the adequacy and effectiveness of our control policies and procedures;

Acting as our Qualified Legal Compliance Committee ( QLCC ); and

Preparing the Audit Committee report that the SEC requires in our annual Proxy Statement.

The Board of Directors designated the Audit Committee to act as the Company's QLCC. The QLCC was created to review any report made directly, or otherwise made known, to the QLCC by attorneys employed or retained by the Company or its subsidiaries of a material violation of U.S. federal or state securities or other law. The QLCC may receive and consider reports, investigate them, retain material experts or counsel to assist or advise them and make recommendations of an appropriate response. The QLCC may notify the SEC of any material violation.

The Audit Committee has adopted a written charter approved by the Board of Directors, which is included as *Appendix A* to this Proxy Statement. The Audit Committee Charter is also available on the Company's website at <http://www.dolby.com> Investor Relations Corporate Governance.

The report of the Audit Committee is included in this Proxy Statement.

#### *Compensation Committee*

The current members of the Compensation Committee are Peter Gotcher, Sanford Robertson and Roger Siboni, each of whom is a non-employee member of our Board of Directors. Mr. Gotcher is the chairman of our Compensation Committee. The Compensation Committee held seven meetings during fiscal 2005. Our Board has determined that each member of our Compensation Committee meets the requirements for independence under the current requirements of the NYSE and SEC rules and regulations. The Compensation Committee is responsible for, among other things:

Reviewing and approving corporate goals and objectives relevant to CEO compensation and evaluating our CEO's performance in light of those goals and objectives;

Reviewing and recommending to the independent members of the Board for our CEO: annual base salary, annual incentive bonus, including the specific goals and amount, equity compensation, employment agreements, severance arrangements and change in control agreements/provisions, and any other benefits, compensation or arrangements;

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Reviewing and recommending to the Board for our other executive officers: annual base salary, annual incentive bonus, including the specific goals and amount, equity compensation, employment agreements, severance arrangements and change in control agreements/provisions, and any other benefits, compensation or arrangements;

Administering the Company's equity incentive plans, including issuing equity awards under such plans;

Evaluating and recommending to the independent members of our Board compensation plans, policies and programs for our CEO;

Evaluating and recommending to the Board compensation plans, policies and programs for our other executive officers; and

Preparing the Compensation Committee report that the SEC requires in our annual Proxy Statement.

The Compensation Committee has adopted a written charter approved by the Board of Directors, which is available on the Company's website at <http://www.dolby.com> Investor Relations Corporate Governance.

*Nominating and Governance Committee*

The current members of the Nominating and Governance Committee are Peter Gotcher, Sanford Robertson and Roger Siboni, each of whom is a non-employee member of our Board of Directors. Mr. Robertson is the chairman of our Nominating and Governance Committee. The Nominating and Governance Committee held one meeting during fiscal 2005. Our Board has determined that each member of our Nominating and Governance Committee meets the requirements for independence under the current requirements of the NYSE and SEC rules and regulations. The Nominating and Governance Committee is responsible for, among other things:

Assisting the Board in identifying prospective director nominees and recommending to the Board director nominees for each annual meeting of stockholders;

Developing and recommending to the Board governance principles applicable to us;

Overseeing the evaluation of the Board of Directors and management;

Recommending to the Board of Directors members for each Board committee; and

Making an annual report to the Board on succession planning.

The Nominating and Governance Committee has adopted a written charter approved by the Board of Directors, which is available on the Company's website at <http://www.dolby.com> Investor Relations Corporate Governance.

*Outside Director Compensation Committee*

The current members of the Outside Director Compensation Committee are Ray Dolby and Bill Jasper. The Outside Director Compensation Committee did not hold any meetings during fiscal 2005. The Outside Director Compensation Committee is responsible for reviewing and recommending the form and amount of compensation awarded to our non-employee directors.

The Outside Director Compensation Committee has adopted a written charter approved by the Board of Directors, which is available on the Company's website at <http://www.dolby.com> Investor Relations Corporate Governance.

*Stock Plan Committee*

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The current members of the Stock Plan Committee are Peter Gotcher and Bill Jasper. The Stock Plan Committee did not hold any meetings during fiscal 2005. The Stock Plan Committee has the authority to grant equity-based awards to employees and consultants who are not executive officers or directors of the Company within guidelines for the size of grants to particular levels of employees or consultants established by the Company and approved by the Board of Directors or the Compensation Committee. The Stock Plan Committee did not grant any equity-based awards in fiscal 2005. Instead, the Compensation Committee granted all equity-based awards that were made in fiscal 2005.

The Stock Plan Committee has adopted a written charter approved by the Board of Directors, which is available on the Company's website at <http://www.dolby.com> Investor Relations Corporate Governance.

### *Delegation of Authority to CEO*

The Board of Directors has delegated the authority to our CEO to grant new hire, performance, promotion and retention equity-based awards to employees and consultants who are not executive officers or directors of the

Company within guidelines for the size of grants to particular levels of employees or consultants established by the Company and approved by the Board of Directors or the Compensation Committee. The CEO did not grant any equity-based awards in fiscal 2005. Instead, the Compensation Committee granted all equity-based awards that were made in fiscal 2005.

## **Corporate Governance Matters**

### *Code of Business Conduct and Ethics*

The Board of Directors has adopted a Code of Business Conduct and Ethics, which is applicable to our directors and employees, including our principal executive officer, principal financial officer, principal accounting officer or controller and persons performing similar functions. The Code of Business Conduct and Ethics is available on the Company's website at <http://www.dolby.com> Investor Relations Corporate Governance or in print by contacting Investor Relations at our principal executive offices. The Company will post on the Investor Relations section of our website any amendments or waivers to the Code of Business Conduct and Ethics that are required to be disclosed by the rules of the SEC or NYSE.

### *Corporate Governance Guidelines*

The Board of Directors has adopted Corporate Governance Guidelines that address the role and composition of, and policies applicable to, the Board of Directors. The Nominating and Governance Committee will periodically review the guidelines and report any recommendations to the Board. The Corporate Governance Guidelines are available on the Company's website at <http://www.dolby.com> Investor Relations Corporate Governance.

### *Board Independence*

The Board of Directors has determined that, other than Messrs. Dolby and Jasper, each of the directors of the Company has no material relationship with the Company and is independent within the meaning of the standards established by the NYSE and the director independence standards of the SEC as currently in effect. In making that determination, the Board of Directors considered all relevant facts and circumstances, including the director's commercial, accounting, legal, banking, consulting, charitable and familial relationships. The Board of Directors also applied the following standards, which provide that a director will not be considered independent if he:

Is, or has been within the last three years, an employee of the Company, or an immediate family member is, or has been within the last three years, an executive officer of the Company;

Has received, or has an immediate family member who has received, during any twelve-month period within the last three years, more than \$100,000 in direct compensation from the Company, other than director and committee fees and pension or other forms of deferred compensation for prior service (provided such compensation is not contingent in any way on continued service);

Is, or has an immediate family member who is, a current partner of a firm that is the Company's internal or external auditor; is a current employee of such firm, or has an immediate family member who is a current employee of such firm and who participates in the firm's audit, assurance or tax compliance (but not tax planning) practice; or, has, or has an immediate family member who has, been within

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the last three years (but is no longer) a partner or employee of such a firm and personally worked on the Company's audit within that time;

During the past three years, has, or has an immediate family member who has, been employed as an executive officer of another company where any of the Company's present executives at the same time, serve, or served, on the other company's compensation committee; or



Has been employed as an employee, or has an immediate family member who has been employed as an executive officer of, another company that makes payments to, or receives payments from, the Company for property or services in an amount which, in any single fiscal year, exceeds the greater of (a) \$1 million or (b) 2% of such other company's consolidated gross revenues.

*Policy for Director Recommendations and Nominations*

It is the policy of the Nominating and Governance Committee to consider recommendations for candidates to the Board of Directors from stockholders holding at least 250,000 shares of the Company's Common Stock continuously for at least twelve months prior to the date of the submission of the recommendation.

A stockholder that wants to recommend a candidate for election to the Board of Directors should send the recommendation by letter to Dolby Laboratories, Inc., 100 Potrero Avenue, San Francisco, CA 94103-4813, Attn: General Counsel. The recommendation must include the candidate's name, home and business contact information, detailed biographical data, relevant qualifications, a signed letter from the candidate confirming willingness to serve, information regarding any relationships between the candidate and the Company and evidence of the recommending stockholder's ownership of Company stock. Such recommendations must also include a statement from the recommending stockholder in support of the candidate, particularly within the context of the criteria for Board membership, addressing issues of character, integrity, judgment, diversity of experience, independence, area of expertise, corporate experience, length of service, potential conflicts of interest, other commitments and the like and personal references.

The committee will use the following procedures to identify and evaluate any individual recommended or offered for nomination to the Board of Directors:

The committee will consider candidates recommended by stockholders in the same manner as candidates recommended to the committee from other sources;

In its evaluation of director candidates, including the members of the Board of Directors eligible for re-election, the committee will consider the following:

The current size and composition of the Board of Directors and the needs of the Board of Directors and the respective committees of the Board;

Such factors as character, integrity, judgment, diversity of experience, independence, area of expertise, corporate experience, length of service, potential conflicts of interest, other commitments and the like. The committee evaluates these factors, among others, and does not assign any particular weighting or priority to any of these factors; and

Other factors that the committee may consider appropriate.

The committee requires the following minimum qualifications, which are the desired qualifications and characteristics for Board membership, to be satisfied by any nominee for a position on the Board:

The highest personal and professional ethics and integrity;

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Proven achievement and competence in the nominee's field and the ability to exercise sound business judgment;

Skills that are complementary to those of the existing Board;

The ability to assist and support management and make significant contributions to the Company's success; and

An understanding of the fiduciary responsibilities that is required of a member of the Board and the commitment of time and energy necessary to diligently carry out those responsibilities.

If the committee determines that an additional or replacement director is required, the committee may take such measures that it considers appropriate in connection with its evaluation of a director candidate,

including candidate interviews, inquiry of the person or persons making the recommendation or nomination, engagement of an outside search firm to gather additional information, or reliance on the knowledge of the members of the committee, the Board or management; and

The committee may propose to the Board a candidate recommended or offered for nomination by a stockholder as a nominee for election to the Board.

*Stockholder Communications with the Board of Directors*

In cases where stockholders wish to communicate directly with our non-management directors, messages can be sent to our General Counsel, at [generalcounsel@dolby.com](mailto:generalcounsel@dolby.com), or to Dolby Laboratories, Inc., 100 Potrero Avenue, San Francisco, CA 94103-4813, Attn: General Counsel. Our General Counsel monitors these communications and will provide a summary of all received messages to the Board of Directors at each regularly scheduled meeting of the Board of Directors. Where the nature of a communication warrants, our General Counsel may obtain the more immediate attention of the appropriate committee of the Board or non-management director, of independent advisors or of Company management, as our General Counsel considers appropriate. Our General Counsel may decide in the exercise of his or her judgment whether a response to any stockholder communication is necessary.

These procedures do not apply to communications to non-management directors from officers or directors of the Company who are stockholders, or to stockholder proposals submitted pursuant to Rule 14a-8 under the Securities and Exchange Act of 1934, as amended (the Exchange Act ).

*Attendance at Annual Meeting of Stockholders*

We encourage our directors to attend our annual meetings of stockholders. Due to preparations associated with the Company's initial public offering, the directors were in Board of Director and committee meetings on January 27, 2005 and unable to attend the 2005 annual meeting of stockholders.

*Compensation Committee Interlocks and Insider Participation*

There were no interlocks or other relationships among the Company's executive officers and directors that are required to be disclosed under applicable executive compensation disclosure regulations. The members of the Compensation Committee are Peter Gotcher, Sanford Robertson and Roger Siboni.

*Whistleblower Policy*

The Audit Committee has established a telephone and internet whistleblower hotline available to employees of the Company for the anonymous submission of suspected violations, including accounting, internal controls, or auditing matters, harassment, fraud and policy violations.

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### *Formation of a Qualified Legal Compliance Committee*

The Audit Committee was designated by the Board of Directors to act as a Qualified Legal Compliance Committee. For more information see the description of the QLCC under the heading *Audit Committee*.

## SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

The following table sets forth certain information, as of December 13, 2005, as to shares of Common Stock beneficially owned by: (i) each person who is known by the Company to own beneficially more than 5% of either our Class A Common Stock or Class B Common Stock, (ii) each of our directors, (iii) each of our executive officers named under Executive Compensation Summary Compensation Table (the Named Executive Officers) and (iv) all of our directors and executive officers as a group. The information provided in the table is based on our records, information filed with the SEC and information furnished by the respective individuals or entities, as the case may be.

Applicable percentage ownership is based on 34,175,120 shares of Class A Common Stock and 70,478,187 shares of Class B Common Stock outstanding at December 13, 2005. In computing the number of shares of Common Stock beneficially owned by a person and the percentage ownership of that person, we deemed outstanding shares of Common Stock subject to options held by that person that are currently exercisable or exercisable within 60 days of December 13, 2005. We did not deem these shares outstanding, however, for the purpose of computing the percentage ownership of any other person.

Unless otherwise indicated below, the address of each beneficial owner listed on the table is c/o Dolby Laboratories, Inc., 100 Potrero Avenue, San Francisco, CA 94103-4813.

We have determined beneficial ownership in accordance with the rules of the SEC. Except as indicated by the footnotes below, we believe, based on the information furnished to us, that the persons and entities named in the table below have sole voting and investment power with respect to all shares of Common Stock that they beneficially own, subject to applicable community property laws.

| Name of Beneficial Owner                              | Shares Beneficially Owned |      |              |      | Voting Power <sup>(1)</sup> |
|---|---------------------------|------|--------------|------|-----------------------------|
|   | Class A                   |      | Class B      |      |                             |
|   | Common Stock              |      | Common Stock |      |                             |
|   | Shares                    | %    | Shares       | %    | % Total                     |
| <b>5% Stockholders:</b>                               |                           |      |              |      |                             |
| Ray Dolby Trust <sup>(2)</sup>                        |                           |      | 63,333,000   | 89.9 | 85.7                        |
| Ray and Dagmar Dolby Investments, L.P. <sup>(3)</sup> |                           |      | 4,667,000    | 6.6  | 6.3                         |
| T. Rowe Price Associates, Inc. <sup>(4)</sup>         | 4,107,000                 | 12.0 |              |      | *                           |
| Tiger Technology Performance, L.L.C. <sup>(5)</sup>   | 2,030,200                 | 5.9  |              |      | *                           |
| Brown Capital Management, Inc. <sup>(6)</sup>         | 1,813,950                 | 5.3  |              |      | *                           |
| <b>Directors and Executive Officers:</b>              |                           |      |              |      |                             |
| Ray Dolby <sup>(7)</sup>                              | 100                       | *    | 68,000,000   | 96.5 | 92.0                        |
| Bill Jasper <sup>(8)</sup>                            | 1,000                     | *    | 1,082,255    | 1.5  | 1.5                         |
| Janet Daly <sup>(9)**</sup>                           |                           |      | 237,380      | *    | *                           |
| Marty Jaffe <sup>(10)</sup>                           |                           |      | 102,500      | *    | *                           |
| Ed Schummer <sup>(11)</sup>                           | 791                       | *    | 186,910      | *    | *                           |
| David Watts <sup>(12)</sup>                           |                           |      | 152,400      | *    | *                           |
| Peter Gotcher <sup>(13)</sup>                         |                           |      | 70,000       | *    | *                           |

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|  |       |   |            |      |      |
|--|-------|---|------------|------|------|
| Sanford Robertson  |       |   |            |      | *    |
| Roger Siboni <sup>(14)</sup>   |       |   | 33,333     | *    | *    |
| All executive officers and directors as a group (11 persons) <sup>(15)</sup> | 2,891 | * | 70,167,768 | 99.6 | 95.0 |

\* Less than one percent.

\*\* Effective October 24, 2005, Ms. Daly resigned as Chief Financial Officer and transitioned to a non-executive officer position, Vice President, Finance Projects.

- (1) Percentage total voting power represents voting power with respect to all shares of our Class A Common Stock and Class B Common Stock, as a single class. Each holder of Class B Common Stock shall be entitled to 10 votes per share of Class B Common Stock and each holder of Class A Common Stock shall be entitled to one vote per share of Class A Common Stock on all matters submitted to our stockholders for a vote. The Class A Common Stock and Class B Common Stock vote together as a single class on all matters submitted to a vote of our stockholders, except as may otherwise be required by law. The Class B Common Stock is convertible at any time by the holder into shares of Class A Common Stock on a share-for-share basis.
- (2) Shares beneficially owned by the Ray Dolby Trust include 63,333,000 shares held of record by Ray Dolby as Trustee of the Ray Dolby Trust under the Dolby Family Trust Instrument dated May 7, 1999.
- (3) Investment power over the 4,667,000 shares held by Ray and Dagmar Dolby Investments, L.P. is held by Ray Dolby, as Trustee of the Ray Dolby Trust under the Dolby Family Instrument dated May 7, 1999. Voting power over 2,333,500 of the shares held by Ray and Dagmar Dolby Investments, L.P. is held by Thomas E. Dolby, son of Ray and Dagmar Dolby, as Special Trustee of the Ray Dolby 2002 Trust A, dated April 19, 2002. Voting power over 2,333,500 of the shares held by Ray and Dagmar Dolby Investments, L.P. is held by David E. Dolby, son of Ray and Dagmar Dolby, as Special Trustee of the Ray Dolby 2002 Trust B, dated April 19, 2002.
- (4) Based on its Schedule 13G/A filed March 10, 2005, wherein T. Rowe Price Associates, Inc. ( Price Associates ) reported beneficial ownership of 4,107,000 shares of Class A Common Stock, and information supplementally provided to us by Price Associates. These securities are owned by various individuals and institutional investors including T. Rowe Price Mid-Cap Growth Fund, Inc. (which owns 2,500,000 shares, representing 7.3% of the shares of Class A Common Stock outstanding), for which Price Associates serves as investment advisor with power to direct investment and/or sole power to vote the securities. Price Associates reported sole voting power as to 665,000 shares and sole dispositive power as to 4,107,000 shares. T. Rowe Price Mid-Cap Growth Fund, Inc. reported sole voting power as to 2,500,000 shares and no dispositive power as to any shares. For purposes of the reporting requirements of the Exchange Act, Price Associates is deemed to be a beneficial owner of such securities; however, Price Associates expressly disclaims that it is the beneficial owner of such securities. The address for Price Associates is 100 E. Pratt Street, Baltimore, MD 21202.
- (5) Based on the Schedule 13G filed June 14, 2005, wherein Charles P. Coleman, III reported beneficial ownership of 2,030,200 shares of Class A Common Stock. Tiger Technology Performance, L.L.C. ( Tiger Performance ) serves as the general partner of two domestic private investment partnerships. Tiger Technology, Management ( Tiger Management ) has been retained by Tiger Performance to serve as the management company of the two partnerships. Tiger Management also serves as the investment manager of an offshore investment vehicle. Charles P. Coleman, III is the managing member of both Tiger Management and Tiger Performance. In accordance with the foregoing, Tiger Management and Mr. Coleman may be deemed to beneficially own the securities of the Company owned by the various entities managed by Tiger Management. Mr. Coleman and Tiger Management reported shared voting and dispositive power as to 2,030,200 shares and Tiger Performance reported shared voting and dispositive power as to 1,653,552 shares. The address for Mr. Coleman, Tiger Management and Tiger Performance is 101 Park Avenue, 48th Floor, New York, NY 10178.
- (6) Based on its Schedule 13G/A filed September 12, 2005, wherein Brown Capital Management, Inc. ( Brown ) reported beneficial ownership of 1,813,950 shares of Class A Common Stock. Brown reported all of the shares are owned by various investment advisory clients of Brown, which is deemed to be a beneficial owner of those shares pursuant to Rule 13d-3 under the Exchange Act, due to its discretionary power to make investment decisions over such shares for its clients and its ability to vote such shares. In all cases, persons other than Brown have the right to receive, or the power to direct the receipt of, dividends from, or the proceeds from the sale of the shares. No individual client holds more than five percent of the class. Brown reported sole voting power as to 798,450 shares and sole dispositive power as to 1,813,950 shares. The address for Brown is 1201 N. Calvert Street, Baltimore, MD 21202.
- (7) Shares beneficially owned by Ray Dolby include the 63,333,000 shares of Class B Common Stock held of record by Ray Dolby as Trustee of the Ray Dolby Trust under the Dolby Family Instrument dated May 7, 1999, and the 4,667,000 shares of Class B Common Stock held of record by Ray and Dagmar Dolby

Investments, L.P. over which Ray Dolby, as Trustee of the Ray Dolby Trust under the Dolby Family Instrument dated May 7, 1999, holds investment power.

- (8) Shares beneficially owned by Mr. Jasper represent 358,500 shares held by Mr. Jasper, 300,000 shares held of record by the N. William Jasper, Jr. 2004 Irrevocable Trust, 125,000 shares held of record by the Kristen L. McFarland 2004 Irrevocable Trust and options held by Mr. Jasper to purchase 299,755 shares of Class B Common Stock that are exercisable within 60 days of December 13, 2005.
- (9) Includes options held by Ms. Daly to purchase 178,125 shares of Class B Common Stock that are exercisable within 60 days of December 13, 2005.
- (10) Includes options held by Mr. Jaffe to purchase 71,250 shares of Class B Common Stock that are exercisable within 60 days of December 13, 2005.
- (11) Includes options held by Mr. Schummer to purchase 101,250 shares of Class B Common Stock that are exercisable within 60 days of December 13, 2005.
- (12) Includes options held by Mr. Watts to purchase 118,650 shares of Class B Common Stock that are exercisable within 60 days of December 13, 2005.
- (13) Includes options held by Mr. Gotcher to purchase 50,000 shares of Class B Common Stock that are exercisable within 60 days of December 13, 2005.
- (14) Includes options held by Mr. Siboni to purchase 33,333 shares of Class B Common Stock that are exercisable within 60 days of December 13, 2005.
- (15) Includes options held by all executive officers and directors to purchase an aggregate of 881,853 shares of Class B Common Stock that are exercisable within 60 days of December 13, 2005.

## CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

### **Asset Contribution; Licensing Agreements with Ray Dolby Regarding Intellectual Property**

Ray Dolby founded Dolby Laboratories to develop noise reduction technologies he had invented. Throughout nearly all of our 40 year history, Ray Dolby had retained ownership of the intellectual property rights he created related to our business. These intellectual property rights were held by entities affiliated with him that licensed this technology to us in exchange for royalty payments, including royalty payments related to certain trademark usage. Under these licensing and royalty agreements, we recorded expenses for royalties payable to Ray Dolby for the use of certain patent and trademark rights of \$18.7 million in fiscal 2005.

On February 16, 2005, Ray Dolby contributed to us all rights in intellectual property related to our business that he and his affiliates held. In connection with the asset contribution, our previous licensing arrangements with Ray Dolby terminated, and we have no further obligation to pay royalties to Ray Dolby. We agreed to pay Ray Dolby's expenses incurred in connection with the asset contribution, and fifty percent of his expenses incurred as a selling stockholder in connection with our initial public offering. The expenses were approximately \$800,000 in the aggregate.

In connection with the asset contribution agreement, Ray Dolby entered into an employee proprietary rights agreement substantially in the form that all employees of the Company enter into in connection with their employment. This agreement became effective on February 16, 2005. Under the terms of this agreement, all future inventions created by Ray Dolby related to our business while he remains an employee will be assigned to the Company. Under this agreement, Ray Dolby also agreed to abide by a conflicts of interest policy substantially in the form that all other employees are required to sign. However, the conflict of interest policy that Ray Dolby signed differs from our standard policy in that, among other matters, it permits him to use our equipment, supplies and facilities to conduct research and development on matters unrelated to our business; does not apply to any lease agreement we have entered into or may enter into with him; and permits him to have up to a ten percent interest, instead of up to a two percent interest, in a competitor, customer, licensee or supplier without being in violation of the policy and limits the provision of the policy related to having interests in these entities only to direct interests.



**Real Estate Transactions**

*Lease for 100 Potrero Avenue*

Since 1980, we have leased our principal executive offices located at 100 Potrero Avenue, San Francisco, California from Ray Dolby. We also lease additional parking and warehouse space from Ray Dolby in connection with our lease of 100 Potrero Avenue. In December 2005 we renegotiated the leases and extended their terms until December 31, 2013, with two options to extend for an additional five years each. Our rent expense for these facilities was \$3.5 million in fiscal 2005. We are generally responsible for the condition, operation, repair, maintenance, security and management of the properties. We have also agreed to indemnify and hold Ray Dolby, as landlord, harmless from and against certain liabilities, damages, claims, costs, penalties and expenses arising from our conduct related to the properties.

*Jointly Owned Real Estate Entities*

Ray and Dagmar Dolby, the Ray Dolby Trust or the Dolby Family Trust Instrument dated May 7, 1999 ( Dolby Family Trust ) owns a majority financial interest in five real estate entities that own and lease commercial real property to us. We own the remaining financial interests in these real estate entities. The following table sets forth, for each of the five real estate entities, the person or entity that owns the majority financial interest in the real estate entity, the percentage interest owned by the majority owner in such real estate entity and the location of the property subject to the applicable lease. The leased property in San Francisco, California includes our principal administrative offices at 999 Brannan Street.

| <u>Real Estate Entity</u>      | <u>Majority Owner</u> | <u>Majority Ownership</u> | <u>Location of Property</u> |
|--------------------------------|-----------------------|---------------------------|-----------------------------|
|                                |                       | <u>Interest</u>           | <u>Leased to Us</u>         |
| Dolby Properties, LLC          | Ray Dolby Trust       | 62.5%                     | San Francisco, California   |
| Dolby Properties Burbank, LLC  | Dolby Family Trust    | 51.0%                     | Burbank, California         |
| Dolby Properties Brisbane, LLC | Dolby Family Trust    | 51.0%                     | Brisbane, California        |
| Dolby Properties UK, LLC       | Dolby Family Trust    | 51.0%                     | Wootton Bassett, England    |
| Dolby Properties, LP           | Ray and Dagmar Dolby  | 90.0%                     | Wootton Bassett, England    |

Our expense recorded for rents payable to such entities was \$5.5 million in fiscal 2005.

When we negotiate a lease agreement with Ray Dolby or any of the jointly owned real estate entities, we engage real estate brokers to provide fair market rent and lease terms based on a summary of comparable properties located in the area of the subject property. The brokers are instructed that the transaction is intended to be completed on an arm s-length basis. We believe that all of our leases were entered into on a reasonable fair market basis.

The properties owned by Dolby Properties, LLC in San Francisco, California, Dolby Properties Burbank, LLC in Burbank, California, and Dolby Properties UK, LLC in Wootton Bassett, England were purchased with capital contributions and proceeds from bank loans. We guarantee each of these bank loans. As of September 30, 2005, the aggregate outstanding principal balance on all these bank loans was approximately \$13.5 million.

**Other Arrangements with Ray Dolby**

Mr. Dolby received a salary of \$389,423 in fiscal 2005 as an employee of the Company. Mr. Dolby agreed to a reduced salary of \$100,000 on an annualized basis effective January 1, 2006. In fiscal 2005, the Company paid Mr. Dolby's life insurance premiums and he was included in our standard health care and retirement plans, for benefits totaling \$33,109.

In the past, we have allowed Ray Dolby and members of his family the use of our office facilities for their personal purposes on a limited basis, and we expect this use to continue in the future. For example, Ray Dolby

currently uses two offices in one of our facilities for non-Company related activities. In addition, members of Ray Dolby's family use our conference and screening rooms for personal purposes approximately ten times per year. We estimate that the aggregate value to Ray Dolby's family of such personal use was less than \$40,000 in fiscal 2005. In addition, through September of 2005 we paid Ray Dolby \$800 per month for the use by our employees of a condominium he owns in Lake Tahoe, California. Commencing in October of 2005, the rent was increased to \$1,200 per month. Our Board of Directors has approved of these arrangements, and has approved the continuation of these arrangements in the future.

## EXECUTIVE COMPENSATION

The following table summarizes all compensation paid to or accrued for (i) the Company's Chief Executive Officer and (ii) each of the Company's other four most highly compensated executive officers as of September 30, 2005 for services rendered in all capacities to the Company for the fiscal years ended September 30, 2005 and September 24, 2004.

Summary Compensation Table

| Name and Principal Position   | Fiscal Year | Annual Compensation        |                           | Long-Term Compensation        | All Other Compensation (\$) <sup>(3)(4)</sup> |
|---|-------------|----------------------------|---------------------------|-------------------------------|---|
|   |             | Salary (\$) <sup>(1)</sup> | Bonus (\$) <sup>(2)</sup> | Securities Underlying Options |   |
| Bill Jasper<br>President and Chief Executive Officer  | 2005        | 611,539                    | 383,078                   | 80,000                        | 33,840 <sup>(5)</sup>                         |
|   | 2004        | 592,949                    | 1,723,165 <sup>(6)</sup>  | 900,000                       | 228,716 <sup>(7)</sup>                        |
| Janet Daly<br>Vice President and Chief Financial Officer*   | 2005        | 292,414                    | 158,123 <sup>(8)</sup>    | 10,000                        | 32,250 <sup>(9)</sup>                         |
|   | 2004        | 242,729                    | 274,844                   | 150,000                       | 133,941 <sup>(10)</sup>                       |
| Marty Jaffe<br>Executive Vice President, Business Affairs   | 2005        | 357,287                    | 173,218                   | 60,000                        | 25,378 <sup>(11)</sup>                        |
|   | 2004        | 334,395                    | 272,658                   | 180,000                       | 57,276 <sup>(12)</sup>                        |
| Ed Schummer<br>Senior Vice President and General Manager, Consumer Division                       | 2005        | 339,212                    | 155,274                   | 50,000                        | 32,498 <sup>(13)</sup>                        |
|   | 2004        | 326,445                    | 206,189                   | 180,000                       | 180,611 <sup>(14)</sup>                       |
| David Watts <sup>(15)</sup><br>Senior Vice President and Managing Director, United Kingdom Branch | 2005        | 318,600                    | 151,144                   | 30,000                        | 53,649 <sup>(16)</sup>                        |
|   | 2004        | 311,034                    | 206,321                   | 180,000                       | 56,753 <sup>(17)</sup>                        |

\* Effective October 24, 2005, Ms. Daly resigned as Chief Financial Officer and transitioned to a non-executive officer position, Vice President, Finance Projects.

- (1) For fiscal 2004, amounts shown represent 52 weeks of salary. For fiscal 2005, amounts shown represent 53 weeks of salary.
- (2) Includes (in each fiscal year) bonuses earned during the fiscal year and paid in the subsequent fiscal year.
- (3) Amounts include employer-matching contributions under our retirement plan. Fiscal 2004 included pay periods for a 52-week year, while fiscal 2005 included pay periods for a 53-week year.
- (4) We previously paid premiums for split-dollar life insurance policies for certain of our executive officers. We ceased these payments in fiscal 2004 and transferred the full value of those policies to the executive officer. In addition, in fiscal 2004 we received a cash dividend

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from an insurer on the split-dollar life insurance policies, which we allocated among the executive officers covered by policies with that insurer.

- (5) Includes \$22,800 in profit-sharing and matching 401(k) plan contributions under our retirement plan, \$2,640 in life insurance premiums and \$8,400 received in connection with an auto allowance.
- (6) Includes \$1,185,415 for a non-cash stock bonus of 571,560 shares (not subject to vesting) granted in January 2004, based on the value on the date of award of \$2.074 per share.

- (7) Includes \$33,386 in profit-sharing and matching 401(k) plan contributions under our retirement plan, \$792 in life insurance premiums, \$103,394 in contributions under our senior executive supplemental retirement plan, \$53,048 received in connection with the transfer of a split-dollar life insurance policy, \$29,696 received in connection with the allocation of a dividend received on split-dollar life insurance policies and \$8,400 received in connection with an auto allowance. We ceased making contributions under our senior executive supplemental retirement plan in fiscal 2004.
- (8) Includes an extension bonus of \$25,000 pursuant to the terms of an employment transition agreement.
- (9) Includes \$22,800 in profit-sharing and matching 401(k) plan contributions under our retirement plan, \$2,250 in life insurance premiums and \$7,200 received in connection with an auto allowance.
- (10) Includes \$25,273 in profit-sharing and matching 401(k) plan contributions under our retirement plan, \$672 in life insurance premiums, \$28,990 in contributions under our senior executive supplemental retirement plan, \$71,806 received in connection with the transfer of a split-dollar life insurance policy and \$7,200 received in connection with an auto allowance. We ceased making contributions under our senior executive supplemental retirement plan in fiscal 2004.
- (11) Includes \$22,800 in profit-sharing and matching 401(k) plan contributions under our retirement plan and \$2,578 in life insurance premiums.
- (12) Includes \$26,694 in profit-sharing and matching 401(k) plan contributions under our retirement plan, \$756 in life insurance premiums and \$29,826 received in connection with the transfer of a split-dollar life insurance policy.
- (13) Includes \$22,800 in profit-sharing and matching 401(k) plan contributions under our retirement plan, \$2,498 in life insurance premiums and \$7,200 received in connection with an auto allowance.
- (14) Includes \$26,307 in profit-sharing and matching 401(k) plan contributions under our retirement plan, \$732 in life insurance premiums, \$45,646 in contributions under our senior executive supplemental retirement plan, \$83,891 received in connection with the transfer of a split-dollar life insurance policy, \$16,835 received in connection with the allocation of a dividend received on split-dollar life insurance policies and \$7,200 received in connection with an auto allowance. We ceased making contributions under our senior executive supplemental retirement plan in fiscal 2004.
- (15) Amounts derived from United Kingdom pounds for fiscal 2005 have been expressed in U.S. dollars based on the noon buying rate for the United Kingdom pound of \$1.77 on September 30, 2005 and, for fiscal 2004, have been expressed in U.S. dollars based on the noon buying rate for the United Kingdom pound of \$1.8031 on September 24, 2004.
- (16) Includes \$53,649 in contributions under our United Kingdom group personal pension plan and funded unapproved retirement benefits scheme.
- (17) Includes \$53,642 in contributions under our United Kingdom group personal pension plan and funded unapproved retirement benefits scheme and \$3,110 in life insurance premiums.

#### *Incentive Compensation*

Our executive officers are eligible for incentive compensation pursuant to our annual incentive plan. In fiscal 2005, this incentive compensation had two distinct components: a profit sharing component, in which the executive officer receives 5% of his or her base salary if we achieved certain overall profit goals, and a performance reward component, in which the executive officer receive a bonus based on both Company and individual performance objectives. The performance reward bonus was also calculated as a percentage of the executive officer's base salary. Our executive officers' targeted standard bonus amounts for fiscal 2005 were 70% of our Chief Executive Officer's base salary and 45% to 50% of our other executive officers' respective base salaries.

The portion of the performance reward bonuses attributable to either the Company or individual performance objectives was weighted based on the employee's position within the Company. For our executive officers, including our Chief Executive Officer, 75% of the total performance reward bonus was tied to Company performance objectives and 25% to individual performance objectives.

The actual bonus amount payable to each executive officer was based on the percentage by which the performance objectives were met. Bonuses payable could range from 75% to 200% of the targeted amount for the Company performance-based bonus, and up to 100% of the targeted amount for the individual performance-based bonus. In addition, the annual incentive plan provided for discretion in awarding bonuses in excess of the maximum individual performance-based bonus in years that we did not reach our Company performance objectives.

For fiscal 2005, the Compensation Committee recommended and the Board of Directors approved for our executive officers Company performance objectives related to the achievement of a certain level of revenue and pre-tax margin, and individual performance objectives for each executive officer, including management objectives related to business development, research expansion, new product introduction, and internal controls and procedures depending on the particular officer.

See *Proposal 2* for proposed changes to the incentive compensation plan.

*Senior Executive Supplemental Retirement Plan and U.K. Funded Unapproved Retirement Benefits Scheme*

*Senior Executive Supplemental Retirement Plan.* We maintain a nonqualified senior executive supplemental retirement plan, which provides supplemental retirement benefits for a select group of executive employees based on contributions we made to the plan and the gains and losses on the investment of those contributions. Distributions from the senior executive supplemental retirement plan are made in a single lump sum, or, at a participant's election, in up to ten installments. Prior to fiscal 2005 we made annual contributions on behalf of each participant in an amount necessary to fund a hypothetical joint and 50% survivor annuity benefit payable to each participant commencing at age 65. The hypothetical monthly benefit is determined on the basis of an 8% interest rate and a standard mortality table by multiplying (i) 2% of a participant's projected average annual compensation by (ii) a participant's total expected years of service with us up to 30 years. A participant's projected average annual compensation is determined by averaging the participant's estimated annual compensation over the three consecutive years of service occurring in the participant's final three plan years preceding attainment of age 65. Each participant is 100% vested in his or her interest in the senior executive supplemental retirement plan at all times. Upon a participant's termination of service with us for any reason other than death, a participant is entitled to his or her account balance determined as of the valuation date immediately preceding his or her termination date, which amount will be paid in a single lump sum or in up to ten installments. Upon a participant's death, the participant's beneficiary will receive all amounts credited to the participant's account as of the date of death and will be paid in a single lump sum. Amounts contributed by us under the senior executive supplemental retirement plan are held in a rabbi trust and a participant's account will be credited with investment gains and losses based on investments selected by the participant. However, if a participant fails to make an investment election, the trustee of the senior executive supplemental retirement plan may direct such investments. In fiscal 2005, the Board of Directors amended and restated the plan to comply with Section 409A of the Internal Revenue Code (the "Code") and Internal Revenue Service regulations under Section 409A and terminated the plan. As a result of the termination of the plan, no additional amounts will be contributed to participants under the plan, but amounts already credited to participants under the plan will remain subject to the terms and conditions of the plan and will continue to be credited with gains and losses based on the gains and losses of investment funds designated by the Company and selected by the participant. Distributions under the plan will be made in the manner and at the time described above without regard to the termination of the plan.

*U.K. Funded Unapproved Retirement Benefits Scheme.* In addition, certain executives in the United Kingdom may participate in the Dolby Laboratories Funded Unapproved Retirement Benefits Scheme ("FURBS"). The FURBS is similar to the senior executive supplemental retirement plan. Under the FURBS we make annual contributions on behalf of each participant in an amount necessary to fund, taking into account any contributions to the senior executive supplemental retirement plan, a hypothetical joint and 50% survivor annuity benefit payable to each participant commencing at age 65 and, under certain circumstances, before then. The hypothetical monthly benefit is determined based on the same assumptions as those used for the senior executive supplemental retirement plan. In addition, participants are also allowed to make voluntarily contributions to the

FURBS. Distributions from the FURBS may be made in a single lump sum, by a life policy or an annuity paid at retirement. Each participant is 100% vested in his or her interest in the FURBS at all times. Upon a participant's death, the participant's beneficiary will receive all benefits credited to the participant's account. Amounts contributed by us under the FURBS are held in a trust and a participant's account will be credited with investment gains and losses based on investments selected by the trustee. Our board of directors may at any time amend (with the agreement of the participant) or terminate the FURBS.

## Stock Options

The following tables set forth certain information as of September 30, 2005 and for the fiscal year then ended with respect to stock options granted to and exercised by the Named Executive Officers.

### Option Grants in Last Fiscal Year

| Name        | Individual Grants   |   |                                       |                 | Potential Realizable Value at Assumed Annual Rates of Stock Price Appreciation for Option Term <sup>(5)</sup> |              |
|-------------|---|---|---------------------------------------|-----------------|---|--------------|
|             | Number of Securities Underlying Options Granted <sup>(1)(2)</sup> | Percent of Total Options Granted to Employees in Fiscal Year <sup>(3)</sup> | Exercise Price (\$/Sh) <sup>(4)</sup> | Expiration Date | 5%(\$)  | 10%(\$)      |
| Bill Jasper | 80,000  | 3.56  | \$ 19.20                              | 6/16/2015       | \$ 965,982  | \$ 2,447,988 |
| Janet Daly* | 10,000  | 0.44  | \$ 19.20                              | 6/16/2015       | \$ 120,748  | \$ 305,999   |
| Marty Jaffe | 60,000  | 2.67  | \$ 19.20                              | 6/16/2015       | \$ 724,487  | \$ 1,835,991 |
| Ed Schummer | 50,000  | 2.22  | \$ 19.20                              | 6/16/2015       | \$ 603,739  | \$ 1,529,993 |
| David Watts | 30,000  | 1.33  | \$ 19.20                              | 6/16/2015       | \$ 362,243  | \$ 917,996   |

\* Effective October 24, 2005, Ms. Daly resigned as Chief Financial Officer and transitioned to a non-executive officer position, Vice President, Finance Projects.

- (1) Options were granted under our 2005 Stock Plan and have a term of ten years, subject to earlier termination relating to termination of employment.
- (2) Options become exercisable in four equal annual installments beginning on July 1, 2006, the first anniversary of the vesting commencement date, and under certain circumstances in connection with a change in control of the Company.
- (3) The percentage is based on options to purchase an aggregate of 2,249,170 shares of our Class A Common Stock granted to our employees during fiscal 2005.
- (4) The exercise price is equal to the fair market value of our Class A Common Stock on the date of grant as determined by the closing price of our Class A Common Stock on the day the option was granted as reported by the NYSE.
- (5) The amounts shown in the table as potential realizable value represent hypothetical gains that could be achieved if options are exercised at the end of the option term. The assumed 5% and 10% rates of stock price appreciation are provided in accordance with SEC rules and do not represent our estimate or projection of the future stock price. Potential realizable values are net of exercise price.

**Aggregated Option Exercises in Last Fiscal Year**

**And Fiscal Year End Option Values**

| Name        | Shares Acquired<br>on Exercise (#) | Value<br>Realized (\$)    | Number of Securities<br>Underlying Unexercised<br>Options at<br>September 30, 2005 (#) | Value of Unexercised<br>In-the-Money Options at<br>September 30, 2005 (\$) <sup>(1)</sup> |
|-------------|------------------------------------|---------------------------|--|---|
|             |                                    |                           | Exercisable/<br>Unexercisable  | Exercisable/<br>Unexercisable   |
| Bill Jasper | 44,610                             | \$ 746,771 <sup>(2)</sup> | 287,500/880,000  | \$ 4,053,250/\$11,238,500   |
| Janet Daly* | 12,470                             | \$ 208,748 <sup>(2)</sup> | 46,875/141,250   | \$ 660,188/\$1,842,375  |
| Marty Jaffe |                                    |                           | 63,750/220,000   | \$ 902,775/\$2,247,700  |
| Ed Schummer |                                    |                           | 149,780/222,500  | \$ 2,170,857/\$2,431,950  |
| David Watts | 33,750                             | \$ 727,988 <sup>(3)</sup> | 106,150/190,000  | \$ 1,527,751/\$2,247,700  |

\* Effective October 24, 2005, Ms. Daly resigned as Chief Financial Officer and transitioned to a non-executive officer position, Vice President, Finance Projects.

- (1) Calculated on the basis of the fair market value of the underlying securities at September 30, 2005 (\$16.00 per share) minus the exercise price.
- (2) Options were exercised prior to our initial public offering and the value realized is calculated on the basis of our initial public offering price of \$18.00 minus the exercise price.
- (3) Options were exercised following our initial public offering and the value realized is calculated on the basis of the fair market value of the underlying securities at the exercise date minus the exercise price.

### Employment Agreements and Change in Control Arrangements

#### *Employment Agreements*

Marty Jaffe, our Executive Vice President, Business Affairs, executed an offer letter dated September 28, 2000, effective as of November 1, 2000. Mr. Jaffe's fiscal 2005 base salary was \$357,287. He is eligible for annual bonus compensation under our annual incentive plan as well as a discretionary bonus. In the event Mr. Jaffe's employment terminates without cause, he will be entitled to receive severance equal to twelve months of his then current salary.

In January 2005, we entered into an employment transition agreement with Janet Daly, our then Chief Financial Officer and Vice President, in connection with her announcement of her intention to retire as our Chief Financial Officer prior to the end of calendar 2005. Effective October 24, 2005, Ms. Daly transitioned to Vice President, Finance Projects and her annual salary decreased to \$275,000. In the event that Ms. Daly were to work for us on a part-time basis, her salary would be pro-rated to reflect her part-time employment status. Under the terms of her agreement, all options held by Ms. Daly as of December 31, 2004 became fully vested and exercisable on December 31, 2005.

#### *Change in Control Arrangements*



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Our 2000 Stock Incentive Plan and 2005 Stock Plan provide for the acceleration of vesting of awards in certain circumstances in connection with or following a change in control of the Company.

**Equity Compensation Plan Information**

The following table sets forth information regarding outstanding options and shares reserved for future issuance under our equity compensation plans as of September 30, 2005:

| Plan Category  | Class of<br>Common<br>Stock | Number of<br>securities to be<br>issued upon<br>exercise of<br>outstanding options | Weighted-average<br>exercise price<br>of<br>outstanding<br>options | Number of securities<br>remaining available for<br>future issuance under<br>equity compensation<br>plans (excluding<br>securities reflected in<br>column (a)) |
|--|-----------------------------|--|--|---|
|  |                             | (a)  | (b)  | (c)   |
| Equity compensation plans approved by<br>security holders <sup>(1)</sup> | Class A                     | 1,375,920  | \$ 19.19   | 5,624,080 <sup>(2)</sup>  |
|  | Class B                     | 10,544,885   | \$ 2.15  | 134,690 <sup>(3)</sup>  |
| Equity compensation plans not approved by<br>security holders            | Class A                     |  |  |   |
|  | Class B                     |  |  |   |
| Total  | Class A                     | 1,375,920  | \$ 19.19   | 5,624,080 <sup>(2)</sup>  |
|  | Class B                     | 10,544,885   | \$ 2.15  | 134,690 <sup>(3)</sup>  |

(1) Consists of the 2000 Stock Incentive Plan, the 2005 Stock Plan and the Employee Stock Purchase Plan.

(2) Includes 1,000,000 shares available for issuance under the Company's Employee Stock Purchase Plan.

(3) Includes 134,690 shares available for issuance under the 2000 Stock Incentive Plan. Our Board of Directors decided not to grant any additional options under the 2000 Stock Incentive Plan following the completion of our initial public offering on February 17, 2005.

*2000 Stock Incentive Plan*

Effective October 2000, we adopted the 2000 Stock Incentive Plan. The 2000 Stock Incentive Plan, as amended in April 2004 and September 2004, provides for the issuance of incentive and nonqualified stock options to employees, directors and consultants of Dolby Laboratories to purchase up to 15.1 million shares of Class B Common Stock. Under the terms of this plan, options become exercisable as established by the Board of Directors (generally ratably over four years), and generally expire ten years after the date of the grant. Options granted under the plan are generally granted at not less than fair market value at the date of grant, but the plan permits options to be granted at less than fair value. Our Board of Directors decided not to grant any additional options under the 2000 Stock Incentive Plan following the completion of our initial public offering on February 17, 2005.

*2005 Stock Plan*

In January 2005 our stockholders approved our 2005 Stock Plan, which our Board of Directors adopted in November 2004. The 2005 Stock Plan became effective on February 16, 2005, the day prior to the completion of our initial public offering. Our 2005 Stock Plan provides for the ability to grant incentive stock options, non-statutory stock options, restricted stock, stock appreciation rights (SARs), deferred stock units, performance units and performance shares. A total of 6,000,000 shares of our Class A Common Stock is authorized for issuance under the 2005 Stock Plan. Any shares subject to an award with a per share price less than the fair market value of our Class A Common Stock on the date of

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grant will be counted against the authorized share reserve as two shares for every one share subject to the award, and if returned to the 2005 Stock Plan, such shares will be counted as two shares for every one share returned.

*See Proposal 2 for proposed changes to the 2005 Stock Plan.*

*Employee Stock Purchase Plan*

In January 2005, our Board of Directors adopted and our stockholders approved our Employee Stock Purchase Plan ( ESPP ) which allows eligible employees to have up to 10 percent of their eligible compensation withheld and used to purchase shares of our Class A Common Stock. The ESPP became effective on February 16, 2005, and the first purchase took place on November 15, 2005. For the first offering period, the plan provided for the purchase of shares at 95 percent of the lower of the Company's initial public offering price of \$18.00 or the closing price on the NYSE on the last day of the offering period. For subsequent offering periods, the purchase price will be 95 percent of the closing price on the NYSE on the last day of the purchase period. With the exception of the first offering period, offering periods generally start on the first day on or after May 15th and November 15th of each year. A total of 1,000,000 shares of our Class A Common Stock are authorized for sale under the ESPP.

**REPORT OF THE COMPENSATION COMMITTEE  
OF THE BOARD OF DIRECTORS ON EXECUTIVE COMPENSATION**

*This report shall not be deemed incorporated by reference by any general statement incorporating by reference this Proxy Statement into any filing under the Securities Act of 1933 (the "Securities Act") or under the Exchange Act, except to the extent the Company specifically incorporates this report by reference, and shall not otherwise be deemed filed under such Acts.*

**Compensation Philosophy and Objectives**

The Company's compensation program is vital to its success. The Compensation Committee believes that compensation of the Company's executive officers should:

Provide a competitive total compensation package that enables the Company to attract, motivate and retain, on a long-term basis, high caliber personnel;

Encourage creation of stockholder value and achievement of strategic corporate objectives;

Recognize individual initiative, effort and accomplishment;

Provide a total compensation program, which includes elements of both annual and long-term compensation, to focus management on the Company's annual and long-term corporate objectives and strategy; and

Align the interests of management and stockholders and enhance stockholder value by providing management with longer-term incentives through equity ownership by management.

We base compensation on the level of job responsibility, individual performance, and Company performance. As employees progress to higher levels in the organization, an increasing proportion of their pay is linked to Company performance.

**Key Elements of Executive Compensation**

For fiscal 2005, the primary components of the executive officers' compensation were base salary, bonus and stock options. To ensure that the primary components of the Company's compensation structure reflected the Compensation Committee's philosophy, the Compensation Committee consulted with an independent outside consultant, Watson Wyatt & Company, to review the Company's salary, bonus and equity programs and to recommend to the Compensation Committees any appropriate changes to the overall compensation program.

Compensation levels for executive officers were largely determined through a competitive analysis of 14 public companies as a primary external reference peer group, as well as review of published surveys. The peer group was chosen based on industry and business focus and was

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comprised of the following companies: Harman International, Scientific-Atlanta, Inc., Avid Technology, Inc., Polycom, Inc., Macromedia, Inc., Pinnacle Systems, Inc., RealNetworks, Inc., DSP Group, Inc., Macrovision Corporation, IMAX Corporation, InterDigital Communications Corporation, Digimarc Corporation, InterVideo, Inc. and DTS, Inc.

To the extent possible, comparisons with the peer group were made on an executive officer level position-by-position basis. Elements of compensation compared included: base salary, annual bonus as a percentage of base salary, total cash compensation, long-term incentives, total equity holdings and total direct compensation (total cash compensation plus expected value of long-term incentives). The Compensation Committee also considered the recommendations of the Company's Chief Executive Officer with respect to the compensation of other executive officers.

### ***Base Salary***

Base salary and total cash compensation (salary plus bonus) for the Company's executive officers is generally targeted at the 60th to 75th percentile range of the peer group. Base salaries are paid on a calendar year basis. In establishing base salaries for calendar 2005 the Compensation Committee considered, among other things, the Company's achievement of financial objectives, achievements in marketing, development of digital cinema products, building an infrastructure to support being a public company, and preparing for lead free manufacturing in fiscal 2004, as well as the individual contributions and achievements of each executive officer in fiscal 2004. Actual compensation is based on an evaluation of job responsibilities for the position, comparisons of compensation levels, Company achievements and individual performance. Individual performance is evaluated by reviewing organizational and management development progress against individual contributions and achievements. Compensation levels for the executive officers are competitive within a range that the Compensation Committee considers to be reasonable and necessary to attract and retain quality executives.

### ***Bonus***

At the beginning of fiscal 2005 and prior to our initial public offering, the Compensation Committee recommended and the Board approved for our executive officers Company performance objectives for fiscal 2005 related to the achievement of a certain level of revenue and pre-tax margin, and individual performance objectives for each executive officer, including management objectives related to business development, research expansion, new product introduction, and internal controls and procedures depending on the particular officer. For fiscal 2005, the independent members of the Board of Directors awarded a cash bonus to our Chief Executive Officer, and the full Board of Directors awarded cash bonuses to the other executive officers, both at the recommendation of the Compensation Committee. The bonuses were based on the extent to which Company objectives and individual objectives were achieved.

In fiscal 2005, this incentive compensation had two distinct components: a profit sharing component, in which the executive officer received 5% of his or her base salary if we achieved 100% of overall profit goals, and a performance reward component, in which the executive officer received a bonus based on both Company and individual performance objectives. The performance reward bonus was also calculated as a percentage of the executive officer's base salary. Our executive officers' bonus target amounts for fiscal 2005 were 70% of base salary for our Chief Executive Officer and 45% to 50% of base salary for our other executive officers. For our executive officers, including our Chief Executive Officer, 75% of the total performance reward bonus was tied to achievement of Company performance objectives and 25% to achievement of individual performance objectives.

The actual bonus amount paid to each executive officer was based on the extent to which the performance objectives were met. Bonuses payable could range from 75% to 200% of the targeted amount for the Company performance-based bonus, and up to 100% of the targeted amount for the individual performance-based bonus. Although the annual incentive plan provided for discretion for fiscal 2005 in awarding bonuses in excess of the maximum individual performance-based bonus if we did not reach our Company performance objectives, this discretion was not exercised for executive officer bonuses.

Pursuant to a delegation of authority by the Company's Board of Directors, the Compensation Committee, which is currently comprised of all of the independent members of the Company's Board of Directors, has approved the Company performance objectives and individual performance objectives for our executive officers for fiscal 2006 and, going forward, will have the authority to approve the Company performance objectives and individual performance objectives for our executive officers.

### ***Stock Options***

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Long-term incentive compensation for the Company's executive officers is generally targeted at the 25th percentile of the peer group.



The Company's 2005 Stock Plan and 2000 Stock Incentive Plan are administered by the Compensation Committee. However, the Board of Directors has delegated to both the Chief Executive Officer and the Stock Plan Committee the authority to grant equity-based awards to employees and consultants who are not executive officers or directors of the Company within guidelines for the size of grants to particular levels of employees or consultants established by the Company and approved by the Board of Directors. The Compensation Committee believes that by providing those persons who have substantial responsibility for the management and growth of the Company with an opportunity to increase their ownership of Company stock, the best interests of stockholders and executives will be closely aligned. Therefore, executive officers, as well as employees and consultants, are eligible to receive stock options under the 2005 Stock Plan from time to time, giving them the right to purchase shares of Common Stock of the Company at a specified price. Prior to the Company's initial public offering, the Board of Directors decided not to grant any additional options under our 2000 Stock Incentive Plan.

In fiscal 2005, the Compensation Committee awarded a total of 355,000 options to our Chief Executive Officer and the other executive officers. The total amount of options granted to our executive officers in fiscal 2005 represented 15.8% of the total amount of options granted to all employees in fiscal 2005. In determining the amount of stock options granted to an individual executive, the Compensation Committee considered such factors as awards previously granted, outstanding awards, the vesting schedule of outstanding awards, the aggregate total of all outstanding awards and the relative quantity of awards offered by companies within the peer group to executives in comparable positions.

#### ***Other Elements of Compensation***

Other elements of the Company's executive officer compensation program include an Employee Stock Purchase Plan and profit-sharing and matching 401(k) plan contributions under the Company's retirement plan. Although the Company maintains a senior executive supplemental retirement plan, the Company ceased making contributions to the plan in fiscal 2004.

#### **Fiscal 2005 CEO Compensation**

In establishing Mr. Jasper's compensation for fiscal 2005, we applied the principles outlined above in the same manner as they were applied to the other executives. As part of this process, the Compensation Committee considered the recommendations of its independent outside consultant as well as the historical compensation levels paid to chief executive officers by those companies selected for peer group comparison. Mr. Jasper's salary for calendar 2005 was \$600,000, which was unchanged from his salary for calendar 2004. Due to an extra pay period in fiscal 2005 (53 weeks in fiscal 2005 versus 52 weeks in fiscal 2004), Mr. Jasper's salary for fiscal 2005 was \$611,539.

In determining Mr. Jasper's annual bonus for fiscal 2005, the Compensation Committee evaluated his performance for fiscal 2005 and made a recommendation to the independent members of the Board of Directors. In this regard, the Compensation Committee considered the Company's achievement of a certain level of revenue and pre-tax margin in fiscal 2005 and Mr. Jasper's accomplishment of objectives that had been established at the beginning of the fiscal year relating to enhancing our leadership in broadcast applications, enhancing the Dolby brand, taking our digital cinema product line to market, and progress towards adoption of Dolby technologies in China.

Based on the formulas for Mr. Jasper's profit sharing and performance reward components described above and the Compensation Committee's recommendation, the independent members of the Board of Directors granted Mr. Jasper a bonus of \$383,078 for his efforts in fiscal 2005. This placed Mr. Jasper's salary and bonus compensation within the 60th to 75th percentile target range of historical salaries and bonus compensation paid by those companies selected for peer group comparison.

In recognition of the Company's achievement of financial objectives, achievements in marketing, development of digital cinema products, building an infrastructure to support being a public company, and preparing for lead free manufacturing in fiscal 2004, in fiscal 2005, the Compensation Committee awarded 80,000 options to our Chief Executive Officer. In addition, the Compensation Committee considered the factors discussed under Stock Options above. The total amount of options granted to our Chief Executive Officer in fiscal 2005 represented 3.6% of the total amount of options granted to all employees in fiscal 2005.

The Compensation Committee believes that Mr. Jasper's performance in fiscal 2005 met its expectations. Under Mr. Jasper's leadership, the Company achieved record revenue in fiscal 2005, a 13% increase over fiscal 2004 revenue as well as strong pre-tax margin in fiscal 2005. In addition, during fiscal 2005 the Company successfully completed its initial public offering raising over \$263 million. The Compensation Committee considers Mr. Jasper's overall compensation level for fiscal 2005 to be competitive, reasonable and necessary.

Mr. Jasper is a member of the Board of Directors, but he did not participate in Board or Compensation Committee deliberations regarding the setting of his compensation for fiscal 2005.

#### **Miscellaneous**

The Company's policy generally is to attempt to qualify compensation, including stock options and annual incentive bonuses, awarded or paid to executive officers for deductibility under Section 162(m) of the Code. However, interpretations of and changes in applicable tax laws and regulations as well as other factors beyond the Compensation Committee's control also can affect deductibility of compensation. For these and other reasons, the Compensation Committee has determined that it may not necessarily seek to limit executive compensation to that deductible under Section 162(m) of the Code.

#### **Compensation Committee**

Peter Gotcher, Chairman

Sanford Robertson

Roger Siboni

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**REPORT OF THE AUDIT COMMITTEE OF THE BOARD OF DIRECTORS**

*This report shall not be deemed incorporated by reference by any general statement incorporating by reference this Proxy Statement into any filing under the Securities Act or under the Exchange Act, except to the extent the Company specifically incorporates this report by reference, and shall not otherwise be deemed filed under such Acts.*

The Audit Committee of the Board of Directors is comprised of three directors, each of whom qualifies as independent under the current listing requirements of the NYSE. The current members of the Audit Committee are Peter Gotcher, Sanford Robertson and Roger Siboni. The Audit Committee acts pursuant to a written charter that was originally adopted by the Board of Directors on November 3, 2004 and is included with this Proxy Statement as *Appendix A*.

In performing its functions, the Audit Committee acts in an oversight capacity and relies on the work and assurances of (i) the Company's management, which has the primary responsibility for financial statements and reports and the Company's internal controls, and (ii) the independent registered public accounting firm, which, in its report, expresses an opinion on the conformity of the Company's annual financial statements with accounting principles generally accepted in the United States. It is not the duty of the Audit Committee to plan or conduct audits, to determine that the Company's financial statements are complete and accurate and are in accordance with generally accepted accounting principles, or to assess the Company's internal control over financial reporting.

Within this framework, the Audit Committee has reviewed and discussed with management the Company's audited financial statements as of and for the fiscal year ended September 30, 2005 and the Company's internal control over financial reporting. The Audit Committee has also discussed with the independent registered public accounting firm the matters required to be discussed by Statement on Auditing Standards No. 61, as amended. In addition, the Audit Committee has received the written disclosures from the independent registered public accounting firm required by Independence Standards Board Standard No. 1, has discussed with the independent registered public accounting firm, KPMG LLP, the independence of that firm and has considered whether the provision of non-audit services was compatible with maintaining the independence of that firm.

Based upon these reviews and discussions, the Audit Committee recommended to the Board of Directors that the audited financial statements be included in the Company's Annual Report on Form 10-K for the fiscal year ended September 30, 2005.

**Audit Committee**

Roger Siboni, Chairman

Peter Gotcher

Sanford Robertson

**STOCK PRICE PERFORMANCE GRAPH**

The following graph illustrates a comparison of the total return of the Company's Class A Common Stock with the total return for the New York Stock Exchange Composite Index (the NYSE Composite) and the Russell 3000 Index (the Russell 3000) for the period from February 17, 2005 (the date the Company's Class A Common Stock commenced trading on the NYSE) through September 30, 2005. The figures represented below assume an investment of \$100 in the Company's Class A Common Stock at the closing price on February 17, 2005 (\$24.30) and in the NYSE Composite and the Russell 3000 on January 31, 2005 and the reinvestment of dividends into shares of common stock. The comparisons in the table are required by the SEC and are not intended to forecast or be indicative of possible future performance of the Company's Class A Common Stock.

|                          | Cumulative Total Return |         |         |         |         |         |         |         |         |
|--------------------------|-------------------------|---------|---------|---------|---------|---------|---------|---------|---------|
|                          | 2/17/05                 | 2/28/05 | 3/31/05 | 4/29/05 | 5/31/05 | 6/30/05 | 7/29/05 | 8/31/05 | 9/30/05 |
| DOLBY LABORATORIES, INC. | 100.00                  | 94.98   | 96.71   | 84.16   | 82.06   | 90.78   | 78.31   | 65.84   | 65.84   |
| NYSE COMPOSITE           | 100.00                  | 102.67  | 100.14  | 97.05   | 101.83  | 105.41  | 111.94  | 110.57  | 119.54  |
| RUSSELL 3000             | 100.00                  | 102.20  | 100.47  | 98.29   | 102.01  | 102.73  | 106.94  | 105.92  | 106.85  |

**PROPOSAL 2**

**AMENDMENT AND RESTATEMENT OF THE 2005 STOCK PLAN**

The Dolby Laboratories, Inc. 2005 Stock Plan (the "Plan") was adopted by our Board of Directors in November 2004, approved by our stockholders in January 2005 and became effective on February 16, 2005, the day prior to the completion of our initial public offering.

On December 22, 2005, our Compensation Committee approved the amendment and restatement of the Plan, subject to stockholder approval, to permit certain future awards under the Plan to qualify as performance-based compensation under Section 162(m) of the Code and to permit the granting of performance cash bonus awards under the Plan.

The number of shares of the Company's Class A Common Stock issuable under the Plan is not being increased.

Our executive officers and directors have an interest in the amendment and restatement of the Plan because they are eligible for awards under the Plan.

**Summary of the Proposed Amendments**

Section 162(m) of the Code ( "Section 162(m)") limits the federal income tax deductibility of compensation paid to the Company's Chief Executive Officer and to each of its four other most highly compensated executive officers to \$1 million in any one year. However, the Company may deduct compensation in excess of that amount if it qualifies as performance-based compensation, as defined in Section 162(m). As amended and restated, the Plan is designed to qualify certain awards under Section 162(m) as performance-based compensation, so that the Company may receive a federal income tax deduction for performance-based awards to its executive officers even if an executive's compensation exceeds \$1 million in that year. In order for future awards under the Plan to qualify as performance-based compensation, the Company's stockholders must approve the changes to the Plan that specify the types of performance criteria that may be used as goals under the Plan and limit the number of securities and/or the dollar amount of performance bonus awards that may be granted to any individual in any fiscal year.

The Plan, as amended and restated, also authorizes the granting of cash bonus awards designed to be performance-based compensation under Section 162(m). Consequently, by approving the amended and restated Plan, Company stockholders will be approving the performance measures upon which specific performance goals applicable to certain awards may be based, limits on the numbers of shares or compensation that would be subject to certain awards, the ability for the Company to grant cash-based performance awards under the Plan and the other material terms of the awards described below.

The proposed changes to the Plan are described in further detail below.

**Description of the Amended and Restated 2005 Stock Plan**

The following description of the principal features of the amended and restated Plan is qualified in its entirety by reference to the text of the amended and restated Plan, which is attached as *Appendix B* to this Proxy Statement.

**Purpose**

The purpose of the Plan is to attract and retain the best available personnel for positions of substantial responsibility, to provide additional incentive to employees, directors and consultants, and to promote the success of the Company's business.

## Eligibility

Plan-eligible participants include employees, consultants and directors of the Company and its subsidiaries. As of December 13, 2005, approximately 834 employees (including two employee directors), three non-employee directors and three consultants were eligible to participate in the Plan.

## Administration of Plan

The Compensation Committee administers the Plan. The administrator has the power to determine the terms of the awards, including the individuals to whom awards will be made, the type of awards, the amount of the awards, the exercisability of the awards, the form of consideration, if any, payable upon exercise. Additionally, the administrator makes all other determinations necessary or advisable for the administration of the Plan, including interpreting the Plan and any award agreements under the Plan. In addition, both the Stock Plan Committee and our CEO may act as Plan administrator in limited circumstances, as they have the authority to grant equity-based awards to employees and consultants who are not executive officers or directors of the Company within guidelines for the size of grants to particular levels of employees or consultants established by the Company and approved by the Board of Directors. In the case of awards intended to qualify as performance-based compensation within the meaning of Section 162(m), the Compensation Committee, which consists of two or more outside directors within the meaning of Section 162(m), approves such grants and the performance goals for any performance period. In the case of awards granted to certain executive officers that require the achievement of specified performance goals, following the completion of the performance period, the Compensation Committee will certify, to the extent required by Section 162(m), in writing whether, and to what extent, the performance goals for the performance period have been achieved.

## Share Reserve

A total of 6,000,000 shares of our Class A Common Stock are authorized for issuance under the Plan. Any shares subject to an award with a per share price less than the fair market value of our Class A Common Stock on the date of grant are counted against the authorized share reserve as two shares for every one share subject to the award, and if returned to the Plan such shares are counted as two shares for every one share returned. Shares subject to awards that expire or are cancelled or forfeited will again become available for issuance under the Plan. Awards settled in cash or by shares withheld to satisfy the purchase price of an award or tax withholding obligations will not count against the authorized share reserve.

The Plan, prior to its amendment and restatement, did not limit the number of shares of the Company's Class A Common Stock that could be issued to any one individual pursuant to options, SARs, restricted stock or performance grants. As amended and restated, the Plan contains annual grant limits intended to satisfy Section 162(m). Specifically, the maximum number of shares which could be issued to any one individual in any fiscal year pursuant to options, SARS, restricted stock, or performance shares is limited to 2,000,000, and the maximum which could be issued to any one individual in any fiscal year pursuant to the grant of performance units or performance bonus awards is \$5,000,000. In addition, an individual may be granted options or SARs to purchase up to an additional 2,000,000 shares of Class A Common Stock in connection with his or her initial hiring by the Company.

The Compensation Committee will adjust the maximum number and type of securities that may be granted pursuant to the Plan, the limitations on annual grants to individuals or in connection with an individual's initial hiring, as well as the number and type of securities subject to outstanding awards, the option price, grant price or other price of shares subject to outstanding awards, any performance conditions relating to shares and any other conditions of outstanding awards, in the event of a merger, reorganization, consolidation, recapitalization, liquidation, stock dividend, spin-off, stock split, reverse stock split, share combination, share exchange, extraordinary dividend, or any change in the corporate structure affecting our Class A Common Stock.





## Awards

The Plan provides for the grant of incentive stock options, nonstatutory stock options, restricted stock, SARs, deferred stock units, performance units, performance shares and performance cash bonus awards. Set forth below is a general description of the types of awards that may be granted under the Plan. On December 15, 2005, the closing price of our Class A Common Stock on the NYSE was \$18.43 per share.

### *Stock Options*

The administrator determines the exercise price of options granted under the Plan, but with respect to nonstatutory stock options intended to qualify as performance-based compensation within the meaning of Section 162(m) and all incentive stock options, the exercise price must at least be equal to the fair market value of our Class A Common Stock on the date of grant. The term of an incentive stock option may not exceed ten years, except that with respect to any participant who owns 10% of the voting power of all classes of our outstanding stock, the term must not exceed five years and the exercise price must equal at least 110% of the fair market value on the grant date. The administrator determines the term of all other options.

Upon termination of a participant's service with us or with a subsidiary of us, he or she may exercise his or her option for the period of time stated in the option agreement. Generally, if termination is due to death or disability, the option will remain exercisable for 12 months. In all other cases, the option will generally remain exercisable for three months. However, an option may never be exercised later than the expiration of its term.

### *Stock Appreciation Rights*

SARs may be granted under the Plan. SARs allow the recipient to receive the appreciation in the fair market value of our Class A Common Stock between the exercise date and the date of grant. The administrator determines the terms of SARs, including when such rights become exercisable and whether to pay the increased appreciation in cash or with shares of our Class A Common Stock, or a combination thereof.

### *Restricted Stock*

Restricted stock may be granted under the Plan. Restricted stock awards are shares of our Class A Common Stock that vest in accordance with terms and conditions established by the administrator. The administrator will determine the number of shares of restricted stock granted to any employee. The administrator may impose whatever conditions to vesting it determines to be appropriate. For example, the administrator may set restrictions based on the achievement of specific performance goals. Shares of restricted stock that do not vest are subject to our right of repurchase or forfeiture.

### *Deferred Stock Units*

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The Plan permits the grant of deferred stock units, which may consist of restricted stock, performance shares or performance unit awards that are paid out in installments or on a deferred basis, as determined in the administrator's sole discretion and in accordance with rules and procedures established by the administrator. Deferred stock units may be settled in cash, shares of our Class A Common Stock or a combination of cash and our Class A Common Stock.

### *Performance-Based Compensation*

Performance units, performance shares and performance cash bonuses may be granted under the Plan. Performance units, performance shares and performance cash bonuses are awards that will result in a payment to a participant only if performance goals established by the administrator are achieved or the awards otherwise vest. As described below, the administrator will establish organizational or individual performance goals in its discretion within the parameters of the Plan, which, depending on the extent to which they are met, will determine the degree of granting, vesting and/or payout value of performance units, performance shares

and performance cash bonuses to be paid out to participants. Performance units will have an initial dollar value established by the administrator on or before the grant date. Performance shares will have an initial value equal to the fair market value of our Class A Common Stock on the grant date.

As originally adopted, the Plan did not provide for performance cash bonus awards, although the Company has historically granted performance cash bonus awards separately pursuant to our annual incentive plan. The addition of performance cash bonus awards to the Plan is intended to allow the Company to structure future cash bonus awards as performance-based compensation under Section 162(m). The Plan also did not provide specific measures for performance goals, but allowed the administrator to determine the performance goals applicable to an award using certain Company or individual performance measures. As amended and restated, the Plan provides specific measures from which the administrator may base performance goals. Specifically, performance goals to be used for awards shall be chosen from one or more of the following measures: (i) revenue, (ii) gross margin, (iii) operating margin, (iv) operating income, (v) pre-tax profit, (vi) earnings before interest, taxes and depreciation, (vii) net income, (viii) cash flow, (ix) expenses, (x) the market price of a share of our Class A Common Stock, (xi) earnings, (xii) return on stockholder equity, (xiii) return on capital, (xiv) product quality, (xv) economic value added, (xvi) number of customers, (xvii) market share, (xviii) return on investments, (xix) profit after taxes, (xx) customer satisfaction, (xxi) business divestitures and acquisitions, (xxii) supplier awards from significant customers, (xxiii) new product development, (xxiv) working capital, (xxv) individual objectives, (xxvi) time to market, (xxvii) return on net assets, and (xxviii) sales.

Prior to the beginning of any applicable performance period or such later date as permitted under Section 162(m), the Compensation Committee will establish one or more performance goals applicable to the awards of the executive officers covered by Section 162(m). The target levels with respect to these performance measures may be expressed on an absolute basis or relative to a standard specified by the Compensation Committee. The degree of attainment of these performance measures will, according to criteria established by the Compensation Committee, be computed before the effect of changes in accounting standards, restructuring charges and similar extraordinary items occurring after the establishment of the performance goals applicable to a performance award.

Following completion of the applicable performance period, the Compensation Committee will certify in writing, as to the executive officers covered by Section 162(m), the extent to which the applicable performance goals have been attained and the resulting value to be paid to each such executive officer. The Compensation Committee retains the discretion to eliminate or reduce, but not increase, the amount that would otherwise be payable to such executive officer on the basis of the performance goals attained. However, no such reduction may increase the amount paid to any other executive officer. Performance award payments may be made in lump sum or in installments. If any payment is to be made on a deferred basis, the Compensation Committee may provide for the payment of dividend equivalents or interest during the deferral period.

No performance award may be sold or transferred other than by will or the laws of descent and distribution prior to the end of the applicable performance period. The Company reserves the right to grant awards that do not qualify for the Section 162(m) performance-based exception.

#### *Outside Director Awards*

The Plan also provides for the automatic grant of nonstatutory stock options to our non-employee directors. Each non-employee director appointed to the Board, except for those inside directors who cease to be inside directors but remain non-employee directors, receive an initial option to purchase 20,000 shares. This initial option vests over three years at a rate of one-third upon each anniversary of the grant date, provided that the director continues to serve on the Board. In addition, on July 15, 2005 our non-employee directors received, and following each annual meeting of our stockholders beginning in 2006, those non-employee directors who have been directors for at least six months will receive, a subsequent option to purchase 10,000 shares. These subsequent options will vest over three years at a rate of one-third upon each anniversary of the grant date, provided that the director continues to serve on the Board. All options granted under the automatic grant provisions have a term of ten years and an exercise price equal to the fair market value of our Class A Common



Stock on the date of grant. The administrator may change the number of shares subject to the initial and subsequent options and the terms of such options, and may grant a different mix of equity awards of an equivalent value to such options as determined by our Board of Directors on the date of grant.

### **Effect of a Change in Control**

The Plan provides that in the event of a change in control of the Company the successor corporation will assume, substitute an equivalent award, or replace with a cash incentive program each outstanding award under the Plan. With respect to awards made to a non-employee director, such awards will become fully vested and exercisable immediately prior to the change in control. With respect to awards made to our employees and consultants, such awards will be subject to an accelerated vesting schedule equal to one year of additional vesting for each year of service the employee or consultant provided to us on the date, following a change in control, if such employee or consultant is terminated by us or a successor to us without cause or if such employee or consultant resigns for good reason, provided that the termination or resignation occurs within the 12 months following a change in control. If there is no assumption, substitution or replacement with a cash incentive program of outstanding awards, such awards will become fully vested and exercisable immediately prior to the change in control unless otherwise determined by the administrator, and the administrator will provide notice to the recipient that he or she has the right to exercise such outstanding awards for a period of 15 days from the date of the notice. The awards will terminate upon the expiration of the 15-day period.

### **Transferability**

Unless otherwise permitted by the administrator, the Plan generally does not allow for the transfer of awards, and, consequently, only the recipient of an award generally may exercise an award during his or her lifetime. The Company has granted non-statutory stock options under the Plan to its executive officers and directors that permit transfers for estate planning purposes.

### **Termination and Amendment**

The Plan will automatically terminate in November 2014, unless we terminate it sooner. In addition, the Compensation Committee has the authority to amend, suspend or terminate the Plan provided such action does not impair the rights of any participant. However, the Company intends to obtain stockholder approval with respect to any further amendments to the Plan to the extent required for awards under the Plan to continue to satisfy the requirements for performance-based compensation under Section 162(m), or as otherwise required by applicable law.

### **Summary of U.S. Federal Income Tax Consequences**

The following summary is intended only as a general guide to the U.S. federal income tax consequences of participation in the Plan and does not attempt to describe all possible federal or other tax consequences of such participation or tax consequences based on particular circumstances.

**Incentive Stock Options.** An optionee recognizes no taxable income for regular income tax purposes as a result of the grant or exercise of an incentive stock option qualifying under Section 422 of the Code. Optionees who neither dispose of their shares within two years following the date the option was granted nor within one year following the exercise of the option will normally recognize a capital gain or loss equal to the difference, if any, between the sale price and the purchase price of the shares. If an optionee satisfies such holding periods upon a sale of the shares, the Company will not be entitled to any deduction for federal income tax purposes. If an optionee disposes of shares within two years

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after the date of grant or within one year after the date of exercise (a disqualifying disposition ), the difference between the fair market value of the shares on the determination date (see discussion under Nonstatutory Stock Options below) and the option exercise price (not to exceed the gain realized on the sale if the disposition is a transaction with respect to which a loss, if sustained, would be recognized) will be taxed as ordinary income at the time of disposition. Any gain in excess of that amount will be a capital gain. If a loss is recognized, there will be no ordinary income, and such loss will be a

capital loss. Any ordinary income recognized by the optionee upon the disqualifying disposition of the shares generally should be deductible by the Company for federal income tax purposes, except to the extent such deduction is limited by applicable provisions of the Code.

The difference between the option exercise price and the fair market value of the shares on the determination date of an incentive stock option (see discussion under *Nonstatutory Stock Options* below) is treated as an adjustment in computing the optionee's alternative minimum taxable income and may be subject to an alternative minimum tax which is paid if such tax exceeds the regular tax for the year. Special rules may apply with respect to certain subsequent sales of the shares in a disqualifying disposition, certain basis adjustments for purposes of computing the alternative minimum taxable income on a subsequent sale of the shares and certain tax credits which may arise with respect to optionees subject to the alternative minimum tax.

***Nonstatutory Stock Options.*** Options not designated or qualifying as incentive stock options will be nonstatutory stock options having no special tax status. An optionee generally recognizes no taxable income as the result of the grant of such an option. Upon exercise of a nonstatutory stock option, the optionee normally recognizes ordinary income in the amount of the difference between the option exercise price and the fair market value of the shares on the determination date (as defined below). If the optionee is an employee, such ordinary income generally is subject to withholding of income and employment taxes. The *determination date* is the date on which the option is exercised unless the shares are subject to a substantial risk of forfeiture (as in the case where an optionee is permitted to exercise an unvested option and receive unvested shares which, until they vest, are subject to the Company's right to repurchase them at the original exercise price upon the optionee's termination of service) and are not transferable, in which case the determination date is the earlier of (i) the date on which the shares become transferable or (ii) the date on which the shares are no longer subject to a substantial risk of forfeiture. If the determination date is after the exercise date, the optionee may elect, pursuant to Section 83(b) of the Code, to have the exercise date be the determination date by filing an election with the Internal Revenue Service no later than 30 days after the date the option is exercised. Upon the sale of stock acquired by the exercise of a nonstatutory stock option, any gain or loss, based on the difference between the sale price and the fair market value on the determination date, will be taxed as capital gain or loss. No tax deduction is available to the Company with respect to the grant of a nonstatutory stock option or the sale of the stock acquired pursuant to such grant. The Company generally should be entitled to a deduction equal to the amount of ordinary income recognized by the optionee as a result of the exercise of a nonstatutory stock option, except to the extent such deduction is limited by applicable provisions of the Code.

***Stock Appreciation Rights.*** No taxable income is reportable when a SAR is granted to a participant. Upon exercise, the participant will recognize ordinary income in an amount equal to the amount of cash received and the fair market value of any shares of our Class A Common Stock received. Any additional gain or loss recognized upon any later disposition of the shares would be capital gain or loss.

***Restricted Stock Awards.*** A participant acquiring restricted stock generally will recognize ordinary income equal to the fair market value of the shares on the *determination date* (as defined above under *Nonstatutory Stock Options*). If the participant is an employee, such ordinary income generally is subject to withholding of income and employment taxes. If the determination date is after the date on which the participant acquires the shares, the participant may elect, pursuant to Section 83(b) of the Code, to have the date of acquisition be the determination date by filing an election with the Internal Revenue Service no later than 30 days after the date the shares are acquired. Upon the sale of shares acquired pursuant to a restricted stock award, any gain or loss, based on the difference between the sale price and the fair market value on the determination date, will be taxed as capital gain or loss. The Company generally should be entitled to a deduction equal to the amount of ordinary income recognized by the participant on the determination date, except to the extent such deduction is limited by applicable provisions of the Code.

***Performance Bonus, Performance Shares and Performance Unit Awards.*** A participant generally will recognize no income upon the grant of a performance share, performance bonus or performance unit award. Upon the settlement and/or payment of such awards, participants normally will recognize ordinary income in the

year of receipt in an amount equal to the cash received and the fair market value of any nonrestricted shares received. If the participant is an employee, such ordinary income generally is subject to withholding of income and employment taxes. If the participant receives shares of restricted stock, the participant generally will be taxed in the same manner as described above (see discussion under Restricted Stock ). Upon the sale of any shares received, any gain or loss, based on the difference between the sale price and the fair market value on the determination date (as defined above under Nonstatutory Stock Options ), will be taxed as capital gain or loss. The Company generally should be entitled to a deduction equal to the amount of ordinary income recognized by the participant on the determination date, except to the extent such deduction is limited by applicable provisions of the Code.

**Deferred Stock Unit Awards.** A participant generally will recognize no income upon the grant of a Deferred Stock Unit Award. Upon the settlement of such an award, the participant normally will recognize ordinary income in the year of settlement in an amount equal to the fair market value of any unrestricted shares of our Class A Common Stock received. Upon the sale of any shares received, any gain or loss, based on the difference between the sale price and the fair market value on the determination date, will be taxed as capital gain or loss. The Company generally should be entitled to a deduction equal to the amount of ordinary income recognized by the participant on the determination date, except to the extent such deduction is limited by applicable provisions of the Code.

### New Plan Benefits

The benefits and amounts that will be received by each of the Named Executive Officers, the executive officers as a group and all other employees under the Plan cannot be determined at this time because the administrator has full discretion to determine the number, type and value of awards under the Plan and the actual amounts will depend on who participates in the Plan, actual performance measured against the attainment of pre-established performance goals and the Compensation Committee's discretion to reduce such amounts. See Compensation of Directors for a description of director compensation under the Plan.

The following table sets forth the following persons or groups who received (i) options to purchase the following numbers of shares of our Class A Common Stock under the Plan in fiscal 2005 and (ii) bonuses under the Dolby annual incentive plan earned in fiscal 2005.

| Name   | Number of Securities Underlying Options Granted Pursuant to the Plan | Bonus Awards Earned in Fiscal 2005 Pursuant to the Dolby Annual Incentive Plan* |
|--|--|---|
| Bill Jasper  | 80,000   | \$ 383,078  |
| Janet Daly**   | 10,000   | \$ 133,123  |
| Marty Jaffe  | 60,000   | \$ 173,218  |
| Ed Schummer  | 50,000   | \$ 155,274  |
| David Watts  | 30,000   | \$ 151,144  |
| All current executive officers of the Company as a group                               | 355,000  | \$ 1,406,856  |
| All current directors who are not officers as a group                                  | 30,000   |   |
| All employees and consultants of the Company (excluding executive officers) as a group | 1,914,170  | Not yet determined.   |

\* Bonuses paid pursuant to the Dolby annual incentive plan, not pursuant to the Plan.

\*\* Effective October 24, 2005, Ms. Daly resigned as Chief Financial Officer and transitioned to a non-executive position.



We did not grant any options under the Plan in fiscal 2005 to any associates of our current directors, executive officers or nominees for director. No single person received five percent of the options granted under the Plan in fiscal 2005.

The Compensation Committee has also established a fiscal year 2006 cash-based performance bonus program under the Plan which is intended to comply with Section 162(m). The Compensation Committee has established, to the extent required by Section 162(m) of the Code, the specific performance measurements and bonus parameters applicable to certain executive officers under the Plan for fiscal 2006 and has made the award of such cash performance bonuses subject to stockholder approval of this amended and restated Plan.

Proposal 2 requires the affirmative **FOR** vote of a majority of the voting power of the shares present and voting at the Annual Meeting in person or by proxy. Under the rules of the NYSE, brokers are prohibited from giving proxies to vote on equity compensation plans unless the beneficial owner of such shares has given voting instructions on the matter. This means that if your broker is the record holder of your shares, you must give voting instructions to your broker with respect to Proposal 2 if you want your broker to vote your shares on the matter.

***The Board of Directors recommends a vote FOR the amendment and restatement of the Company's 2005 Stock Plan to permit certain future awards under the Plan to qualify as performance-based compensation under Section 162(m) and to permit the granting of performance cash bonus awards under the Plan.***

**PROPOSAL 3****RATIFICATION OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

The Audit Committee has appointed the firm of KPMG LLP as the Company's independent registered public accounting firm for the fiscal year ending September 29, 2006. Representatives of KPMG LLP are expected to be present at the Company's Annual Meeting. They will have an opportunity to make a statement, if they desire to do so, and will be available to respond to appropriate questions.

**Principal Accountant Fees and Services**

The following table sets forth the aggregate fees billed or expected to be billed by KPMG LLP for audit and other services rendered.

|                                   | <b>Fiscal Years Ended</b> |                     |
|-----------------------------------|---------------------------|---------------------|
|                                   | <b>2005</b>               | <b>2004</b>         |
| Audit Fees <sup>(1)</sup>         | \$ 875,355                | \$ 862,000          |
| Audit-Related Fees <sup>(2)</sup> | 990,179                   | 293,000             |
| Tax Fees <sup>(3)</sup>           |                           |                     |
| All Other Fees <sup>(4)</sup>     | 13,658                    |                     |
|                                   | <b>\$ 1,879,192</b>       | <b>\$ 1,155,000</b> |

- (1) Audit fees consist of fees incurred for professional services rendered for the audit of our annual consolidated financial statements, review of our quarterly consolidated financial statements and foreign statutory audits and services that are normally provided by KPMG LLP in connection with statutory and regulatory filings or engagements.
- (2) Audit-related fees consist of fees billed for assurance and related services that are reasonably related to the performance of the audit or review of our consolidated financial statements and are not reported under Audit Fees. In fiscal 2004, this consisted principally of documentation assistance procedures to meet the requirements of the Sarbanes-Oxley Act of 2002. In fiscal 2005, this consisted primarily of accounting advice and consultations related to our initial public offering, as well as documentation assistance procedures to meet the requirements of the Sarbanes-Oxley Act of 2002.
- (3) The Company generally does not engage KPMG LLP for tax services.
- (4) All other fees consist of fees billed in connection with audits of our licensees. In addition, the Company has prepaid \$76,342 for similar services, but KPMG LLP had not yet rendered such services in fiscal 2005.

The Audit Committee considered whether the provision of services other than audit services is compatible with maintaining KPMG LLP's independence.

**Pre-Approval Policies and Procedures**

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The Audit Committee has established a policy to pre-approve all audit and permissible non-audit services provided by the Company's independent registered public accounting firm.

All services and fees provided to the Company by KPMG LLP in fiscal 2005 were pre-approved by the Audit Committee.

### **Required Vote**

Ratification requires the affirmative vote of a majority of the voting power of the shares present and voting at the Annual Meeting in person or by proxy. Stockholder ratification of the selection of KPMG LLP as the Company's independent registered public accounting firm is not required by the Company's Bylaws or otherwise. However, the Board is submitting the selection of KPMG LLP to the stockholders for ratification as a

matter of corporate practice. If the stockholders fail to ratify the selection, the Audit Committee will reconsider whether or not to retain that firm. Even if the selection is ratified, the Audit Committee in its discretion may direct the appointment of a different independent registered public accounting firm at any time during the year if the Audit Committee determines that such a change would be in the best interests of the Company and its stockholders.

*The Board of Directors recommends a vote FOR ratification of KPMG LLP as the Company's independent registered public accounting firm.*

**SECTION 16(a) BENEFICIAL OWNERSHIP REPORTING COMPLIANCE**

Section 16(a) of the Exchange Act requires the Company's executive officers and directors and persons who beneficially own more than 10% of the Company's Class A Common Stock (collectively, "Reporting Persons") to file reports of beneficial ownership and changes in beneficial ownership with the SEC and the NYSE. Reporting Persons are required by SEC regulations to furnish the Company with copies of all Section 16(a) forms they file. Based solely on our review of such reports received or written representations from certain Reporting Persons, the Company believes that during the fiscal year ended September 30, 2005 all Reporting Persons complied with all applicable reporting requirements, except that Janet Daly was one business day late in reporting an option grant.

**STOCKHOLDER PROPOSALS FOR THE 2007 ANNUAL MEETING**

The deadline for submitting a stockholder proposal for inclusion in the Company's proxy statement and form of proxy for the Company's 2007 Annual Meeting of Stockholders pursuant to Rule 14a-8 of the Exchange Act is September 19, 2006.

Our Bylaws contain additional advance notice requirements, including requirements with respect to advance notice of stockholder proposals. Under our Bylaws, a stockholder proposal will be ineligible for presentation at the meeting unless the stockholder gives timely notice of the proposal in writing to the Secretary of the Company at the principal executive offices of the Company and otherwise complies with the provisions of the Company's Bylaws. To be timely, the Company's Bylaws provide that such stockholder's notice must be delivered to or mailed and received by the secretary of the Company at the principal executive offices of the Company not later than the close of business on the 90th day, nor earlier than the close of business on the 120th day, prior to the anniversary date of the immediately preceding annual meeting; provided, however, that in the event that no annual meeting was held in the previous year or the annual meeting is called for a date that is not within 30 days before or after such anniversary date, notice by the stockholder to be timely must be so received not later than the close of business on the 10th day following the day on which such notice of the date of the meeting was mailed or public disclosure of the date of the meeting was made, whichever occurs first.

**ANNUAL REPORT**

**The Company will furnish without charge, upon written request of any person who was a stockholder or beneficial owner of Common Stock at the close of business on January 9, 2006, a copy of the Company's Annual Report on Form 10-K, including the financial statements and the financial statement schedules. The written request should be sent to: Investor Relations Department, Dolby Laboratories, Inc., 100 Potrero Avenue, San Francisco, CA 94103-4813.**

Whether you intend to be present at the Annual Meeting or not, we urge you vote by using the internet or telephone, or signing and mailing the enclosed proxy promptly.

By order of the Board of Directors.

/s/ Bill Jasper  
Bill Jasper  
*President and Chief Executive Officer*

January 17, 2006

*Appendix A*

**Audit Committee Charter**

**DOLBY LABORATORIES, INC.**

**AUDIT COMMITTEE CHARTER**

(As adopted November 3, 2004)

**PURPOSE**

The primary functions of the Audit Committee are to assist the Board of Directors of Dolby Laboratories, Inc. in monitoring (1) the integrity of Dolby's financial statements, (2) Dolby's compliance with legal and regulatory requirements, (3) the independent auditors' qualifications and independence, (4) the performance of Dolby's internal audit function and independent auditors and (5) Dolby's system of internal controls regarding finance, accounting, legal compliance and ethics that management and the Board have established.

The Audit Committee shall also prepare the report required by the rules of the Securities and Exchange Commission to be included in Dolby's annual proxy statement.

**MEMBERSHIP REQUIREMENTS**

The Audit Committee shall consist of at least three members of the Board. The members of the Audit Committee shall meet the independence requirements of the New York Stock Exchange and the rules and regulations of the SEC.

Each member of the Audit Committee must be financially literate, as such qualification is interpreted by Dolby's Board in its business judgment. At least one member of the Audit Committee must have accounting or related financial management expertise, as Dolby's Board interprets such qualification in its business judgment. Audit Committee members shall not serve on the audit committee of more than three other publicly traded companies unless the Board determines in advance that the simultaneous service does not impair such Audit Committee member's ability to effectively serve on the Audit Committee and makes the related required disclosure in Dolby's annual proxy statement.

The members of the Audit Committee shall be appointed by the Board upon recommendation of the Nominating and Governance Committee. Audit Committee members may be replaced by the Board.

**AUTHORITY AND RESPONSIBILITIES**

The Audit Committee shall appoint and oversee the work of the independent auditors, approve the compensation of the independent auditors and review and, if necessary, discharge the independent auditors. In this regard, the independent auditors shall report directly to the Audit Committee, and the Audit Committee shall have the sole authority to approve the hiring and discharging of the independent auditors, all audit engagement fees and terms and, to the extent permissible, all non-audit engagements with the independent auditors.

The Audit Committee shall pre-approve (or, where permitted under the rules of the SEC, subsequently approve) engagements of the independent auditors to render audit or non-audit services and/or establish pre-approval policies and procedures for such engagements, provided that (A) such policies and procedures are detailed as to the particular services rendered, (B) the Audit Committee is informed of each such service and (C) such policies and procedures do not include delegation to management of the Audit Committee's responsibilities under the Securities Exchange Act of 1934.

The Audit Committee shall evaluate, at least annually, the independent auditors' qualifications, performance and independence, which evaluation shall include a review and evaluation of the lead

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partner of the independent auditors and consideration of whether there should be rotation of the lead audit partner or the auditing firm, and take appropriate action to oversee the independence of the independent auditors. In making its evaluation, the Audit Committee should take into account the opinions of management and Dolby's internal auditors and the report delivered by the independent auditors described in the following provision.

The Audit Committee shall, at least annually, obtain and review a report by the independent auditors describing: (A) the audit firm's internal quality-control procedures; (B) any material issues raised by the most recent internal quality-control review, or peer review, of the audit firm, or by any inquiry or investigation by governmental or professional authorities, within the preceding five years, respecting one or more independent audits carried out by the audit firm, and any steps taken to deal with any such issues; (C) all relationships between the independent auditors and Dolby to enable the Audit Committee to assess the auditors' independence; and (D) any other matters required to be included in a letter from the independent auditors pursuant to Independence Standards Board Standard No. 1.

The Audit Committee shall set clear hiring policies for employees or former employees of Dolby's independent auditors.

The Audit Committee shall review, in consultation with the independent auditors, the annual audit plan and scope of audit activities and monitor such plan's progress.

The Audit Committee shall discuss and, as appropriate, review with management and the independent auditors Dolby's annual and quarterly financial statements and annual and quarterly reports on Forms 10-K and 10-Q, including Dolby's disclosures under Management's Discussion and Analysis of Financial Condition and Results of Operations, discuss with the independent auditors any other matters required to be discussed by Statement on Auditing Standards 61 and recommend to the Board whether the audited financial statements and management's discussion and analysis should be included in Dolby's Form 10-K or 10-Q.

The Audit Committee shall discuss with management, the internal auditor and the independent auditors significant financial reporting issues and judgments made in connection with the preparation of Dolby's financial statements, including the review of (A) major issues regarding accounting principles and financial statement presentations, including any significant changes in Dolby's selection or application of accounting principles, and major issues as to the adequacy of Dolby's internal controls and any special audit steps adopted in light of material control deficiencies; (B) analyses prepared by management and/or the independent auditors setting forth significant financial reporting issues and judgments made in connection with the preparation of the financial statements, including analyses of the effects of alternative GAAP methods on the financial statements; (C) the effect of regulatory and accounting initiatives, as well as off-balance sheet structures, on Dolby's financial statements; and (D) the type and presentation of information to be included in earnings press releases, as well as any financial information and earnings guidance to be provided to analysts and rating agencies.

The Audit Committee shall receive, review and discuss quarterly reports from the independent auditors on (A) the major critical accounting policies and practices to be used; (B) significant alternative treatments of financial information within GAAP that have been discussed with management; (C) ramifications of the use of such alternative disclosures and treatments; (D) any treatments preferred by the independent auditors; and (E) other material written communications between the independent auditors and management, such as any management letter or schedule of unadjusted differences.

The Audit Committee shall review on a regular basis with the Company's independent auditors any problems or difficulties encountered by the independent auditors in the course of any audit work, including management's response with respect thereto, any restrictions on the scope of the independent auditors' activities or on access to requested information, and any significant disagreements with management. The Audit Committee shall resolve any disagreements between management and the independent auditors regarding financial reporting.

The Audit Committee shall discuss with management and the independent auditors any correspondence with regulators or governmental agencies and any published reports that raise material issues regarding Dolby's financial statements or accounting policies.

The Audit Committee shall discuss, in a general manner, earnings press releases and financial information and earnings guidance to be provided to analysts and rating agencies, including the proposed use of any pro forma or adjusted non-GAAP information.

The Audit Committee shall discuss guidelines and policies with respect to risk assessment and risk management.

The Audit Committee shall discuss with Dolby's general counsel legal matters that may have a material impact on the financial statements or Dolby's compliance procedures.

The Audit Committee shall review the adequacy and effectiveness of Dolby's internal control policies and procedures on a regular basis, including the responsibilities, budget and staffing of Dolby's audit function, as well as any special audit steps adopted in light of material control deficiencies, through inquiry and discussions with Dolby's independent auditors and management. In addition, the Audit Committee shall review the reports prepared by management, and attested to by Dolby's independent auditors, assessing the adequacy and effectiveness of Dolby's internal controls and procedures, prior to the inclusion of such reports in Dolby's periodic filings as required under SEC rules. The Audit Committee shall review disclosures regarding Dolby's internal controls that are required to be included in SEC reports.

The Audit Committee shall establish procedures for receiving, retaining and treating complaints received by Dolby regarding accounting, internal accounting controls or auditing matters and procedures for the confidential, anonymous submission by employees of concerns regarding questionable accounting or auditing matters.

The Audit Committee shall review, approve and monitor the portions of Dolby's code of ethics applicable to its senior financial officers.

The Audit Committee shall review on a regular basis management's assessment (and the basis therefore) of the adequacy and effectiveness of Dolby's system of disclosure controls and procedures, including by meeting periodically with the Company's management, independent auditors and legal counsel to review their assessment of such disclosure controls and procedures and to review, before its release, the disclosure regarding such system of disclosure controls and procedures required under SEC rules to be contained in the Company's periodic filings.

The Audit Committee shall act as Dolby's Qualified Legal Compliance Committee ( QLCC ) for the purposes of internal and external attorney reporting under SEC rules. The Audit Committee shall establish procedures for the confidential receipt, retention and consideration of any attorney report to the QLCC.

The Audit Committee shall make regular reports to the Board, which reports shall include any issues that arise with respect to the quality or integrity of Dolby's financial statements, Dolby's compliance with legal or regulatory requirements, the performance and independence of Dolby's independent auditors or the performance of the internal audit function.

At least annually, the Audit Committee shall evaluate its performance. The Audit Committee shall deliver to the Board a report setting forth the results of its evaluation, including any recommended changes to Dolby's, the Board's or the Audit Committee's own policies or procedures.

The Audit Committee shall review and reassess the adequacy and scope of this Charter annually and recommend any proposed changes to the Board for approval.

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The Audit Committee shall have the authority to engage independent counsel and other advisers, as it determines necessary to carry out its duties. Dolby shall provide for appropriate funding, as determined

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by the Audit Committee, for payment of (1) compensation to the independent auditors engaged for the purpose of preparing or issuing an audit report or performing other audit review or attest services for Dolby, (2) compensation to any advisers employed by the Audit Committee and (3) ordinary administrative expenses of the Audit Committee that are necessary or appropriate for carrying out its duties.

Periodically, the Audit Committee shall meet separately with Dolby's management, with the internal auditors and with the independent auditors.

The Audit Committee may form subcommittees for any purpose that the Audit Committee deems appropriate and may delegate to such subcommittees such power and authority as the Audit Committee deems appropriate. The Audit Committee shall not delegate to a subcommittee any power or authority required by law, regulation or listing standard to be exercised by the Audit Committee as a whole.

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assumptions to be reasonable under the circumstances. As future events and their effects cannot be determined with precision, actual values and results could differ from these estimates. Any changes in estimates resulting from future changes in the economic environment will be reflected in the financial statements in future periods.

c. Reclassifications

Certain amounts in the accompanying unaudited consolidated financial statements have been reclassified to conform to the 2016 presentation. These reclassifications had no impact to previously reported net loss, stockholders' equity or cash flows.

d. Accounts receivable

The Company sells produced oil, NGL and natural gas and purchased oil to various customers and participates with other parties in the development and operation of oil and natural gas properties. The Company's accounts receivable are generally unsecured. Accounts receivable for joint interest billings are recorded as amounts billed to customers less an allowance for doubtful accounts.

Joint interest operations amounts are considered past due after 30 days. The Company determines joint interest operations accounts receivable allowances based on management's assessment of the creditworthiness of the joint interest owners. Additionally, as the operator of the majority of its wells, the Company has the ability to realize some or all of the receivables through netting of anticipated future production revenues. The Company maintains an allowance for doubtful accounts for estimated losses inherent in its accounts receivable portfolio. In establishing the required allowance, management considers historical losses, current receivables aging and existing industry and economic data. The Company reviews its allowance for doubtful accounts quarterly. Past due amounts greater than 90 days and over a specified amount are reviewed individually for collectability. Account balances are charged off against the allowance after all means of collection have been exhausted and the potential for recovery is remote.

Accounts receivable consisted of the following components for the periods presented:

| (in thousands)                            | June 30, December |           |
|---|-------------------|-----------|
|   | 2016              | 31, 2015  |
| Oil, NGL and natural gas sales            | \$42,629          | \$ 25,582 |
| Joint operations, net <sup>(1)</sup>      | 18,425            | 21,375    |
| Sales of purchased oil and other products | 15,000            | 11,775    |
| Matured derivatives                       | 12,223            | 27,469    |
| Other                                     | 266               | 1,498     |
| Total                                     | \$88,543          | \$ 87,699 |

(1) Accounts receivable for joint operations are presented net of an allowance for doubtful accounts of \$0.2 million as of both June 30, 2016 and December 31, 2015.

e. Derivatives

The Company uses derivatives to reduce exposure to fluctuations in the prices of oil, NGL and natural gas. By removing a significant portion of the price volatility associated with future production, the Company expects to mitigate, but not eliminate, the potential effects of variability in cash flows from operations due to fluctuations in commodity prices. These transactions are in the form of puts, swaps, collars and, in prior periods, basis swaps. Derivatives are recorded at fair value and are presented on a net basis on the unaudited consolidated balance sheets as assets or liabilities. The Company nets the fair value of derivatives by counterparty where the right of offset exists. The Company determines the fair value of its derivatives by utilizing pricing models for substantially similar instruments. Inputs to the pricing models include publicly available prices and forward price curves generated from a compilation of data gathered from third parties. See Note 9 for discussion regarding the fair value of the Company's derivatives.

The Company's derivatives were not designated as hedges for accounting purposes for any of the periods presented. Accordingly, the changes in fair value are recognized in the unaudited consolidated statements of operations in the period of change. Gains and losses on derivatives are included in cash flows from operating activities. See Notes 8 and 9 for discussion regarding the Company's derivatives.

Laredo Petroleum, Inc.

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f. Property and equipment

The following table sets forth the Company's property and equipment as of the periods presented:

| (in thousands)                                 | June 30,<br>2016 | December<br>31, 2015 |
|--|------------------|----------------------|
| Evaluated oil and natural gas properties       | \$5,309,151      | \$5,103,635          |
| Less accumulated depletion and impairment      | (4,448,482 )     | (4,218,942 )         |
| Evaluated oil and natural gas properties, net  | 860,669          | 884,693              |
| Unevaluated properties not being depleted      | 114,507          | 140,299              |
| Midstream service assets                       | 148,227          | 147,811              |
| Less accumulated depreciation                  | (20,175 )        | (16,086 )            |
| Midstream service assets, net                  | 128,052          | 131,725              |
| Depreciable other fixed assets                 | 46,255           | 46,799               |
| Less accumulated depreciation and amortization | (20,218 )        | (18,169 )            |
| Depreciable other fixed assets, net            | 26,037           | 28,630               |
| Land   | 14,914           | 14,908               |

Total property and equipment, net \$1,144,179 \$1,200,255

For the three months ended June 30, 2016 and 2015, depletion expense was \$7.06 per barrel of oil equivalent ("BOE") sold and \$16.19 per BOE sold, respectively. For the six months ended June 30, 2016 and 2015, depletion expense was \$8.01 per BOE sold and \$16.13 per BOE sold, respectively.

The Company uses the full cost method of accounting for its oil and natural gas properties. Under this method, all acquisition, exploration and development costs, including certain related employee costs, incurred for the purpose of finding oil, NGL and natural gas are capitalized and depleted on a composite unit of production method based on proved oil, NGL and natural gas reserves. Such amounts include the cost of drilling and equipping productive wells, dry hole costs, lease acquisition costs, delay rentals and other costs related to such activities. Costs, including related employee costs, associated with production and general corporate activities are expensed in the period incurred. Sales of oil and natural gas properties, whether or not being depleted currently, are accounted for as adjustments of capitalized costs, with no gain or loss recognized, unless such adjustments would significantly alter the relationship between capitalized costs and proved reserves of oil, NGL and natural gas.

The Company excludes the costs directly associated with acquisition and evaluation of unevaluated properties from the depletion calculation until it is determined whether or not proved reserves can be assigned to the properties. The Company capitalizes a portion of its interest costs on its unevaluated properties. Capitalized interest becomes a part of the cost of the unevaluated properties and is subject to depletion when proved reserves can be assigned to the associated properties. All items classified as unevaluated property are assessed on a quarterly basis for possible impairment or reduction in value. The assessment includes consideration of the following factors, among others: intent to drill, remaining lease term, geological and geophysical evaluations, drilling results and activity, the assignment of evaluated reserves and the economic viability of development if proved reserves are assigned. During any period in which these factors indicate an impairment, the cumulative drilling costs incurred to date for such property and all or a portion of the associated leasehold costs are transferred to the full cost pool and are then subject to depletion. The full cost ceiling is based principally on the estimated future net revenues from proved oil and natural gas properties discounted at 10%. Per the SEC guidelines, companies are required to use the unweighted arithmetic average first-day-of-the-month price for each month within the 12-month period prior to the end of the reporting period before differentials ("Benchmark Prices"). The Benchmark Prices are then adjusted for quality, transportation

fees, geographical differentials, marketing bonuses or deductions and other factors affecting the price received at the wellhead ("Realized Prices"). The Realized Prices are utilized to calculate the discounted future net revenues in the full cost ceiling calculation.

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In the event the unamortized cost of evaluated oil and natural gas properties being depleted exceeds the full cost ceiling, as defined by the SEC, the excess is charged to expense in the period such excess occurs. Once incurred, a write-down of oil and natural gas properties is not reversible.

The following table presents the Benchmark Prices, Realized Prices and the corresponding non-cash full cost ceiling impairments recorded as of the periods presented:

|  | For the quarters ended |                   |                      |                       |                  |
|--|------------------------|-------------------|----------------------|-----------------------|------------------|
|  | June<br>30,<br>2016    | March<br>31, 2016 | December<br>31, 2015 | September<br>30, 2015 | June 30,<br>2015 |
| <b>Benchmark Prices</b>                              |                        |                   |                      |                       |                  |
| Oil (\$/Bbl)   | \$39.63                | \$42.77           | \$46.79              | \$55.73               | \$68.17          |
| NGL (\$/Bbl)   | \$17.08                | \$17.51           | \$18.75              | \$21.87               | \$26.73          |
| Natural gas (\$/MMBtu)                               | \$2.17                 | \$2.31            | \$2.47               | \$2.89                | \$3.22           |
| <b>Realized Prices</b>                               |                        |                   |                      |                       |                  |
| Oil (\$/Bbl)   | \$37.96                | \$41.33           | \$45.58              | \$54.28               | \$66.68          |
| NGL (\$/Bbl)   | \$10.80                | \$11.25           | \$12.50              | \$15.25               | \$19.56          |
| Natural gas (\$/Mcf)                                 | \$1.64                 | \$1.75            | \$1.89               | \$2.30                | \$2.62           |
| Non-cash full cost ceiling impairment (in thousands) | \$—                    | \$161,064         | \$975,011            | \$906,420             | \$488,046        |

Full cost ceiling impairment expense is included in the "Impairment expense" line item in the unaudited consolidated statements of operations and in the financial information provided for the Company's exploration and production segment presented in Note 16.

g. Long-lived assets and inventory

Impairment losses are recorded on property and equipment used in operations and other long-lived assets when indicators of impairment are present and the undiscounted cash flows estimated to be generated by those assets are less than the assets' carrying amount. Impairment is measured based on the excess of the carrying amount over the fair value of the asset.

Materials and supplies inventory used in developing oil and natural gas properties and midstream service assets are carried at the lower of cost or market ("LCM") with cost determined using the weighted-average cost method and are included in "Other current assets" and "Other assets, net" on the unaudited consolidated balance sheets. The market price for materials and supplies is determined utilizing a replacement cost approach (Level 2).

Beginning at March 31, 2016, frac pit water inventory used in developing oil and natural gas properties is carried at LCM with cost determined using the weighted-average cost method and is included in "Other current assets" on the unaudited consolidated balance sheets. The market price for frac pit water inventory is determined utilizing a replacement cost approach.

The minimum volume of product in a pipeline system that enables the system to operate is known as line-fill and is generally not available to be withdrawn from the pipeline system until the expiration of the transportation contract. The Company owns oil line-fill in third-party pipelines, which is accounted for at LCM with cost determined using the weighted-average cost method and is included in "Other assets, net" on the unaudited consolidated balance sheets. The LCM adjustment is determined utilizing a quoted market price adjusted for regional price differentials (Level 2).



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The following table presents inventory impairments recorded as of the periods presented:

|                                       | Three<br>months<br>ended June<br>30, |         | Six months<br>ended June<br>30, |         |
|---------------------------------------|--------------------------------------|---------|---------------------------------|---------|
| (in thousands)                        | 2016                                 | 2015    | 2016                            | 2015    |
| Inventory impairments:                |                                      |         |                                 |         |
| Materials and supplies <sup>(1)</sup> | \$963                                | \$1,553 | \$963                           | \$2,320 |
| Line-fill <sup>(2)</sup>              | —                                    | —       | —                               | 111     |
| Total inventory impairments           | \$963                                | \$1,553 | \$963                           | \$2,431 |

(1) Included in "Impairment expense" in the unaudited consolidated statements of operations and in "Impairment expense" for the Company's exploration and production segment presented in Note 16.

(2) Included in "Impairment expense" in the unaudited consolidated statements of operations and in "Impairment expense" for the Company's midstream and marketing segment presented in Note 16.

h. Debt issuance costs

Debt issuance fees, which are recorded at cost, net of amortization, are amortized over the life of the respective debt agreements utilizing the effective interest and straight-line methods. The Company capitalized \$6.8 million of debt issuance costs during the six months ended June 30, 2015 mainly as a result of the issuance of the March 2023 Notes (as defined below). No debt issuance costs were capitalized in the six months ended June 30, 2016. The Company had total debt issuance costs of \$20.9 million and \$23.9 million, net of accumulated amortization of \$19.2 million and \$17.0 million, as of June 30, 2016 and December 31, 2015, respectively.

The Company wrote-off approximately \$0.8 million of debt issuance costs during the six months ended June 30, 2016 as a result of changes in the borrowing base and aggregate elected commitment of the Senior Secured Credit Facility, which are included in the unaudited consolidated statements of operations in the "Write-off of debt issuance costs" line item. During the six months ended June 30, 2015, the Company wrote-off approximately \$6.6 million of debt issuance costs as a result of the early redemption of the January 2019 Notes (as defined below), which are included in the unaudited consolidated statements of operations in the "Loss on early redemption of debt" line item. Unamortized debt issuance costs related to the Company's senior unsecured notes are presented in "Long-term debt, net" on the Company's unaudited consolidated balance sheets. Unamortized debt issuance costs related to the Senior Secured Credit Facility are presented in "Other assets, net" on the Company's unaudited consolidated balance sheets. See Note 5.g for additional discussion of debt issuance costs.

Future amortization expense of debt issuance costs as of the period presented is as follows:

| (in thousands) | June 30,<br>2016 |
|----------------|------------------|
| Remaining 2016 | \$2,092          |
| 2017           | 4,238            |
| 2018           | 4,068            |
| 2019           | 2,915            |
| 2020           | 3,005            |
| Thereafter     | 4,585            |
| Total          | \$20,903         |

i. Other current assets and liabilities

Other current assets consist of the following components for the periods presented:

| (in thousands)           | June 30, December<br>2016 31, 2015 |          |
|--------------------------|------------------------------------|----------|
| Inventory <sup>(1)</sup> | \$6,986                            | \$ 6,974 |

|                            |          |           |
|----------------------------|----------|-----------|
| Prepaid expenses and other | 7,459    | 7,600     |
| Total other current assets | \$14,445 | \$ 14,574 |

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(1) See Note 2.g for discussion of inventory held by the Company.

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Laredo Petroleum, Inc.  
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Other current liabilities consist of the following components for the periods presented:

| (in thousands)  | June 30, December |           |
|---|-------------------|-----------|
|   | 2016              | 31, 2015  |
| Accrued interest payable  | \$24,161          | \$24,208  |
| Costs of purchased oil payable  | 15,629            | 12,189    |
| Lease operating expense payable                                       | 11,570            | 13,205    |
| Accrued compensation and benefits                                     | 8,720             | 14,342    |
| Capital contribution payable to equity method investee <sup>(1)</sup> | —                 | 27,583    |
| Other accrued liabilities   | 12,440            | 14,695    |
| Total other current liabilities                                       | \$72,520          | \$106,222 |

(1) See Notes 14 and 15 for additional discussion regarding our equity method investee.

j. Asset retirement obligations

Asset retirement obligations associated with the retirement of tangible long-lived assets are recognized as a liability in the period in which they are incurred and become determinable. The associated asset retirement costs are part of the carrying amount of the long-lived asset. Subsequently, the asset retirement cost included in the carrying amount of the related long-lived asset is charged to expense through depletion, or for midstream service asset retirement cost through depreciation, of the associated asset. Changes in the liability due to the passage of time are recognized as an increase in the carrying amount of the liability and as corresponding accretion expense.

The fair value of additions to the asset retirement obligation liability is measured using valuation techniques consistent with the income approach, which converts future cash flows into a single discounted amount. Significant inputs to the valuation include: (i) estimated plug and abandonment cost per well based on Company experience, (ii) estimated remaining life per well, (iii) estimated removal and/or remediation costs for midstream service assets, (iv) estimated remaining life of midstream service assets, (v) future inflation factors and (vi) the Company's average credit adjusted risk-free rate. Inherent in the fair value calculation of asset retirement obligations are numerous assumptions and judgments including, in addition to those noted above, the ultimate settlement of these amounts, the ultimate timing of such settlement and changes in legal, regulatory, environmental and political environments. To the extent future revisions to these assumptions impact the fair value of the existing asset retirement obligation liability, a corresponding adjustment will be made to the asset balance.

The Company is obligated by contractual and regulatory requirements to remove certain pipeline assets and perform other remediation of the sites where such pipeline assets are located upon the retirement of those assets. However, the fair value of the asset retirement obligation cannot currently be reasonably estimated because the settlement dates are indeterminate. The Company will record an asset retirement obligation for pipeline assets in the periods in which settlement dates become reasonably determinable.

The following reconciles the Company's asset retirement obligation liability for the periods presented:

| (in thousands)  | Six      | Year     |
|---|----------|----------|
|   | months   | ended    |
|   | ended    | December |
|   | June 30, | 31, 2015 |
|   | 2016     |          |
| Liability at beginning of period  | \$46,306 | \$32,198 |
| Liabilities added due to acquisitions, drilling, midstream service asset construction and other | 253      | 2,236    |
| Accretion expense   | 1,704    | 2,423    |
| Liabilities settled upon plugging and abandonment   | (526)    | (146)    |
| Liabilities removed due to sale of property   | —        | (2,005)  |
| Revision of estimates <sup>(1)</sup>  | —        | 11,600   |
| Liability at end of period  | \$47,737 | \$46,306 |

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(1) The revision of estimates that occurred during the year ended December 31, 2015 is mainly related to a change in the estimated remaining life per well due to the decline in commodity prices.

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k. Fair value measurements

The carrying amounts reported in the unaudited consolidated balance sheets for cash and cash equivalents, accounts receivable, accounts payable, undistributed revenue and royalties, accrued capital expenditures and other accrued assets and liabilities approximate their fair values. See Note 5.f for fair value disclosures related to the Company's debt obligations. The Company carries its derivatives at fair value. See Note 9 for details regarding the fair value of the Company's derivatives.

l. Treasury stock

Laredo's employees may elect to have the Company withhold shares of stock to satisfy their tax withholding obligations that arise upon the lapse of restrictions on their stock awards. Such treasury stock is recorded at cost and retired upon acquisition.

m. Compensation awards

Stock-based compensation expense, net of amounts capitalized, is included in "General and administrative" in the unaudited consolidated statements of operations over the awards' vesting periods and is based on the awards' grant date fair value. The Company utilizes the closing stock price on the grant date, less an expected forfeiture rate, to determine the fair value of service vesting restricted stock awards and a Black-Scholes pricing model to determine the fair values of service vesting restricted stock option awards. The Company utilizes a Monte Carlo simulation prepared by an independent third party to determine the fair values of the performance share awards and, in prior periods, the performance unit awards. The Company capitalizes a portion of stock-based compensation for employees who are directly involved in the acquisition, exploration and development of its oil and gas properties into the full cost pool. Capitalized stock-based compensation is included as an addition to "Oil and natural gas properties" in the unaudited consolidated balance sheets. See Note 6 for further discussion regarding the restricted stock awards, restricted stock option awards, performance share awards and performance unit awards.

n. Environmental

The Company is subject to extensive federal, state and local environmental laws and regulations. These laws, among other things, regulate the discharge of materials into the environment and may require the Company to remove or mitigate the environmental effects of the disposal or release of petroleum or chemical substances at various sites. Environmental expenditures are expensed in the period incurred. Liabilities for expenditures of a non-capital nature are recorded when environmental assessment or remediation is probable and the costs can be reasonably estimated. Such liabilities are generally undiscounted unless the timing of cash payments is fixed and readily determinable. Management believes no materially significant liabilities of this nature existed as of June 30, 2016 or December 31, 2015.

o. Non-cash investing and supplemental cash flow information

The following presents the non-cash investing and supplemental cash flow information for the periods presented:

| (in thousands)  | Six months ended |            |
|---|------------------|------------|
|   | June 30,<br>2016 | 2015       |
| Non-cash investing information:   |                  |            |
| Change in accrued capital expenditures  | \$(22,012)       | \$(53,209) |
| Change in accrued capital contribution to equity method investee <sup>(1)</sup> | \$(27,583)       | \$27,917   |
| Capitalized asset retirement cost   | \$253            | \$1,402    |
| Supplemental cash flow information:   |                  |            |
| Capitalized interest  | \$115            | \$178      |

(1) See Notes 14 and 15 for additional discussion regarding our equity method investee.

Note 3—Equity offerings

On May 16, 2016, the Company completed the sale of 10,925,000 shares of Laredo's common stock (the "May 2016 Equity Offering") for net proceeds of \$119.3 million, after underwriting discounts, commissions and offering

expenses. See Note 19.e for discussion regarding the completion of an equity offering subsequent to June 30, 2016. On March 5, 2015, the Company completed the sale of 69,000,000 shares of Laredo's common stock (the "March 2015 Equity Offering") for net proceeds of \$754.2 million, after underwriting discounts, commissions and offering expenses. Entities

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affiliated with Warburg Pincus LLC ("Warburg Pincus") purchased 29,800,000 shares in the March 2015 Equity Offering, following which Warburg Pincus owned 41.0% of Laredo's common stock.

Note 4—Divestiture

a. 2015 Divestiture of non-strategic assets

On September 15, 2015, the Company completed the sale of non-strategic and primarily non-operated properties and associated production totaling 6,060 net acres and 123 producing properties in the Midland Basin to a third-party buyer for a purchase price of \$65.5 million. After transaction costs reflecting an economic effective date of July 1, 2015, the net proceeds were \$64.8 million, net of working capital adjustments and post-closing adjustments. The purchase price, excluding post-closing adjustments, was allocated to oil and natural gas properties pursuant to the rules governing full cost accounting.

Effective at closing, the operations and cash flows of these properties were eliminated from the ongoing operations of the Company, and the Company has no continuing involvement in the properties. This divestiture does not represent a strategic shift and will not have a major effect on the Company's operations or financial results.

The following table presents revenues and expenses of the oil and natural gas properties sold included in the accompanying unaudited consolidated statements of operations for the periods presented:

| (in thousands)                 | Three<br>months<br>ended<br>June<br>30,<br>2015 | Six<br>months<br>ended<br>June<br>30,<br>2015 |
|--------------------------------|---|---|
| Oil, NGL and natural gas sales | \$ 1,970  | \$ 4,048                                      |
| Expenses <sup>(1)</sup>        | 2,098   | 4,710   |

(1) Expenses include (i) lease operating expense, (ii) production and ad valorem tax expense, (iii) accretion expense and (iv) depletion expense.

Note 5—Debt

a. March 2023 Notes

On March 18, 2015, the Company completed an offering of \$350.0 million in aggregate principal amount of 6 1/4% senior unsecured notes due 2023 (the "March 2023 Notes"). The March 2023 Notes will mature on March 15, 2023 and bear an interest rate of 6 1/4% per annum, payable semi-annually, in cash in arrears on March 15 and September 15 of each year, commencing September 15, 2015. The March 2023 Notes are fully and unconditionally guaranteed on a senior unsecured basis by LMS, GCM and certain of the Company's future restricted subsidiaries, subject to certain automatic customary releases, including the sale, disposition or transfer of all of the capital stock or of all or substantially all of the assets of a subsidiary guarantor to one or more persons that are not the Company or a restricted subsidiary, exercise of legal defeasance or covenant defeasance options or satisfaction and discharge of the applicable indenture, designation of a subsidiary guarantor as a non-guarantor restricted subsidiary or as an unrestricted subsidiary in accordance with the applicable indenture, release from guarantee under the Senior Secured Credit Facility, or liquidation or dissolution (collectively, the "Releases").

b. January 2022 Notes

On January 23, 2014, the Company completed an offering of \$450.0 million in aggregate principal amount of 5 5/8% senior unsecured notes due 2022 (the "January 2022 Notes"). The January 2022 Notes will mature on January 15, 2022 and bear an interest rate of 5 5/8% per annum, payable semi-annually, in cash in arrears on January 15 and July 15 of each year, commencing July 15, 2014. The January 2022 Notes are fully and unconditionally guaranteed on a senior unsecured basis by LMS, GCM and certain of the Company's future restricted subsidiaries, subject to certain Releases.

c. May 2022 Notes

On April 27, 2012, the Company completed an offering of \$500.0 million in aggregate principal amount of 7 3/8% senior unsecured notes due 2022 (the "May 2022 Notes"). The May 2022 Notes will mature on May 1, 2022 and bear an interest rate of 7 3/8% per annum, payable semi-annually, in cash in arrears on May 1 and November 1 of each year, commencing November 1, 2012. The May 2022 Notes are fully and unconditionally guaranteed on a senior unsecured basis by LMS, GCM and certain of the Company's future restricted subsidiaries, subject to certain Releases.

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Laredo Petroleum, Inc.

Condensed notes to the consolidated financial statements

(Unaudited)

d. January 2019 Notes

On January 20, 2011, the Company completed an offering of \$350.0 million 9 1/2% senior unsecured notes due 2019 (the "January Notes") and on October 19, 2011, the Company completed an offering of an additional \$200.0 million 9 1/2% senior unsecured notes due 2019 (the "October Notes" and together with the January Notes, the "January 2019 Notes"). The January 2019 Notes were due to mature on February 15, 2019 and bore an interest rate of 9 1/2% per annum, payable semi-annually, in cash in arrears on February 15 and August 15 of each year. The January 2019 Notes were fully and unconditionally guaranteed on a senior unsecured basis by LMS, GCM and certain of the Company's future restricted subsidiaries, subject to certain Releases.

On April 6, 2015 (the "Redemption Date"), utilizing a portion of the proceeds from the March 2015 Equity Offering and the March 2023 Notes offering, the entire \$550.0 million outstanding principal amount of the January 2019 Notes was redeemed at a redemption price of 104.750% of the principal amount of the January 2019 Notes, plus accrued and unpaid interest up to the Redemption Date. The Company recognized a loss on extinguishment of \$31.5 million related to the difference between the redemption price and the net carrying amount of the extinguished January 2019 Notes.

e. Senior Secured Credit Facility

As of June 30, 2016, the Fourth Amended and Restated Credit Agreement (as amended, the "Senior Secured Credit Facility"), which matures on November 4, 2018, had a maximum credit amount of \$2.0 billion, a borrowing base and an aggregate elected commitment of \$815.0 million with \$110.3 million outstanding and was subject to an interest rate of 2.00%. It contains both financial and non-financial covenants, all of which the Company was in compliance with as of June 30, 2016. Laredo is required to pay an annual commitment fee on the unused portion of the financial institutions' commitment of 0.375% to 0.5%, based on the ratio of outstanding revolving credit to the total commitment under the Senior Secured Credit Facility. Additionally, the Senior Secured Credit Facility provides for the issuance of letters of credit, limited to the lesser of total capacity or \$20.0 million. No letters of credit were outstanding as of June 30, 2016 or 2015.

See Note 19.a for discussion of additional borrowings and payments on the Senior Secured Credit Facility subsequent to June 30, 2016.

f. Fair value of debt

The Company has not elected to account for its debt instruments at fair value. The following table presents the carrying amount and fair values of the Company's debt for the periods presented:

| (in thousands)                 | June 30, 2016  |             | December 31, 2015 |             |
|--------------------------------|----------------|-------------|-------------------|-------------|
|                                | Long-term debt | Fair value  | Long-term debt    | Fair value  |
| January 2022 Notes             | \$450,000      | \$426,564   | \$450,000         | \$388,301   |
| May 2022 Notes                 | 500,000        | 501,250     | 500,000           | 460,000     |
| March 2023 Notes               | 350,000        | 349,965     | 350,000           | 301,000     |
| Senior Secured Credit Facility | 110,318        | 110,261     | 135,000           | 134,993     |
| Total value of debt            | \$1,410,318    | \$1,388,040 | \$1,435,000       | \$1,284,294 |

The fair values of the debt outstanding on the January 2022 Notes, May 2022 Notes and the March 2023 Notes were determined using the June 30, 2016 and December 31, 2015 quoted market price (Level 1) for each respective instrument. The fair values of the outstanding debt on the Senior Secured Credit Facility as of June 30, 2016 and December 31, 2015 were estimated utilizing pricing models for similar instruments (Level 2). See Note 9 for information about fair value hierarchy levels.

Laredo Petroleum, Inc.

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g. Debt issuance costs

The following table summarizes the net presentation of the Company's long-term debt and debt issuance cost on the unaudited consolidated balance sheets for the periods presented:

|                    | June 30, 2016  |                          | December 31, 2015   |                |                          |                     |
|--------------------|----------------|--------------------------|---------------------|----------------|--------------------------|---------------------|
| (in thousands)     | Long-term debt | Debt issuance costs, net | Long-term debt, net | Long-term debt | Debt issuance costs, net | Long-term debt, net |
| January 2022 Notes | \$450,000      | \$(5,451)                | \$444,549           | \$450,000      | \$(5,939)                | \$444,061           |
| May 2022 Notes     | 500,000        | (6,624 )                 | 493,376             | 500,000        | (7,066 )                 | 492,934             |
| March 2023 Notes   | 350,000        | (5,366 )                 | 344,634             |                |                          |                     |