UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

Form 10-Q

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

For the Quarterly Period Ended June 30, 2010

Commission File Number 000-50335

Digital Entertainment

DTS, Inc.

(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	**77-0467655** (I.R.S. Employer Identification No.)
5220 Las Virgenes Road **Calabasas, California 91302** (Address of principal executive offices and zip code)	**(818) 436-1000** (Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ☐ No ☐

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

Large accelerated filer ☐ Accelerated filer ☒ Non-accelerated filer ☐ (Do not check if a smaller reporting company) Smaller reporting company ☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☒

As of July 30, 2010 a total of 17,135,648 shares of the Registrant's Common Stock, $0.0001 par value, were outstanding.

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

DTS, INC.

CONSOLIDATED BALANCE SHEETS

	As of June 30, 2010	As of December 31, 2009
	(Unaudited) (Amounts in thousands, except per share amounts)	
ASSETS		
Current assets:		
Cash and cash equivalents	$ 30,415	$ 42,222
Short-term investments	46,145	33,129
Accounts receivable, net of allowance for doubtful accounts of $225 and $229 at June 30, 2010 and December 31, 2009, respectively	5,226	5,731
Deferred income taxes	4,970	4,945
Prepaid expenses and other current assets	2,415	1,617
Income taxes receivable, net	2,687	2,613
Total current assets	91,858	90,257
Property and equipment, net	34,310	33,885
Intangible assets, net	6,965	6,565
Goodwill	1,257	1,257
Deferred income taxes	13,409	13,152
Long-term investments	1,587	8,515
Other assets	775	587
Total assets	$150,161	$154,218
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 710	$ 826
Accrued expenses	6,483	5,663
Deferred revenue	2,929	43
Total current liabilities	10,122	6,532
Other long-term liabilities	6,676	5,862
Commitments and contingencies (Note 5)		
Stockholders' equity:		
Preferred stock—$0.0001 par value, 5,000 shares authorized at June 30, 2010 and December 31, 2009; no shares issued and outstanding	—	—
Common stock—$0.0001 par value, 70,000 shares authorized at June 30, 2010 and December 31, 2009; 19,894 and 19,652 shares issued at June 30, 2010 and December 31, 2009, respectively; 17,088 and 17,522 shares outstanding at June 30, 2010 and December 31, 2009, respectively	2	2
Additional paid-in capital	169,363	161,710
Treasury stock, at cost—2,806 and 2,130 shares at June 30, 2010 and December 31, 2009, respectively	(68,091)	(45,498)
Accumulated other comprehensive income	362	362
Retained earnings	31,727	25,248
Total stockholders' equity	133,363	141,824
Total liabilities and stockholders' equity	$150,161	$154,218

See accompanying notes to consolidated financial statements.

DTS, INC.

CONSOLIDATED STATEMENTS OF INCOME

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2010	2009	2010	2009
	(Unaudited) (Amounts in thousands, except per share amounts)			
Revenue	$17,460	$24,165	$39,196	$41,427
Cost of revenue	460	449	910	894
Gross profit	17,000	23,716	38,286	40,533
Operating expenses:				
Selling, general and administrative	11,727	16,067	24,126	28,855
Research and development	2,842	2,380	5,315	4,563
Total operating expenses	14,569	18,447	29,441	33,418
Income from operations	2,431	5,269	8,845	7,115
Interest and other income, net	139	718	351	862
Income from continuing operations before income taxes	2,570	5,987	9,196	7,977
Provision for income taxes	1,014	2,361	3,720	4,161
Income from continuing operations	1,556	3,626	5,476	3,816
Income from discontinued operations, net of tax	1,173	4	1,003	1
Net income	$ 2,729	$ 3,630	$ 6,479	$ 3,817
Net income per common share:				
Basic:				
Continuing operations	$ 0.09	$ 0.21	$ 0.32	$ 0.22
Discontinued operations	0.07	—	0.06	—
Net income	$ 0.16	$ 0.21	$ 0.38	$ 0.22
Diluted:				
Continuing operations	$ 0.09	$ 0.21	$ 0.31	$ 0.22
Discontinued operations	0.06	—	0.05	—
Net income	$ 0.15	$ 0.21	$ 0.36	$ 0.22
Weighted average shares used to compute net income per common share:				
Basic	17,051	17,123	17,133	17,096
Diluted	17,776	17,683	17,863	17,504

See accompanying notes to consolidated financial statements.

DTS, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

	For the Six Months Ended June 30,	
	2010	2009
	(Unaudited) (Amounts in thousands)	
Cash flows from operating activities:		
Net income	$ 6,479	$ 3,817
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	2,463	1,820
Gain on sale of assets from discontinued operations	(2,000)	—
Stock-based compensation charges	3,655	2,909
Deferred income taxes	(282)	(81)
Tax benefits from stock-based awards	613	90
Excess tax benefits from stock-based awards	(555)	(221)
Other	11	146
Changes in operating assets and liabilities:		
Accounts receivable	505	1,257
Prepaid expenses and other assets	14	17
Accounts payable, accrued expenses and other liabilities	1,395	5,177
Deferred revenue	2,886	16
Income taxes receivable	(74)	48
Net cash provided by operating activities	15,110	14,995
Cash flows from investing activities:		
Purchases of held-to-maturity investments	(29,674)	(25,452)
Maturities of held-to-maturity investments	21,336	24,400
Sales of available for sale investments	2,250	2,950
Proceeds from the sale of assets from discontinued operations	1,000	—
Cash paid for business acquisition, net	—	(27)
Purchase of property and equipment	(1,993)	(5,048)
Purchase of intangible assets	(1,183)	(192)
Net cash used in investing activities	(8,264)	(3,369)
Cash flows from financing activities:		
Proceeds from the issuance of common stock under stock-based compensation plans	4,128	959
Repurchase and retirement of common stock for restricted stock award withholdings	(743)	(264)
Excess tax benefits from stock-based awards	555	221
Purchase of treasury stock	(22,593)	—
Net cash provided by (used in) financing activities	(18,653)	916
Net increase (decrease) in cash and cash equivalents	(11,807)	12,542
Cash and cash equivalents, beginning of period	42,222	25,658
Cash and cash equivalents, end of period	$ 30,415	$ 38,200

See accompanying notes to consolidated financial statements.

Note 1—Basis of Presentation

The accompanying unaudited consolidated financial statements of DTS, Inc. (the "Company") have been prepared in accordance with accounting principles generally accepted in the United States of America and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. In the opinion of management, the unaudited consolidated financial statements reflect all adjustments, consisting only of normal recurring adjustments, considered necessary for a fair statement of the Company's financial position at June 30, 2010, and the results of operations and cash flows for the periods presented. All significant intercompany transactions have been eliminated in consolidation. Operating results for the three and six months ended June 30, 2010 are not necessarily indicative of the results that may be expected for the fiscal year ending December 31, 2010. The information included in this Form 10-Q should be read in conjunction with the consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2009, filed on March 3, 2010.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosures of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Discontinued Operations

All discussions and amounts in the consolidated financial statements and related notes, except for cash flows, for all periods presented relate to continuing operations only, unless otherwise noted. For additional information, refer to Footnote 9 of the consolidated financial statements, "Discontinued Operations."

Note 2—Significant Accounting Policies

Revenue Recognition

Deferred revenues arise primarily from payments for licensing audio technology received in advance of the culmination of the earnings process. Deferred revenues expected to be recognized within the next twelve months are classified within current liabilities. Deferred revenues will be recognized as revenue in future periods when the applicable revenue recognition criteria are met. For additional information regarding the Company's significant accounting policies for revenue recognition, refer to Footnote 2 of the Company's Annual Report on Form 10-K for the year ended December 31, 2009, filed on March 3, 2010, "Significant Accounting Policies."

Recent Accounting Pronouncements

In October 2009, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2009-13, "Revenue Recognition: Multiple-Deliverable Revenue Arrangements" and ASU 2009-14, "Software: Certain Revenue Arrangements That Include Software

Note 2—Significant Accounting Policies (Continued)

Elements." ASU 2009-13 requires entities to allocate revenue in an arrangement using estimated selling prices of the delivered goods and services based on a selling price hierarchy. ASU 2009-13 also eliminates the residual method of revenue allocation and requires revenue to be allocated using the relative selling price method. In addition, ASU 2009-13 expands the disclosure requirements for revenue recognition. ASU 2009-14 removes tangible products from the scope of software revenue guidance and provides guidance on determining whether software deliverables in an arrangement that includes a tangible product are covered by the scope of the software revenue guidance. ASU 2009-13 and ASU 2009-14 will be effective for the first annual reporting period beginning on or after June 15, 2010, with early adoption permitted provided that the revised guidance is retroactively applied to the beginning of the year of adoption. The Company is currently evaluating the future impact of this new accounting update on its consolidated financial statements.

In January 2010, the FASB issued ASU 2010-6, "Fair Value Measurements and Disclosures: Improving Disclosures About Fair Value Measurements," which requires entities to make new disclosures about recurring or nonrecurring fair value measurements including significant transfers into and out of Level 1 and Level 2 fair value measurements and information on purchases, sales, issuances, and settlements on a gross basis in the reconciliation of Level 3 fair value measurements. ASU 2010-6 is effective for annual reporting periods beginning after December 15, 2009, except for Level 3 reconciliation disclosures which are effective for annual periods beginning after December 15, 2010. The adoption of ASU 2010-6, with respect to Level 1 and Level 2 guidance, did not have a material impact on the Company's consolidated financial statements. The Company is currently evaluating the future impact of this new accounting update, with respect to Level 3 guidance, on its consolidated financial statements.

Note 3—Fair Value Measurements

As of June 30, 2010, the Company's remaining auction rate securities have all been redeemed at par. As of December 31, 2009, the Company held certain financial assets that are required to be measured at fair value on a recurring basis. These financial assets are the Company's auction rate security instruments, which are classified as available-for-sale investments. The auction rate securities held at December 31, 2009 are tax-exempt municipal bonds issued by governmental entities located within the United States that are insured and have a AAA rating.

On October 24, 2008, the Company accepted an offer from UBS AG ("UBS") to liquidate its auction rate securities held in UBS accounts on February 13, 2008. The terms or rights of the UBS offer were publicly filed in a prospectus, dated October 7, 2008. As of December 31, 2009, the Company owned $2,250 par value of these securities. From January 2, 2009 and ending January 4, 2011, the Company had the right, but not the obligation, to sell, at par, these auction rate securities to UBS, and such a transaction would be initiated by UBS. Prior to January 4, 2011, the Company continued to earn and receive all interest that was payable for these auction rate securities. Furthermore, prior to January 4, 2011, UBS, at its sole discretion, may sell, or otherwise dispose of, and/or enter orders in the auctions process with respect to these securities on the Company's behalf so long as it receives par value for the auction rate securities sold. UBS has also agreed to use its best efforts to facilitate issuer redemptions and/or to resolve the liquidity concerns of holders of their auction rate securities through

(Amounts in thousands, except per share data)

Note 3—Fair Value Measurements (Continued)

restructurings and other means. In addition, UBS has agreed to provide “no net cost” loans to holders of the illiquid securities that are subject to bank repurchase, thereby providing the Company with short-term liquidity on its auction rate securities portfolio at no additional cost. As a result of this arrangement with UBS, the Company believes that it had Level 2 inputs within the fair value hierarchy as of December 31, 2009, and par value or cost was a reasonable approximation of fair value.

Due to the Company’s belief that it may have taken until January 2011 to liquidate the remaining securities, its auction rate security instruments have been classified as long-term investments on the consolidated balance sheet as of December 31, 2009.

The Company’s financial assets measured at fair value on a recurring basis were as follows:

		Fair Value Measurements at Reporting Date Using		
Auction Rate Securities	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
As of December 31, 2009	$2,250	$—	$2,250	$—

Note 4—Property and Equipment

Property and equipment consist of the following:

	As of June 30, 2010	As of December 31, 2009
Land	$ 6,600	$ 6,600
Building and improvements	21,018	19,946
Machinery and equipment	2,866	2,647
Office furniture and fixtures	5,725	5,300
Leasehold improvements	1,240	1,156
Software	5,871	5,608
	43,320	41,257
Less: Accumulated depreciation	(9,010)	(7,372)
Property and equipment, net	$34,310	$33,885

Note 5—Commitments and Contingencies

Indemnities, Commitments and Guarantees

In the normal course of business, the Company makes certain indemnities, commitments and guarantees under which the Company may be required to make payments in relation to certain transactions. These indemnities, commitments and guarantees include, among others, intellectual property indemnities to customers in connection with the sale of products and licensing of technology,

Note 5—Commitments and Contingencies (Continued)

indemnities for liabilities associated with the infringement of other parties' technology based upon the Company's products and technology, guarantees of timely performance of the Company's obligations, and indemnities to the Company's directors and officers to the maximum extent permitted by law. The duration of these indemnities, commitments and guarantees varies, and in certain cases, is indefinite. The majority of these indemnities, commitments and guarantees do not provide for any limitation of the maximum potential future payments that the Company could be obligated to make. The Company has not recorded a liability for these indemnities, commitments or guarantees in the accompanying consolidated balance sheets, as future payment is currently not probable.

Note 6—Income Taxes

For the three months ended June 30, 2010, the Company recorded an income tax provision of $1,014 on pre-tax income from continuing operations of $2,570. For the six months ended June 30, 2010, the Company recorded an income tax provision of $3,720 on pre-tax income from continuing operations of $9,196, which resulted in an annualized effective tax rate of 40%. This rate differed from the U.S. statutory rate of 35% primarily due to state income taxes and reserves for federal and state tax audits.

Other long-term liabilities at June 30, 2010 and December 31, 2009, include unrecognized tax benefits of $6,332 and $5,578, respectively, for both domestic and foreign issues. The net increase of $754 was due primarily for uncertainties relating to the Company's transfer pricing with its foreign licensing subsidiaries and eligibility for the extraterritorial income exclusion. The Company believes that its accruals for uncertain tax positions are adequate for all open years, based on the assessment of many factors including past experience and interpretations of tax law applied to the facts of each matter. Inherent uncertainties exist in estimating accruals for uncertain tax positions due to the progress of income tax audits and changes in tax law, both legislated and concluded through the various jurisdictions' tax court systems.

The Company may, from time to time, be assessed interest or penalties by major tax jurisdictions, although any such assessments historically have been minimal and immaterial to the Company's financial results. In accordance with the Company's accounting policy, interest expense and penalties related to income taxes are included in income tax expense.

The Company, or one of its subsidiaries, files income tax returns in the U.S. and other foreign jurisdictions. With few exceptions, the Company is no longer subject to U.S. federal income tax examinations by tax authorities for the years prior to 2004. The Internal Revenue Service is examining the Company's 2005 through 2007 federal income tax returns, including certain prior period carry forwards. In addition, the California Franchise Tax Board is conducting a state tax examination for the years 2004 and 2005.

Licensing revenue is recognized gross of withholding taxes that are remitted by the Company's licensees directly to their local tax authorities. For the three months ended June 30, 2010 and 2009, withholding taxes were $989 and $592, respectively. For the six months ended June 30, 2010 and 2009, withholding taxes were $2,307 and $1,781, respectively.

(Amounts in thousands, except per share data)

Note 6—Income Taxes (Continued)

In the first quarter of 2009, the Company's management identified an adjustment in its reserve for unrecognized tax benefits. This adjustment primarily related to imputed interest on inter-company balances for the years 2003 through 2008, that was recorded during the quarter. The adjustment had the effect of increasing income tax expense in the quarter by $882. The adjustment decreased income from continuing operations by $882 and net income by $882. The Company's management determined that the effect on previously filed reports was not material.

Note 7—Comprehensive Income

At June 30, 2010 and December 31, 2009, accumulated other comprehensive income was comprised mostly of foreign currency translation.

Comprehensive income for the three months ended June 30, 2010 and 2009 was $2,746 and $3,608, respectively. Comprehensive income for the six months ended June 30, 2010 and 2009 was $6,479 and $3,772, respectively.

Note 8—Operating Segment and Geographic Information

The Company's revenue by geographical area, based on the customer's country of domicile, was as follows:

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2010	2009	2010	2009
United States	$ 1,807	$11,833	$ 3,539	$13,536
International	15,653	12,332	35,657	27,891
Total revenue	$17,460	$24,165	$39,196	$41,427

The following table sets forth long-lived tangible assets by geographic area:

	As of June 30, 2010	As of December 31, 2009
United States	$32,926	$32,494
International	1,384	1,391
Total long-lived tangible assets	$34,310	$33,885

Note 9—Discontinued Operations

The Company entered into a Settlement Agreement and Release (the "Settlement Agreement"), dated June 22, 2010, with Datasat Digital Entertainment, Inc., Beaufort International Group Plc and Datasat Communications Limited (collectively the "Datasat Parties"), providing that the Datasat Parties pay the Company $2,000 and pursuant to which the Datasat Parties are released from the obligation to

(Amounts in thousands, except per share data)

Note 9—Discontinued Operations (Continued)

pay the Company any further consideration associated with the purchase of its digital cinema business on May 9, 2008. The Settlement Agreement requires that an initial payment of $1,000 ("Initial Payment") be paid to the Company on June 25, 2010, and the final payment of $1,000 ("Final Payment") be paid to the Company on July 23, 2010. As of June 30, 2010, the Initial Payment has been received, and the Final Payment has been recorded as a receivable in prepaid and other current assets on the consolidated balance sheet. In July 2010, the Final Payment was received by the Company. For additional information, refer to Part II Item 1, "Legal Proceedings," in this report and Footnote 11 of the Company's Annual Report on Form 10-K for the year ended December 31, 2009, filed on March 3, 2010, "Discontinued Operations."

The following table presents pre-tax income and tax information for discontinued operations during the three and six months ended June 30, 2010 and 2009.

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2010	2009	2010	2009
Pre-tax income	$1,902	$ 4	$1,627	$ 1
Income tax provision	729	—	624	—
Income from discontinued operations, net of tax	$1,173	$ 4	$1,003	$ 1

Note 10—Net Income Per Common Share

Basic net income per common share is calculated by dividing net income by the weighted average number of common shares outstanding during the period. Diluted net income per common share is calculated by dividing net income by the sum of the weighted average number of common shares outstanding plus the dilutive effect of unvested restricted stock, outstanding stock options, and the employee stock purchase plan ("ESPP") using the "treasury stock" method.

(Amounts in thousands, except per share data)

Note 10—Net Income Per Common Share (Continued)

The following table sets forth the computation of basic and diluted net income per common share:

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2010	2009	2010	2009
Basic net income per common share:				
Numerator:				
Income from continuing operations	$ 1,556	$ 3,626	$ 5,476	$ 3,816
Income from discontinued operations	1,173	4	1,003	1
Net income	$ 2,729	$ 3,630	$ 6,479	$ 3,817
Denominator:				
Weighted average common shares outstanding	17,051	17,123	17,133	17,096
Continuing operations	$ 0.09	$ 0.21	$ 0.32	$ 0.22
Discontinued operations	0.07	—	0.06	—
Basic net income per common share	$ 0.16	$ 0.21	$ 0.38	$ 0.22
Diluted net income per common share:				
Numerator:				
Income from continuing operations	$ 1,556	$ 3,626	$ 5,476	$ 3,816
Income from discontinued operations	1,173	4	1,003	1
Net income	$ 2,729	$ 3,630	$ 6,479	$ 3,817
Denominator:				
Weighted average shares outstanding	17,051	17,123	17,133	17,096
Effect of dilutive securities:				
Common stock options	592	468	596	336
Restricted stock	114	80	114	67
ESPP	19	12	20	5
Diluted shares outstanding	17,776	17,683	17,863	17,504
Continuing operations	$ 0.09	$ 0.21	$ 0.31	$ 0.22
Discontinued operations	0.06	—	0.05	—
Diluted net income per common share	$ 0.15	$ 0.21	$ 0.36	$ 0.22

For the three months ended June 30, 2010 and 2009, 359 and 382 shares, respectively, of the Company's stock options and restricted stock were excluded from the calculation of diluted earnings per share because their inclusion would have been anti-dilutive. For the six months ended June 30, 2010 and 2009, 303 and 1,076 shares, respectively, of the Company's stock options and restricted stock were excluded from the calculation of diluted earnings per share because their inclusion would have been anti-dilutive.

Note 11—Common Stock Repurchases

In November 2009, the Company's Board of Directors authorized, subject to certain business and market conditions, the purchase of up to 1,000 shares of the Company's common stock in the open market or in privately negotiated transactions. During the three months ending June 30, 2010, the Company repurchased 421 shares of common stock under this authorization for an aggregate of $14,138. During the six months ending June 30, 2010, the Company repurchased 676 shares of common stock under this authorization for an aggregate of $22,593.

All shares repurchased under this authorization are accounted for as treasury stock.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Forward-Looking Statements May Prove Inaccurate

This quarterly report on Form 10-Q and the documents incorporated herein by reference contain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Words such as "believes," "anticipates," "estimates," "expects," "projections," "may," "potential," "plan," "continue" and similar expressions are intended to identify forward-looking statements, but are not the exclusive means of identifying forward-looking statements in this report. All statements, other than statements of historical fact, are statements that could be deemed forward-looking statements, including, but not limited to, statements regarding our future financial performance or position, our business strategy, plans or expectations, and our objectives for future operations, including relating to our products and services. Although forward-looking statements in this report reflect our good faith judgment, such statements can only be based on facts and factors currently known by us. Consequently, forward-looking statements contained herein are inherently subject to risks and uncertainties and our actual results and outcomes may be materially different from those expressed or implied by the forward-looking statements. Factors that could cause or contribute to such differences in results and outcomes include, without limitation, those discussed under the "Risk Factors" section contained in Part II Item 1A, and elsewhere in this report and in other documents we file with the Securities and Exchange Commission, or SEC. We cannot guarantee future results, levels of activity, performance or achievements. You should read the following discussion of our financial condition and results of operations in conjunction with the consolidated financial statements and the notes to those statements included elsewhere in this report. You are urged not to place undue reliance on the forward-looking statements contained in this report, which speak only as of the date of this report. We do not undertake any obligation to revise or update these forward-looking statements to reflect future events or circumstances.

Overview

We are a leading provider of high quality branded entertainment technologies, which are incorporated into an array of entertainment products by hundreds of licensee customers around the world. Our core DTS digital multi-channel audio technology enables the delivery and playback of compelling surround sound and is currently used in a variety of product applications, including audio/video receivers, Blu-ray Disc players, DVD based products, personal computers or PCs, car audio products, video game consoles, network capable televisions, digital media players, home theater systems and mobile handsets. In addition, we provide products and services to studios, radio and television broadcasters, game developers and other content creators to facilitate the inclusion of compelling, realistic DTS-encoded soundtracks in movies, sporting events, television shows and music content.

We derive revenues from licensing our audio technology, trademarks, and know-how under agreements with substantially all of the major consumer audio electronics manufacturers. Our business model generally provides for these manufacturers to pay us a per-unit amount for DTS-enabled products that they manufacture.

We actively engage in intellectual property compliance and enforcement activities focused on identifying third parties who have either incorporated our technology, trademarks, or know-how without a license or who have under-reported the amount of royalties owed under license agreements with us. We continue to invest in our compliance and enforcement infrastructure to support the value of our intellectual property to us and our licensees and to improve the long-term realization of revenue from our intellectual property. As a result of these activities, from time to time, we recognize royalty revenues that relate to consumer electronics manufacturing activities from prior periods. These royalty recoveries may cause revenues to be higher than expected during a particular reporting period and may not occur in subsequent periods. While we consider such revenues to be a regular part of our normal operations, we cannot predict such recoveries or the amount or timing of such revenues.

Our cost of revenues consists primarily of amounts paid for products and materials, salaries and related benefits for operations personnel, amortization of acquired intangibles and payments to third parties for copyrighted material.

Our selling, general, and administrative expenses consist primarily of salaries and related benefits for personnel engaged in sales and licensee support, as well as costs associated with promotional and other selling and licensing activities. Selling, general, and administrative expenses also include professional fees, facility-related expenses, and other general corporate expenses, including personnel engaged in corporate administration, finance, human resources, information systems and legal.

Our research and development costs consist primarily of salaries and related benefits for research and development personnel, engineering consulting expenses associated with new product and technology development, and quality assurance and testing costs. Research and development costs are expensed as incurred.

Executive Summary

Financial Highlights

- Revenues decreased $6.7 million and $2.2 million for the three and six months ended June 30, 2010, respectively, compared to the same prior year periods, due primarily to a decrease in royalty recoveries from intellectual property compliance and enforcement activities.
- Royalty recoveries from intellectual property compliance and enforcement activities decreased $13.0 million and $13.6 million for the three and six months ended June 30, 2010, respectively, compared to the same prior year periods. These decreases resulted primarily from the settlement of legal matters with Zoran Corporation during the second quarter of 2009.
- Royalties from Blu-ray product markets increased 129% and 95% for the three and six months ended June 30, 2010, respectively, compared to the same prior year periods.
- Royalties from newer markets, including televisions and digital media players, comprised over 15% of total revenue for the three months ended June 30, 2010, compared to less than 5% for the three months ended June 30, 2009. For the six months ended June 30, 2010 and 2009, these royalties comprised nearly 15% and less than 5% of total revenue, respectively.

Trends, Opportunities, and Challenges

Historically, our revenue has been primarily dependent upon the DVD based home theater market. The success of DVD based systems and products has fueled a demand for higher quality entertainment in the home, and this demand is extending into the car audio, personal computer, portable electronics, online networked devices, broadcast, video game console and mobile handset markets as well. We have seen the acceleration of the market for high definition televisions drive demand for Blu-ray Disc players and advanced home theater systems. Consumers are more broadly embracing the Blu-ray technology as prices decline and content availability increases, and as customers realize the value of the advanced features that Blu-ray provides, such as the ability to connect to the internet and ultimately playback 3-D content.

Because we are a mandatory technology in the Blu-ray Disc standard, our revenue growth is closely tracking the growth in sales of Blu-ray equipped players, game consoles and PCs. Further, we believe that this mandatory position in the Blu-ray Disc standard will give us the ability to extend the reach of a broad array of our technologies in several large markets, such as applications beyond optical media. For example, we have signed agreements with a number of digital media player, networkconnected digital television and mobile handset manufacturers to incorporate DTS decoders into their products.

One of the largest challenges that we face is the growing consumer trend toward open platform, on-line entertainment consumption and the need to constantly and rapidly evolve our technologies to address the emerging markets. We believe that although the trend has begun, any transition to such open platform, on-line entertainment will take many years. During the transition period, we expect that both optical media and on-line entertainment formats will continue to thrive.

Further, we currently face a challenge regarding our ability to determine the impact of the current global economic downturn on consumer buying patterns. While we do not have near-term visibility into the timing or extent of an economic recovery, we continue to remain optimistic that our revenues from both Blu-ray enabled products and our newer markets will continue to grow.

Critical Accounting Policies and Estimates

Management's Discussion and Analysis of Financial Condition and Results of Operations are based upon our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of our consolidated financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues, and expenses, and related disclosure of contingent assets and liabilities. On an on-going basis, estimates and judgments are evaluated, including those related to revenue recognition, allowance for doubtful accounts, impairment of long-lived assets, stock-based compensation, and income taxes. These estimates and judgments are based on historical experience and on various other assumptions that we believe to be reasonable under the circumstances, which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. By their nature, estimates are subject to an inherent degree of uncertainty. Actual results may differ from these estimates. There has been no material change to our critical accounting policies and estimates from the information provided in our Form 10-K filed on March 3, 2010.

Results of Continuing Operations

Revenues

	2010	2009	Change $	Change %
	($ in thousands)			
Three months ended June 30,	$17,460	$24,165	$(6,705)	(28)%
Six months ended June 30,	$39,196	$41,427	$(2,231)	(5)%

The decrease in revenues for the three months ended June 30, 2010, compared to the same prior year period, was largely attributable to a $13.0 million decrease in royalty recoveries from intellectual property compliance and enforcement activities. This decrease in royalty recoveries resulted primarily from the settlement of legal matters with Zoran Corporation during the second quarter of 2009. Partially offsetting this decrease was continued growth in Blu-ray related royalties and royalties from newer markets, including televisions and digital media players. Blu-ray related royalties comprised over 25% and less than 10% of total revenue for the three months ended June 30, 2010 and 2009, respectively. In dollar terms, these royalties were up 129% for the three months ended June 30, 2010, compared to the same prior year period. Royalties from newer markets comprised over 15% and less than 5% of total revenue for the three months ended June 30, 2010 and 2009, respectively. The growth in newer markets results from a growing consumer interest in on-line content. Royalties from the car market also increased for the three months ended June 30, 2010, compared to the same prior year period and excluding any impact from the aforementioned royalty recoveries. We continue to be cautious regarding the outlook for the consumer electronics industry as a whole, and the revenues we derive from that industry, in light of the recent turmoil in the global economic environment. However, we expect technology licensing revenues to grow as wider availability of Blu-ray enabled players, PCs and game consoles, coupled with expected aggressive pricing and promotion of these products by retailers and consumer electronics product manufacturers, should result in increasing licensing revenues from the Blu-ray format.

The decrease in revenues for the six months ended June 30, 2010, compared to the same prior year period, was largely attributable to a $13.6 million decrease in royalty recoveries from intellectual property compliance and enforcement activities. Partially offsetting this decrease was continued growth in Blu-ray related royalties and royalties from newer markets. Blu-ray related royalties comprised nearly 30% and nearly 15% of total revenue for the six months ended June 30, 2010 and 2009, respectively. In dollar terms, these royalties were up 95% for the six months ended June 30, 2010, compared to the same prior year period. Royalties from newer markets comprised nearly 15% and less than 5% of total revenue for the six months ended June 30, 2010 and 2009, respectively. Royalties from the car market also increased for the six months ended June 30, 2010, compared to the same prior year period and excluding any impact from the aforementioned royalty recoveries.

Gross Profit

	2010	%	2009	%	Percentage point change in gross profit margin relative to prior period
	($ in thousands)				
Three months ended June 30,	$17,000	97%	$23,716	98%	(1)%
Six months ended June 30,	$38,286	98%	$40,533	98%	0%

Consolidated gross profit percentage for the three and six months ended June 30, 2010, compared to the same prior year period, remained fairly consistent.

We expect consolidated gross margins in the 97% to 98% range for 2010.

Selling, General and Administrative ("SG&A")

	2010	2009	Change $	Change %
	($ in thousands)			
Three months ended June 30,	$11,727	$16,067	$(4,340)	(27)%
% of Revenue	*67%*	*66%*		
Six months ended June 30,	$24,126	$28,855	$(4,729)	(16)%
% of Revenue	*62%*	*70%*		

The dollar decrease for the three months ended June 30, 2010, compared to the same prior year period, was primarily due to a $6.2 million decrease in professional fees. This decrease resulted largely from the fees associated with the Zoran litigation matters in the prior year period. Partially offsetting this decrease was a $1.2 million increase in employee related costs, a $0.3 million increase in depreciation for our new corporate headquarters and a $0.2 million increase in travel related costs. The increase in employee related costs was primarily attributable to expanded operations and stock-based compensation for the three months ended June 30, 2010, compared to the same prior year period. The increase in travel related costs was primarily attributable to increased sales support and expanded operations.

The decrease for the six months ended June 30, 2010, compared to the same prior year period, was primarily due to an $8.8 million decrease in professional fees. This decrease resulted largely from the fees associated with the Zoran litigation matters in the prior year period. Partially offsetting this decrease was a $2.8 million increase in employee related costs, a $0.6 million increase in depreciation for our new corporate headquarters, a $0.5 million increase in advertising expenses and a $0.3 million increase in travel related costs. The increase in employee related costs was primarily attributable to expanded operations and stock-based compensation for the six months ended June 30, 2010, compared to the same prior year period. The increase in advertising expenses was primarily attributable to increased tradeshow advertising and related activities. The increase in travel related costs was primarily attributable to increased sales support and expanded operations.

We expect SG&A expenses to continue to increase, primarily to support activities such as new technology initiatives, international expansion and intellectual property enforcement.

Research and Development ("R&D")

	2010	2009	Change $	Change %
	($ in thousands)			
Three months ended June 30,	$2,842	$2,380	$462	19%
% of Revenue	*16%*	*10%*		
Six months ended June 30,	$5,315	$4,563	$752	16%
% of Revenue	*14%*	*11%*		

The increase for the three and six months ended June 30, 2010, compared to the same prior year period, was primarily due to an increase in employee related costs, including expanded operations and stock-based compensation.

We intend to continue to invest in R&D to support the activities mentioned above, and thus expect to see sequential growth through the remainder of the year.

Interest and Other Income, Net

	2010	2009	Change $	Change %
	($ in thousands)			
Three months ended June 30,	$139	$718	$(579)	(81)%
Six months ended June 30,	$351	$862	$(511)	(59)%

The decrease for the three and six months ended June 30, 2010, compared to the same prior year period, was due to interest and other income associated with certain royalty recoveries and a less favorable interest rate environment for our investment portfolio.

We expect interest and other income for the year to continue on its current trend, based on the current interest rate environment and current investment balances.

Income Taxes

	2010	2009
	($ in thousands)	
Three months ended June 30,	$1,014	$2,361
Effective tax rate	*39%*	*39%*
Six months ended June 30,	$3,720	$4,161
Effective tax rate	*40%*	*52%*

Our effective tax rate is based upon a projection of annual fiscal year results, and these rates differed from the U.S. statutory rate of 35% primarily due to state income taxes and reserves for federal and state audits. Also, in the first quarter of 2009, the Company's management identified an adjustment in its reserve for unrecognized tax benefits. This adjustment primarily related to imputed interest on inter-company balances for the years 2003 through 2008, that was recorded during the quarter. The adjustment had the effect of increasing income tax expense in the quarter by $0.9 million. The adjustment decreased income from continuing operations by $0.9 million and net income by $0.9 million. The Company's management determined that the effect on previously filed reports was not material.

Results of Discontinued Operations

The income from discontinued operations for the three and six months ended June 30, 2010, resulted primarily from a $2.0 million settlement agreement and release with the buyer of the cinema business. For additional information, refer to Footnote 9 of the consolidated financial statements, "Discontinued Operations."

Liquidity and Capital Resources

At June 30, 2010, we had cash, cash equivalents and short-term investments of $76.6 million, compared to $75.4 million at December 31, 2009.

Net cash provided by operating activities was $15.1 million and $15.0 million for the six months ended June 30, 2010 and 2009, respectively. Cash flows from operating activities consisted of net income adjusted for certain non-cash items, including stock-based compensation, depreciation and amortization, and the effect of changes in working capital and other operating activities. The operating cash flows for the six months ended June 30, 2010 and 2009, remained fairly consistent. However, the operating cash flows during the six months ended June 30, 2010, were impacted by increases in deferred revenue arising primarily from payments for licensing audio technology received in advance of the culmination of the earnings process and income from operations. The operating cash flows during the six months ended June 30, 2009, were impacted by increases in liabilities for legal expenses related to the aforementioned litigation with Zoran Corporation.

We typically use cash in investing activities primarily to purchase office equipment, fixtures, computer hardware and software, engineering and manufacturing test and certification equipment, for business and technology acquisitions, for securing patent and trademark protection for our proprietary technology and brand name, and to purchase short-term and long-term investments such as bank certificates of deposit and municipal bonds. Net cash used in investing activities totaled $8.3 million and $3.4 million for the six months ended June 30, 2010 and 2009, respectively. Investing activities for the six months ending June 30, 2010, were primarily impacted by the net impact of investment purchases, sales and maturities. Investing activities for the six months ending June 30, 2009, were primarily impacted by capital expenditures associated with our new corporate headquarters.

Net cash used in financing activities totaled $18.7 million for the six months ended June 30, 2010, which results primarily from the purchase of treasury stock during the six months ended June 30, 2010. Partially offsetting the cash used in financing activities for the six months ended June 30, 2010, were proceeds from the issuance of common stock under stock-based compensation plans. Net cash provided by financing activities totaled $0.9 million for the six months ended June 30, 2009, and were largely comprised of proceeds from the issuance of common stock under stock-based compensation plans.

We believe that our cash, cash equivalents, short-term investments, and cash flows from operations will be sufficient to satisfy our working capital and capital expenditure requirements for at least the next twelve months. Changes in our operating plans, including lower than anticipated revenues, increased expenses, acquisition of companies, products or technologies or other events, including those described in "Risk Factors" included elsewhere herein, in our Form 10-K filed on March 3, 2010 and in other filings, may cause us to seek additional debt or equity financing on an accelerated basis. Financing may not be available on acceptable terms, or at all, particularly given current economic conditions, including lack of confidence in the financial markets and limited availability of capital and demand for debt and equity securities. Our failure to raise capital when needed could negatively impact our growth plans and our financial condition and results of operations. Additional equity financing may be dilutive to the holders of our common stock and debt financing, if available, and may involve significant cash payment obligations and financial or operational covenants that restrict our ability to operate our business.

Contractual obligations

There have been no material changes to our contractual obligations since December 31, 2009, with the exception of the increased obligations associated with our gross unrecognized tax benefits. As of June 30, 2010, our total amount of unrecognized tax benefits was $6.3 million and was considered a long-term obligation. We are currently unable to make reasonably reliable estimates of the periods of cash settlements associated with these obligations.

Recently Issued Accounting Standards

Refer to Footnote 2 of the consolidated financial statements, "Significant Accounting Policies."

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Market risk represents the risk of loss arising from adverse changes in market rates and foreign exchange rates.

Our interest income is sensitive to changes in the general level of U.S. interest rates, particularly since a significant portion of our investments are and will be in short-term and long-term marketable securities, U.S. government securities and corporate bonds. Due to the nature and maturity of our short-term investments, we have concluded that there is no material market risk exposure to our principal at June 30, 2010. The estimated average maturity of our investment portfolio is less than one year. As of June 30, 2010, a one percentage point change in interest rates throughout a one-year period would have an annual effect of approximately $0.8 million on our income before income taxes.

During the six months ended June 30, 2010, we derived approximately 91% of our revenues from sales outside the United States, and maintain international research, sales, marketing, and business development offices. Therefore, our results could be negatively affected by such factors as changes in foreign currency exchange rates, trade protection measures, longer accounts receivable collection patterns, and changes in regional or worldwide economic or political conditions. The risks of our international operations are mitigated in part by the extent to which our revenues are denominated in U.S. dollars and, accordingly, we are not exposed to significant foreign currency risk on these items. We do have foreign currency risk on certain revenues and operating expenses such as salaries and overhead costs of our foreign operations and cash maintained by these operations. Revenues denominated in foreign currencies accounted for approximately 4% of total revenues during the six months ended June 30, 2010. Operating expenses, including cost of sales, for our foreign subsidiaries were approximately $7.4 million for the six months ended June 30, 2010. Based upon the expenses for the six months ended June 30, 2010, a one percentage point change in foreign currency rates throughout a one-year period would have an immaterial annual effect on income before income taxes.

Our international business is subject to risks, including, but not limited to, differing economic conditions, changes in political climate, differing tax structures, other regulations and restrictions, and foreign exchange rate volatility when compared to the United States dollar. Accordingly, our future results could be materially impacted by changes in these or other factors.

We are also affected by exchange rate fluctuations as the financial statements of our foreign subsidiaries are translated into the United States dollar in consolidation. As exchange rates vary, these results, when translated, may vary from expectations and could adversely or positively impact overall profitability. During the six months ended June 30, 2010, the impact of foreign exchange rate fluctuations related to translation of our foreign subsidiaries' financial statements was immaterial to comprehensive income.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

We maintain disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934, as amended (the "Exchange Act")) that are designed to ensure that information required to be disclosed in the reports we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the SEC and that such information is accumulated and communicated to our management, including our chief executive officer and chief financial officer, as appropriate to allow timely decisions regarding required disclosure.

We carried out an evaluation, under the supervision and with the participation of our management, including our chief executive officer and chief financial officer, of the effectiveness of our disclosure controls and procedures as of the end of the period covered by this report. Based on such evaluation, our chief executive officer and chief financial officer concluded that as of the end of the period covered by this report our disclosure controls and procedures were effective.

Changes in Internal Control over Financial Reporting

There has been no change in our internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during our most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

In the ordinary course of our business, we actively pursue legal remedies to enforce our intellectual property rights and to stop unauthorized use of our technology and trademarks.

The description of legal matters with Datasat Digital Entertainment, Inc., Beaufort International Group Plc and Datasat Communications Limited (collectively the "Datasat Parties") referred to in our Annual Report on Form 10-K for the year ended December 31, 2009, filed with the Securities and Exchange Commission on March 3, 2010, is incorporated herein by reference. In addition, we entered into a Settlement Agreement and Release, dated June 22, 2010, with the Datasat Parties (the "Settlement Agreement"), providing that the Datasat Parties pay us $2.0 million and pursuant to which the Datasat Parties are released from the obligation to pay us any further consideration associated with the purchase of our digital cinema business on May 9, 2008. The Settlement Agreement also contains, among other terms, mutual releases of all claims of the parties in the complaint and amended cross-complaint, and will, upon completion of the settlement payments, result in a request for dismissal of the lawsuit.

We are not currently a party to any other material legal proceedings. We may, however, become subject to lawsuits from time to time in the course of our business.

Item 1A. Risk Factors

Set forth below and elsewhere in this report and in other documents we file with the SEC are risks and uncertainties that could cause our actual results to differ materially from the results contemplated by the forward-looking statements contained in this report and other public statements we make. If any of the following risks actually occurs, our business, financial condition, or results of operations could suffer. In that case, the trading price of our common stock could decline, and you may lose all or part of your investment. The risk factors described below include any material changes to and supersede the risk factors previously disclosed in Part I, Item 1A of our most recent Annual Report on Form 10-K.

Risks Related to Our Business

Our business is highly dependent on the growth in Blu-ray Disc products, and we do not have near-term visibility into the precise timing of this expected growth or how smooth or linear this growth will be. To the extent that consumer adoption of Blu-ray Disc products fails to materialize or does not materialize as quickly or extensively as we expect, or alternative technologies in which we do not participate replace DVD or Blu-ray Disc based products as a dominant medium for consumer video entertainment, our business will be adversely affected.

Past growth in our business has been due in large part to the rapid growth in sales of DVD based products and home theater systems incorporating our technologies. As the markets for DVD based products mature, we are seeing sales of these products declining and growth in our business shifting to Blu-ray Disc based products. While the release and consumer adoption of Blu-ray Disc players continues to ramp up, potentially slow adoption by consumers of Blu-ray Disc players could adversely affect our business. In addition, if new technologies, including direct downloads of content, are developed or deployed that substantially compete with or replace Blu-ray Disc products as a dominant medium for consumer video entertainment, our business, operating results and prospects could be adversely affected.

Economic downturns could disrupt and materially harm our business.

Negative trends in the general economy could cause a downturn in the market for our technology, products and services. The current and continuing financial disruption affecting the global financial markets and the concern whether investment banks and other financial institutions will continue operations in the foreseeable future have resulted in a tightening in the credit markets, a low level of liquidity in many financial markets and extreme volatility in credit and equity markets. The ongoing financial crisis may adversely affect our operating results if it results, for example, in the insolvency of a key licensee or other customer, the inability of our licensees and/or other customers to obtain credit to finance their operations, including to finance the manufacture of products containing our technologies, and delays in reporting and/or payments from our licensees. Tight credit markets could also delay or prevent us from acquiring or making investments in other technologies, products or businesses that could enhance our technical capabilities, complement our current products and services, or expand the breadth of our markets. If we are unable to execute such acquisitions and/or strategic investments, our operating results and business prospects may suffer.

In addition, global economic conditions, including the credit crisis, increased cost of commodities, widespread employee layoffs, actual or threatened military action by the United States and the continued threat of terrorism, have resulted in decreased consumer spending and may continue to negatively impact consumer confidence and spending. Any reduction in consumer confidence or disposable income, in general, may negatively affect the demand for consumer electronics products that incorporate our digital audio technology.

We cannot predict other negative events that may have adverse effects on the global economy in general and the consumer electronics industry specifically. However, the factors described above and such unforeseen events could negatively affect our revenues and operating results.

If we fail to protect our intellectual property rights, our ability to compete could be harmed.

Protection of our intellectual property is critical to our success. Patent, trademark, copyright, and trade secret laws and confidentiality and other contractual provisions afford only limited protection and may not adequately protect our rights or permit us to gain or keep any competitive advantage. We face numerous risks in protecting our intellectual property rights, including the following:

- our patents may be challenged, found unenforceable or invalidated by our competitors;
- our pending patent applications may not issue, or if issued, may not provide meaningful protection for related products or proprietary rights;
- we may not be able to prevent the unauthorized disclosure or use of our technical knowledge or other trade secrets by employees, consultants, and advisors;
- we may not be able to practice our trade secrets as a result of patent protection afforded a third-party for such product, technique or process;
- the laws of foreign countries may not protect our intellectual property rights to the same extent as the laws of the United States, and mechanisms for enforcement of intellectual property rights may be inadequate in foreign countries;
- our competitors may produce competitive products or services that do not unlawfully infringe upon our intellectual property rights;
- efforts to identify and prosecute unauthorized uses of our technology are time consuming, expensive, and divert resources from the operation of our business; and
- we may be unable to successfully identify or prosecute unauthorized uses of our technology.

As a result, our means of protecting our intellectual property rights and brands may not be adequate. Furthermore, despite our efforts, third parties may violate, or attempt to violate, our intellectual property rights. Enforcement, including infringement claims and lawsuits would likely be expensive to resolve and would require management's time and resources. In addition, we have not sought, and do not intend to seek, patent and other intellectual property protections in all foreign countries. In countries where we do not have such protection, products incorporating our technology may be lawfully produced and sold without a license.

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

Establishing, maintaining and strengthening our "DTS" brand is critical to our success. Our brand identity is key to maintaining and expanding our business and entering new markets. Our success depends in large part on our reputation for providing high quality products, services and technologies to the consumer electronics products industry and the entertainment industry. If we fail to promote and maintain our brand successfully, our business and prospects may suffer. Moreover, we believe that the likelihood that our technologies will be adopted in industry standards depends, in part, upon the strength of our brand, because professional organizations and industry participants are more likely to incorporate technologies developed by a well-respected and well-known brand into standards.

We may not be able to evolve our technology, products, and services or develop new technology, products, and services that are acceptable to our customers or the changing market.

The market for our technology, products, and services is characterized by:

- rapid technological change;
- new and improved product introductions;
- changing customer demands;
- evolving industry standards; and
- product obsolescence.

Our future success depends on our ability to enhance our existing technology, products, and services and to develop acceptable new technology, products, and services on a timely basis. The development of enhanced and new technology, products, and services is a complex and uncertain process requiring high levels of innovation, highly-skilled engineering and development personnel, and the accurate anticipation of technological and market trends. We may not be able to identify, develop, market, or support new or enhanced technology, products, or services on a timely basis, if at all. Furthermore, our new technology, products, and services may never gain market acceptance, and we may not be able to respond effectively to evolving consumer demands, technological changes, product announcements by competitors, or emerging industry standards. Any failure to respond to these changes or concerns would likely prevent our technology, products, and services from gaining market acceptance or maintaining market share and could lead to our technology, products and services becoming obsolete.

We may be sued by third parties for alleged infringement of their proprietary rights.

Companies that participate in the digital audio, digital image processing, consumer electronics, and entertainment industries hold a large number of patents, trademarks, and copyrights, and are frequently involved in litigation based on allegations of patent infringement or other violations of intellectual property rights. Intellectual property disputes frequently involve highly complex and costly scientific matters, and each party generally has the right to seek a trial by jury which adds additional costs and uncertainty. Accordingly, intellectual property disputes, with or without merit, could be costly and time consuming to litigate or settle, and could divert management's attention from executing our business plan. In addition, our technology and products may not be able to withstand any third-party claims or rights against their use. If we were unable to obtain any necessary license following a determination of infringement or an adverse determination in litigation or in interference or other administrative proceedings, we may need to redesign some of our products to avoid infringing a third party's rights and could be required to temporarily or permanently discontinue licensing our products.

We may be subject to litigation proceedings that could harm our business.

In the past, we have been a party to litigation related to protection and enforcement of our intellectual property, and we may be a party to additional litigation in the future. Litigation is subject to inherent uncertainties, and unfavorable rulings could occur. An unfavorable ruling could include monetary damages (including treble damages under the Clayton Act) and an injunction prohibiting us from licensing our technology in particular ways or at all. Were an unfavorable ruling to occur, our business and results of operations could be materially harmed. In addition, any protracted litigation could divert management's attention from our day-to-day operations, disrupt our business and cause our operating results to suffer.

We face intense competition. Certain of our competitors have greater brand recognition and resources than we do.

The digital audio, consumer electronics and entertainment markets are intensely competitive, subject to rapid change, and significantly affected by new product introductions and other market activities of industry participants. Our principal competitor is Dolby Laboratories, Inc., who competes with us in most of our markets. We also compete with other companies offering digital audio technology incorporated into consumer electronics product and entertainment mediums, including Fraunhofer Institut Integrierte Schaltungen, Koninklijke Philips Electronics N.V. (Philips), Microsoft Corporation, Sony Corporation, Thomson and SRS Labs, Inc.

Certain of our current and potential competitors may enjoy substantial competitive advantages, including:

- greater name recognition;
- a longer operating history;
- more developed distribution channels and deeper relationships with our common customer base;
- a more extensive customer base;
- digital technologies that provide features that ours do not;
- broader product and service offerings;
- greater resources for competitive activities, such as research and development, strategic acquisitions, alliances, joint ventures, sales and marketing, and lobbying industry and government standards;
- more technicians and engineers; and
- greater technical support.

As a result, these current and potential competitors may be able to respond more quickly and effectively than we can to new or changing opportunities, technologies, standards, or customer requirements.

In addition to the competitive advantages described above, Dolby also enjoys other unique competitive strengths relative to us. For example, it introduced multi-channel audio technology before we did. Its technology has been incorporated in significantly more DVD based products than our technology. It has also achieved mandatory standard status in product categories that we have not, including DVD based products, for its stereo technology and terrestrial digital television broadcasts in the United States. As a result of these factors, Dolby has a competitive advantage in selling its digital multi-channel audio technology to consumer electronics products manufacturers.

We have limited control over existing and potential customers' and licensees' decisions to include our technology in their product offerings.

Except for Blu-ray enabled products, where our technology is mandatory, we are dependent on our customers and licensees—including consumer electronics product manufacturers, semiconductor manufacturers, producers and distributors of content for music, videos, and games—to incorporate our technology into their products, purchase our products and services, or release their content in our proprietary DTS audio format. Although we have contracts and license agreements with many of these companies, these agreements do not require any minimum purchase commitments, are on a non-exclusive basis, and do not typically require incorporation or use of our technology, trademarks or services. Our customers, licensees and other manufacturers might not utilize our technology or services in the future.

If we are unable to maintain and increase the amount of entertainment content released with DTS audio soundtracks, demand for the technology, products, and services that we offer to consumer electronics product manufacturers may significantly decline.

We expect to derive a significant percentage of our revenues from the technology, products, and services that we offer to manufacturers of consumer electronics products. To date, the most significant driver for the use of our technology in the home theater market has been the release of major movie titles with DTS audio soundtracks. We also believe that demand for our DTS audio technology in growing markets for multi-channel audio, including cars, personal computers, video game consoles, digital media players and mobile handsets will be based on the number, quality, and popularity of the Blu-ray Disc titles, computer software programs, and video games either released with DTS audio soundtracks or capable of being coded and played in DTS format. Although we have existing relationships with many leading providers of movie, music, computer, and video game content, we do not have contracts that require any of these parties to develop and release content with DTS audio soundtracks. In addition, we may not be successful in maintaining existing relationships or developing relationships with other existing providers or new market entrants that provide content. As a result, we cannot assure you that a significant amount of content in movies, Blu-ray Disc titles, computer software programs, video games, or other entertainment mediums will be released with DTS audio soundtracks. If the amount, variety, and popularity of entertainment content released with DTS audio soundtracks do not increase, consumer electronics products manufacturers that pay us per-unit licensing fees may discontinue offering DTS playback capabilities in the consumer electronics products that they sell.

Declining retail prices for consumer electronics products could force us to lower the license or other fees we charge our customers.

The market for consumer electronics products is intensely competitive and price sensitive. Retail prices for consumer electronics products that include our DTS audio technology have decreased significantly and we expect prices to continue to decrease for the foreseeable future. Declining prices for consumer electronics products could create downward pressure on the licensing fees we currently charge our customers who integrate our technology into the consumer electronics products that they sell and distribute. Most of the consumer electronics products that include our audio technology also include Dolby's multi-channel audio technology. As a result of pricing pressure, consumer electronics products manufacturers who manufacture products in which our audio technology is not a mandatory standard could decide to exclude our DTS audio technology from their products altogether.

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

Our licensing revenue from consumer electronics product manufacturers depends in large part upon the availability of ICs that implement our technologies. IC manufacturers incorporate our technologies into these ICs, which are then incorporated into consumer electronics products. We do not manufacture these ICs, but rather depend on IC manufacturers to develop, produce and then sell them to licensed consumer electronics product manufacturers. We do not control the IC manufacturers' decisions whether or not to incorporate our technologies into their ICs, and we do not control their product development or commercialization efforts. If these IC manufacturers are unable or unwilling, for any reason, to implement our technologies into their ICs, or if, for any reason, they sell fewer ICs incorporating our technologies, our operating results will be adversely affected.

We rely on the accuracy of our customers' manufacturing reports for reporting and collecting our revenues, and if these reports are untimely or incorrect, our revenues could be delayed or inaccurately reported.

Most of our revenues are generated from consumer electronics product manufacturers who license and incorporate our technology in their consumer electronics products. Under our existing agreements, these customers pay us per-unit licensing fees based on the number of consumer electronics products manufactured that incorporate our technology. We rely on our customers to accurately report the number of units manufactured in collecting our license fees, preparing our financial reports, projections, budgets, and directing our sales and product development efforts. Most of our license agreements permit us to audit our customers, but audits are generally expensive, time consuming, difficult to manage effectively, dependent in large part on the cooperation of our licensees and the quality of the records they keep, and could harm our customer relationships. If any of our customer reports understate the number of products they manufacture, we may not collect and recognize revenues to which we are entitled, or may endure significant expense to obtain compliance.

We expect our operating expenses to increase in the future, which may impact profitability.

We expect our operating expenses to increase as we, among other things:

- expand our sales and marketing activities, including the continued development of our international operations;
- adopt a more customer-focused business model which is expected to entail additional hiring;
- acquire businesses or technologies and integrate them into our existing organization;
- increase our research and development efforts to advance our existing technology, products, and services and develop new technology, products, and services;
- hire additional personnel, including engineers and other technical staff;
- expand and defend our intellectual property portfolio;
- upgrade our operational and financial systems, procedures, and controls; and
- continue to assume the responsibilities of being a public company.

As a result, we will need to grow our revenues and manage our costs in order to positively impact profitability. In addition, we may fail to accurately estimate and assess our increased operating expenses as we grow.

We have a limited operating history in certain new and evolving markets.

Our technology has only recently been incorporated into other consumer electronics markets, such as personal computers, video game consoles, portable electronics devices, digital satellite and cable broadcast products, digital media players and mobile handsets. Recently, we have also entered into the "virtual" surround space with the internal development of technology that we have branded DTS Surround Sensation. We do not have experience in this specific segment of the market and it is dominated by existing technologies from companies including Dolby Laboratories, Inc., SRS Labs, Inc. and BBE Sound, Inc. As a result, the demand for our technology, products, and services and the income potential of these businesses are unproven. In addition, because the market for digital audio technology is relatively new and rapidly evolving, we have limited insight into trends that may emerge and affect our business. We may make errors in predicting and reacting to relevant business trends, which could harm our business. Before investing in our common stock, you should consider the risks, uncertainties, and difficulties frequently encountered by companies in new and rapidly evolving markets such as ours. We may not be able to successfully address any or all of these risks.

Our technology and products are complex and may contain errors that could cause us to lose customers, damage our reputation, or incur substantial costs.

Our technology or products could contain errors that could cause our products or technology to operate improperly and could cause unintended consequences. If our products or technology contain errors we, could be required to replace them, and if any such errors cause unintended consequences, we could face claims for product liability. Although we generally attempt to contractually limit our exposure to incidental and consequential damages, as well as provide insurance coverage for such events, if these contract provisions are not enforced or are unenforceable for any reason, if liabilities arise that are not effectively limited, or if our insurance coverage is inadequate to satisfy the liability, we could incur substantial costs in defending and/or settling product liability claims.

We cannot be certain of the future effectiveness of our internal control over financial reporting or the impact thereof on our operations or the market price of our common stock.

Pursuant to Section 404 of the Sarbanes-Oxley Act of 2002, we are required to include in our annual reports on Form 10-K our assessment of the effectiveness of our internal control over financial reporting. We cannot assure you that our system of internal control will be effective in the future as our operations and control environment change. If we cannot adequately maintain the effectiveness of our internal control over financial reporting, our financial reporting may not be timely and/or accurate. If reporting delays or errors actually occur, we could be subject to sanctions or investigation by regulatory authorities, such as the SEC. Moreover, even if we conclude that our internal control is effective, our independent registered public accounting firm may disagree. If our independent registered public accounting firm is not satisfied with our internal control over financial reporting or the level at which our internal control over financial reporting is documented, designed, operated or reviewed, or if the independent registered public accounting firm interprets the requirements, rules or regulations differently than we do, then it may issue an adverse or qualified opinion. Any of the above outcomes could adversely affect our financial results or result in a loss of investor confidence in the reliability of our financial information, which could materially and adversely affect the market price of our common stock.

We are subject to additional risks associated with our international operations.

Our licensing headquarters are located in Limerick, Ireland, and we market and sell our products and services outside the United States. We currently have employees located in eight countries, and many of our customers and licensees are located outside the United States. As a key component of our business strategy, we intend to expand our international sales and customer support. During the six months ended June 30, 2010, approximately 91% of our revenues were derived internationally. We face numerous risks in doing business outside the United States, including:

- unusual or burdensome foreign laws or regulatory requirements or unexpected changes to those laws or requirements;
- tariffs, trade protection measures, import or export licensing requirements, trade embargos, and other trade barriers;
- difficulties in attracting and retaining qualified personnel and managing foreign operations;
- competition from foreign companies;
- dependence on foreign distributors and their sales channels;
- longer accounts receivable collection cycles and difficulties in collecting accounts receivable;
- less effective and less predictable protection and enforcement of our intellectual property;
- changes in the political or economic condition of a specific country or region, particularly in emerging markets;
- fluctuations in the value of foreign currency versus the U.S. dollar and the cost of currency exchange;
- potentially adverse tax consequences; and
- cultural differences in the conduct of business.

Such factors could cause our future international sales to decline.

Our business practices in international markets are also subject to the requirements of the Foreign Corrupt Practices Act. If any of our employees is found to have violated these requirements, we and our employees could be subject to significant fines, criminal sanctions and other penalties.

Our international revenue is mostly denominated in U.S. dollars. As a result, fluctuations in the value of the U.S. dollar and foreign currencies may make our technology, products, and services more expensive for international customers, which could cause them to decrease their purchases from us. Expenses for our subsidiaries are denominated in their respective local currencies. As a result, if the U.S. dollar weakens against the local currency, the translation of our foreign-currency-denominated expenses will result in higher operating expense without a corresponding increase in revenue. Significant fluctuations in the value of the U.S. dollar and foreign currencies could have a material impact on our consolidated financial statements. The main foreign currencies we encounter in our operations are the Yen, Euro, CAD, RMB and GBP. We do not currently engage in currency hedging activities to limit the risk of exchange rate fluctuations.

We face risks in expanding our business operations in China.

An important strategy of ours is to expand our business operations in China. However, we may be unsuccessful in implementing this strategy as planned or at all. Factors that could inhibit our successful expansion into China include its historically poor recognition of intellectual property rights and poor performance in stopping counterfeiting and piracy activity as well as enforcing judgments. If we are unable to successfully stop unauthorized use of our intellectual property and assure compliance by our Chinese licensees, we could experience increased operational and enforcement costs both inside and outside China.

Even if we are successful in expanding into China, we may be greatly impacted by the political, economic, and military conditions in China, Taiwan, North Korea, and South Korea. Such disputes may continue or escalate, resulting in economic embargos, disruptions in shipping, or even military hostilities. This could severely harm our business by interrupting or delaying production or shipment of our products or products that incorporate our technology.

We may experience fluctuations in our operating results.

We have historically experienced moderate seasonality in our business due to our business mix and the nature of our products. Consumer electronics manufacturing activities are generally lowest in the first calendar quarter of each year, and increase progressively throughout the remainder of the year. Manufacturing output is generally strongest in the third and fourth quarters as our technology licensees increase manufacturing to prepare for the holiday buying season. Since recognition of revenues generally lags manufacturing activity by one quarter, our revenues and earnings are generally lowest in the second quarter. The introduction of new products and inclusion of our technologies in new and rapidly growing markets can distort and amplify the seasonality described above. For example, the introduction of Blu-ray Disc players may result in an overall near-term slowdown in our business as sales of DVD based products slow in anticipation of purchasing Blu-ray Disc products, but purchases of Blu-ray Disc products are in an early phase market adoption. Our revenues may continue to be subject to fluctuations, seasonal or otherwise, in the future. Unanticipated fluctuations, whether due to seasonality, economic down turns, product cycles, or otherwise, could cause us to miss our earnings projections, or could lead to higher than normal variation in short-term earnings, either of which could cause our stock price to decline.

In addition, we actively engage in intellectual property compliance and enforcement activities focused on identifying third parties who have either incorporated our technology, trademarks, or know-how without a license or who have underreported to us the amount of royalties owed under license agreements with us. As a result of these activities, from time to time, we may recognize royalty revenues that relate to manufacturing activities from prior periods and we may incur expenditures related to enforcement activity. These expenditures and royalty recoveries, as applicable, may cause revenues to be higher than expected,or net profit to be lower than expected, during a particular reporting period and may not recur in future reporting periods. Such fluctuations in our revenues and operating results may cause declines in our stock price.

Our future capital needs are uncertain and we may need to raise additional funds in the future, and such funds may not be available on acceptable terms or at all.

Our capital requirements will depend on many factors, including:

- acceptance of, and demand for, our products and technology;
- the costs of developing new products or technology;
- the extent to which we invest in new technology and research and development projects;
- the number and timing of acquisitions and other strategic transactions;
- the costs associated with our expansion, if any; and
- the costs of litigation and enforcement activities to defend our intellectual property.

In the future, we may need to raise additional funds, and such funds may not be available on favorable terms, or at all, particularly given the continuing credit crisis and downturn in the overall global economy. Furthermore, if we issue equity or debt securities to raise additional funds, our existing stockholders may experience dilution, and the new equity or debt securities may have rights, preferences, and privileges senior to those of our existing stockholders. If we cannot raise funds on acceptable terms, or at all, we may not be able to develop or enhance our products and services, execute our business plan, take advantage of future opportunities, or respond to competitive pressures or unanticipated customer requirements. This may materially harm our business, results of operations, and financial condition.

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

Even if a standards-setting body mandates our technologies for a particular market, our technologies may not be the sole technologies adopted for that market as an industry standard. Further, even when inclusion of certain of our technologies is mandated by a particular standard, market participants may choose not to implement or adopt any of our technologies beyond those required by the mandate. Our revenues and operating results depend on manufacturers choosing to adopt our technologies instead of or along with competitive technologies that may also be acceptable under industry standards. For example, the continued growth of our revenue from the Blu-ray Disc market depends upon both the continued growth of the format generally and manufacturers' choosing to incorporate our multi-channel technologies where they are an optional industry standard.

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

When a standards-setting body adopts our technologies as explicit industry standards, we generally must agree to license such technologies on a fair, reasonable and non-discriminatory basis, which we believe means that we treat similarly situated licensees similarly. In these situations, we may be required to limit the royalty rates we charge for these technologies, which could adversely affect our business. Furthermore, we may have limited control over whom we license such technologies to, and may be unable to restrict many terms of the license. From time to time, we may be subject to claims that our licenses of our industry standard technologies may not conform to the requirements of the standards-setting body. Claimants in such cases could seek to restrict or change our licensing practices or our ability to license our technologies in ways that could injure our reputation and otherwise materially and adversely affect our business, operating results and prospects.

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

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

We are dependent on our management team and technical talent.

Our success depends, in part, upon the continued availability and contributions of our management team and engineering and technical personnel because of the complexity of our products and services. Important factors that could cause the loss of key personnel include:

- our existing employment agreements with the members of our management team allow such persons to terminate their employment with us at any time;
- we do not have employment agreements with a majority of our key engineering and technical personnel;
- significant portions of the equity awards held by the members of our management team are vested; and

- equity awards held by some of our executive officers provide for accelerated vesting in the event of a sale or change of control of our company.

The loss of key personnel or an inability to attract qualified personnel in a timely manner could slow our technology and product development and harm our ability to execute our business plan.

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

From time to time, one or a small number of our customers or licensees may represent a significant percentage of our revenue. For instance, in 2009, one customer accounted for 15% of revenues from our continuing operations. Although we have agreements with many of our customers, these agreements typically do not require any material minimum purchases or minimum royalty fees and do not prohibit customers from purchasing products and services from competitors. A decision by any of our major customers or licensees not to use our technologies, or their failure or inability to pay amounts owed to us in a timely manner, or at all, could have a significant adverse effect on our business.

Unanticipated changes in our tax provisions or adverse outcomes resulting from examination of our income tax returns could adversely affect our net income.

We are subject to income taxes in both the United States and foreign jurisdictions. Our effective income tax rates have recently been and could in the future be adversely affected by changes in tax laws or interpretations of those tax laws, by changes in the mix of earnings in countries with differing statutory tax rates, or by changes in the valuation of our deferred tax assets and liabilities. Significant judgment is required in determining our worldwide provision for income taxes. In the ordinary course of our business, there are many transactions and calculations where the ultimate tax determination is uncertain. We may come under audit by tax authorities. For instance, the Internal Revenue Service is examining our 2005 to 2007 federal income tax returns, including certain prior period carryforwards, and the State of California is examining our 2004 and 2005 corporate tax returns. Although we believe our tax estimates are reasonable, the final determination of tax audits and any related litigation could be materially different from our historical income tax provisions and accruals. Based on the results of an audit or litigation, a material effect on our income tax provision, net income or cash flows in the period or periods for which that determination is made could result. In addition, changes in tax rules may adversely affect our future reported financial results or the way we conduct our business. For example, we consider the operating earnings of our foreign subsidiaries to be invested indefinitely outside the United States. We have not provided for United States federal or foreign withholding taxes that may result on future remittances of undistributed earnings of foreign subsidiaries. Our future reported financial results may be adversely affected if tax or accounting rules regarding unrepatriated earnings change.

Current and future governmental and industry standards may significantly limit our business opportunities.

Technology standards are important in the audio and video industry as they help to assure compatibility across a system or series of products. Generally, standards adoption occurs on either a mandatory basis, requiring a particular technology to be available in a particular product or medium, or an optional basis, meaning that a particular technology may be, but is not required to be, utilized. For example, both our digital multi-channel audio technology and Dolby's have optional status in DVD based products and Blu-ray Disc. In the standard for Blu-ray Disc, both DTS and Dolby technologies have been selected as mandatory standards for two-channel output. However, if either or both of these standards are re-examined or a new standard is developed, we may not be included as mandatory in any such new or revised standard which would cause revenue growth in our consumer business to be significantly lower than expected and could have a material adverse affect on our business.

Various national governments have adopted or are in the process of adopting standards for all digital television broadcasts, including cable, satellite, and terrestrial. In the United States, Dolby's audio technology has been selected as the sole, mandatory audio standard for terrestrial digital television broadcasts. As a result, the audio for all digital terrestrial television broadcasts in the United States must include Dolby's technology and must exclude any other format, including ours. We do not know whether this standard will be reopened or amended. If it is not, our audio technology may never be included in that standard. Certain large and developing markets, such as China, have not fully developed their digital television standards. Our technology may or may not ultimately be included in these standards.

As new technologies and entertainment media emerge, new standards relating to these technologies or media may develop. New standards may also emerge in existing markets that are currently characterized by competing formats, such as the market for personal computers. We may not be successful in our efforts to include our technology in any such standards.

We may not successfully address problems encountered in connection with any acquisitions.

We expect to consider opportunities to acquire or make investments in other technologies, products, and businesses that could enhance our technical capabilities, complement our current products and services, or expand the breadth of our markets. We have a limited history of acquiring and integrating businesses. Acquisitions and strategic investments involve numerous risks, including:

- problems assimilating the purchased technologies, products, or business operations;
- significant future charges relating to in-process research and development and the amortization of intangible assets;
- significant amount of goodwill that is not amortizable and is subject to annual impairment review;
- problems maintaining uniform standards, procedures, controls, and policies;
- unanticipated costs associated with the acquisition, including accounting and legal charges, capital expenditures, and transaction expenses;
- diversion of management's attention from our core business;
- adverse effects on existing business relationships with suppliers and customers;
- risks associated with entering markets in which we have no or limited prior experience;
- unanticipated or unknown liabilities relating to the acquired businesses;
- the need to integrate accounting, management information, manufacturing, human resources and other administrative systems to permit effective management; and
- potential loss of key employees of acquired organizations.

If we fail to properly evaluate and execute acquisitions and strategic investments, our management team may be distracted from our day-to-day operations, our business may be disrupted, and our operating results may suffer. In addition, if we finance acquisitions by issuing equity or convertible debt securities, our existing stockholders would be diluted. Foreign acquisitions involve unique risks in addition to those mentioned above, including those related to integration of operations across different geographies, cultures and languages, currency risks and risks associated with the particular economic, political and regulatory environment in specific countries. Also, the anticipated benefit of our acquisitions may not materialize, whether because of failure to obtain stockholder approval or otherwise. Future acquisitions could result in potentially dilutive issuances of our equity securities, the incurrence of debt, contingent liabilities or amortization expenses, or write-offs of goodwill, any of which could harm our operating results or financial condition. Future acquisitions may also require us to obtain additional equity or debt financing, which may not be available on favorable terms or at all.

We may have difficulty managing any growth that we might experience.

As a result of a combination of internal growth and growth through acquisitions, we expect to continue to experience growth in the scope of our operations and the number of our employees. If our growth continues, it may place a significant strain on our management team and on our operational and financial systems, procedures, and controls. Our future success will depend in part on the ability of our management team to manage any growth effectively. This will require our management to:

- hire and train additional personnel in the United States and internationally;
- implement and improve our operational and financial systems, procedures, and controls;
- maintain our cost structure at an appropriate level based on the revenues we generate;
- manage multiple concurrent development projects; and
- manage operations in multiple time zones with different cultures and languages.

Any failure to successfully manage our growth could distract management's attention, and result in our failure to execute our business plan.

Risks Related to Our Common Stock

We expect that the price of our common stock will fluctuate substantially.

The market price of our common stock is likely to be highly volatile and may fluctuate substantially due to many factors, including:

- actual or anticipated fluctuations in our results of operations;
- market perception of our progress toward announced objectives;
- announcements of technological innovations by us or our competitors or technology standards;
- announcements of significant contracts by us or our competitors;
- changes in our pricing policies or the pricing policies of our competitors;
- developments with respect to intellectual property rights;
- the introduction of new products or product enhancements by us or our competitors;
- the commencement of or our involvement in litigation;
- resolution of significant litigation in a manner adverse to our business;
- our sale or purchase of common stock or other securities in the future;
- conditions and trends in technology industries;
- changes in market valuation or earnings of our competitors;
- the trading volume of our common stock;
- announcements of potential acquisitions;

- the adoption rate of new products incorporating our or our competitors' technologies, including Blu-ray Disc players;
- changes in the estimation of the future size and growth rate of our markets; and
- general economic conditions.

In addition, the stock market in general, and the Nasdaq Global Select Market and the market for technology companies in particular, has experienced extreme price and volume fluctuations that have often been unrelated or disproportionate to the operating performance of those companies. Further, the market prices of securities of technology companies have been particularly volatile. These broad market and industry factors may materially harm the market price of our common stock, regardless of our operating performance. In the past, following periods of volatility in the market price of a company's securities, securities class-action litigation has often been instituted against that company. Such litigation, if instituted against us, could result in substantial costs and a diversion of management's attention and resources.

Shares of our common stock are relatively illiquid.

As a result of our relatively small public float, our common stock may be less liquid than the common stock of companies with broader public ownership. Among other things, trading of a relatively small volume of our common shares may have a greater impact on the trading price for our shares than would be the case if our public float were larger.

Anti-takeover provisions under our charter documents and Delaware law could delay or prevent a change of control and could also limit the market price of our stock.

Our Restated Certificate of Incorporation and Restated Bylaws contain provisions that could delay or prevent a change of control of our company or changes in our Board of Directors that our stockholders might consider favorable. Some of these provisions:

- authorize the issuance of preferred stock which can be created and issued by the Board of Directors without prior stockholder approval, with rights senior to those of the common stock;
- provide for a classified Board of Directors, with each director serving a staggered three-year term;
- prohibit stockholders from filling Board vacancies, calling special stockholder meetings, or taking action by written consent; and
- require advance written notice of stockholder proposals and director nominations.

In addition, we are governed by the provisions of Section 203 of the Delaware General Corporate Law, which may prohibit certain business combinations with stockholders owning 15% or more of our outstanding voting stock. These and other provisions in our Restated Certificate of Incorporation, Restated Bylaws and Delaware law could make it more difficult for stockholders or potential acquirors to obtain control of our Board or initiate actions that are opposed by the then-current Board, including delay or impede a merger, tender offer, or proxy contest involving our company. Any delay or prevention of a change of control transaction or changes in our Board could cause the market price of our common stock to decline.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

(c) Purchases of Equity Securities by the Issuer and Affiliated Purchasers

Stock repurchase activity during the quarter ended June 30, 2010 was as follows:

Period	Total Number of Shares Purchased(1)	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plan	Maximum Number of Shares that May Yet Be Purchased Under the Plan
April 1, 2010 through April 30, 2010	—	—	—	615,000
May 1, 2010 through May 31, 2010	372,134	$33.65	350,020	264,980
June 1, 2010 through June 30, 2010	71,312	$33.16	71,312	193,668
Total	443,446	$33.57(2)	421,332	193,668

Notes:

(1) Consists of shares repurchased in open-market transactions pursuant to an authorization by our Board of Directors that we previously announced. In November 2009, our Board of Directors authorized us to repurchase up to one million shares of our common stock in the open market or in privately negotiated transactions, depending upon market conditions and other factors. Also consists of shares repurchased and retired from employees to satisfy statutory withholding requirements upon the vesting of restricted stock.

(2) Represents weighted average price paid per share during the quarter ended June 30, 2010.

Item 3. Defaults Upon Senior Securities

None.

Item 4. (Removed and Reserved)

Item 5. Other Information

None.

Item 6. Exhibits

Exhibit Number	Exhibit Description
10.1	Amendment to Employment Agreement by and between the Registrant and Brian D. Towne, executed June 28, 2010#
10.2	2003 Equity Incentive Plan, as amended on May 9, 2005, May 15, 2008, February 19, 2009, February 15, 2010 and June 3, 2010#
31.1	Certification of the Chief Executive Officer under Securities Exchange Act Rules 13a-14(a) or 15d-14(a)
31.2	Certification of the Chief Financial Officer under Securities Exchange Act Rules 13a-14(a) or 15d-14(a)
32.1	Certification of the Chief Executive Officer under Securities Exchange Act Rules 13a-14(b) or 15d-14(b) and 18 U.S.C. 1350*
32.2	Certification of the Chief Financial Officer under Securities Exchange Act Rules 13a-14(b) or 15d-14(b) and 18 U.S.C. 1350*

# Indicates management contract, arrangement or compensatory plan.

* This certification is being furnished solely to accompany this report pursuant to 18 U.S.C. 1350, and is not being filed for purposes of Section 18 of the Securities Exchange Act of 1934, and is not to be incorporated by reference into any filing of the Company, whether made before or after the date hereof, regardless of any general incorporation language in such filing.

SIGNATURES

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

DTS, Inc.

by: /s/ JON E. KIRCHNER

Jon E. Kirchner
Chairman and Chief Executive Officer
(Duly Authorized Officer)

Date: August 9, 2010

by: /s/ MELVIN L. FLANIGAN

Melvin L. Flanigan
Executive Vice President, Finance and
Chief Financial Officer
(Principal Financial and Accounting Officer)

Date: August 9, 2010

EXHIBIT INDEX

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EXHIBIT 31.1

CERTIFICATION PURSUANT TO SECURITIES ACT RULES 13a-14(a) OR 15d-14(a)

I, Jon E. Kirchner, certify that:

1. I have reviewed this quarterly report on Form 10-Q of DTS, Inc.;

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

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

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

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

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

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

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

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

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

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

Date: August 9, 2010

By: /s/ JON E. KIRCHNER

Jon E. Kirchner
Chairman and Chief Executive Officer

EXHIBIT 31.2

CERTIFICATION PURSUANT TO SECURITIES ACT RULES 13a-14(a) OR 15d-14(a)

I, Melvin L. Flanigan, certify that:

1. I have reviewed this quarterly report on Form 10-Q of DTS, Inc.;

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

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

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

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

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

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

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

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

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

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

Date: August 9, 2010

By: /s/ MELVIN L. FLANIGAN

Melvin L. Flanigan
Chief Financial Officer

EXHIBIT 32.1

CERTIFICATION PURSUANT TO SECURITIES EXCHANGE ACT RULES 13a-14(b) OR 15d-14(b) AND 18 U.S.C. SECTION 1350

In connection with the quarterly report on Form 10-Q of DTS, Inc. (the "Company") for the quarterly period ended June 30, 2010 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Jon E. Kirchner, Chairman and Chief Executive Officer of the Company, hereby certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

(1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: August 9, 2010

By: /s/ JON E. KIRCHNER

Jon E. Kirchner
Chairman and Chief Executive Officer

A signed original of this written statement required by Section 906 of the Sarbanes-Oxley Act of 2002 has been provided to DTS, Inc. and will be retained by DTS, Inc. and furnished to the Securities and Exchange Commission upon request.

EXHIBIT 32.2

CERTIFICATION PURSUANT TO SECURITIES EXCHANGE ACT RULES 13a-14(b) OR 15d-14(b) AND 18 U.S.C. SECTION 1350

In connection with the quarterly report on Form 10-Q of DTS, Inc. (the "Company") for the quarterly period ended June 30, 2010 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Melvin L. Flanigan, Chief Financial Officer of the Company, hereby certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

(1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: August 9, 2010

By: /s/ MELVIN L. FLANIGAN

Melvin L. Flanigan
Chief Financial Officer

A signed original of this written statement required by Section 906 of the Sarbanes-Oxley Act of 2002 has been provided to DTS, Inc. and will be retained by DTS, Inc. and furnished to the Securities and Exchange Commission upon request.