

Securities Regulation Daily Wrap Up, TOP STORY—N.D. Cal.: HP shareholders fail to plead fraud related to former CEO Mark Hurd's harassment scandal, (Aug. 12, 2013)

Securities Regulation Daily Wrap Up

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By Matthew Garza, J.D.

Hewlett Packard (HP) shareholders failed to plead fraud against the company and its former CEO Mark Hurd sufficiently to overcome a motion to dismiss but were granted leave to cure the deficiencies in their complaint by the federal district court in San Francisco ([Cement & Concrete Workers District Council Pension Fund v. Hewlett Packard Company](#), August 9, 2013, Tigar, J.).

Scandal. The suit was filed after a drop in the price of HP stock occurred after a sexual harassment scandal involving Hurd and an independent consultant hit the news, leading to Hurd's resignation. The court noted that the day the HP board announced Hurd's departure, August 6, 2010, the stock traded at \$46 per share. The day the first amended complaint was filed two years later, it traded at approximately \$14.

Shareholders alleged that the company was recovering from a 2006 scandal and that Hurd's commitment to ethical conduct was key to success of the company. His failure to live up to company standards allegedly cost billions of dollars of market capitalization. After the 2006 scandal, the complaint alleged, investors relied on Hurd's statements in congressional testimony, press releases, and public letters to HP employees that he was seeking to restore public trust by establishing high ethical standards.

False and misleading statements. The class, made of up of purchasers of HP stock who purchased between November 13, 2007, and August 6, 2010, alleged that HP and Hurd made false and misleading statements when they issued and updated HP's Standards of Business Conduct Brochure (SBC) in 2006, 2008, and 2010, as well as in HP's 10-K and 10-Q, throughout the class period.

When Hurd made statements that he made a commitment "to build trust in everything we do by living our values and conducting business consistent with the high ethical standards embodied within our SBC" and that "[w]e are open, honest, and direct in all our dealings," he was in violation of the company's SBC, shareholders alleged. "These statements were misleading because in light of Hurd's endorsement of these tenets, there was an implication that Hurd was in fact in compliance with them," according to the complaint. Although the SBC was directed primarily at HP's employees, investors alleged that the intended audience of the 2008 and 2010 SBC amendments also included Wall Street, HP shareholders, and potential investors. Statements made in the risk factors section of HP's 10-K also said the loss of key employees could factor into the company's success and created a duty to disclose Hurd's conduct.

Puffery. The court initially held that the SBC statements, and alleged omissions from them, were mere puffery and not grounds for a fraud action. The fact that investors were looking for these types of statements after the 2006 scandal did not distinguish them from previous authority finding corporate ethics statements to be vague, generalized, and unspecific assertions of corporate optimism. "[N]otwithstanding the 2006 scandal, it remains the case that the statements Plaintiff identifies as material misrepresentations in the SBCs are 'so general that a reasonable investor would not depend on [them] as a guarantee that [HP] would never take a step that might adversely affect its reputation.'" The risk factors disclosed in HP's 10-Ks also did not create a duty to disclose Hurd's conduct, according to the court.

Other elements. The court also held that the shareholders failed to establish the falsity of the company's SBC, instead arguing "in general terms" that Hurd was engaged in unethical conduct at the time the SBCs were written. Scienter on Hurd's part was sufficiently pleaded, assuming materiality could be established, according

to the court, but scienter on the part of the company could not be established at this stage of the litigation. The court also said that a finding on causation was premature on a motion to dismiss.

The case is [No. 12-cv-04115-JST](#).

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Companies: Hewlett Packard Company

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