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# The Story of Hewlett-Packard

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## INTRODUCTION: THE STORY OF HEWLETT-PACKARD

*Barbara Black\**

A bedrock principle of corporate governance is that the board of directors acts as a collective body to promote better decision-making. A frequently-cited treatise states the principle thusly: “[t]he board of directors is a collegial body that, for the most part, is expected to make decisions by consensus.”<sup>1</sup> As an illustration of the importance of this principle, courts defer to board actions, even those involving a considerable outlay of cash, that are undertaken “to resolv[e] an internal rift in management of serious proportions and at the highest executive level.”<sup>2</sup>

Collegial, informed decision-making requires that directors can trust that their fellow directors will maintain the confidentiality of their deliberations. Moreover, serious adverse legal ramifications can result from unauthorized disclosures of corporate information.<sup>3</sup> Accordingly, a director owes the corporation a duty of confidentiality which is an aspect of the director’s more general duty to act in good faith and in the best interests of the corporation.<sup>4</sup>

Nevertheless, headlines frequently provide examples of corporate boards that do not live up to the model of collegiality. Hewlett-Packard Co. (HP) is a recent, well-publicized example of a dysfunctional board. For many years HP was a well-respected corporation known for its “William Hewlett/Dave Packard Way.” Bitter divisions developed on the board of directors, however, under the leadership of Carly Fiorina, HP’s first outside CEO. Fiorina was hired in 1999 as an agent of change to revive the company. Her centralization of power and cost-cutting

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1. STEPHEN M. BAINBRIDGE, CORPORATE LAW § 5.4B.1, at 76 (2d ed., 2009).

2. *Grobow v. Perot*, 539 A.2d 180, 191 (Del. 1988) (according business judgment rule presumption to GM board’s purchase of its stock owned by Ross Perot). Similarly, courts do not view “group think” as a serious danger. *See Beam v. Stewart*, 845 A.2d 1040, 1050–51 (Del. 2004) (rejecting plaintiff’s “structural bias” argument).

3. AMERICAN BAR ASSOCIATION, CORPORATE DIRECTOR’S HANDBOOK 78–79 (4th ed., 2004) (discussing impact of Regulation FD on corporate policies regarding the persons who are authorized to communicate with the public).

4. *Id.* at 10–11.

measures created resentment within the company, as did her image as a “Rock Star CEO.”<sup>5</sup> In 2002 she pushed through a controversial Compaq merger that Walter Hewlett, a director and son of co-founder William Hewlett, fiercely opposed. In January 2005, and again in January 2006, confidential discussions at the annual directors’ retreats were leaked to the press. An investigation after the first leak did not determine the source.<sup>6</sup> After the second leak, the board of directors put heavy pressure on Patricia C. Dunn, who was appointed the nonexecutive chair of the board after Fiorina was fired in February 2005,<sup>7</sup> to find the source of the leaks. As she testified to a Congressional subcommittee, “the majority of directors told me during my first few weeks as Chairman that, next to leading the Board’s CEO search, coming to grips with HP’s famously leaky Board should be my top priority.”<sup>8</sup> The investigation that she authorized did discover, by May 2006, the source of the second leak, Dr. George A. Keyworth II,<sup>9</sup> but HP paid a heavy price for this knowledge. In fall 2006, HP became embroiled in headline-grabbing scandal and disgrace after another director, Thomas J. Perkins, disclosed to the SEC and California authorities that the investigators used possibly illegal and certainly unethical techniques to obtain information about HP directors and employees as well as journalists. These methods included “pretexting” to obtain personal telephone records, sending an email to a journalist that had an attached tracing mechanism, and surveillance of the individuals.<sup>10</sup>

All HP directors and employees are subject to the company’s Standards of Business Conduct that require prior approval before

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5. See Pui-Wing Tam, *Hewlett-Packard Board Considers a Reorganization*, WALL ST. J., Jan. 24, 2005.

6. *Hewlett-Packard’s Pretexting Scandal: Hearing Before the Subcomm. on Oversight and Investigations of the H. Comm. on Energy and Commerce*, 109th Cong. 45 (2006) [hereinafter *Hearing*] (prepared statement of Patricia C. Dunn, Former Chairman of the Board, Hewlett-Packard Co.), available at [http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=109\\_house\\_hearings&docid=f:31472.pdf](http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=109_house_hearings&docid=f:31472.pdf).

7. See Pui-Wing Tam, *H-P’s Board Ousts Fiorina as CEO*, WALL ST. J., Feb. 10, 2005, available at <http://online.wsj.com/article/SB110795431536149934.html>.

8. *Hearing*, *supra* note 6, at 45 (prepared statement of Patricia C. Dunn, Former Chairman of the Board, Hewlett-Packard Co.).

9. Keyworth had been a director since 1986, the longest serving director. See Hewlett Packard Co., 2005 Definitive Proxy Statement, at 16–17 (2004). He had served as Science Advisor to the President and Director of the White House’s Office of Science and Technology Policy under President Reagan. *Id.* at 17.

10. See HEWLETT PACKARD CO., Annual Report (Form 8-K), at 2 (Sept. 6, 2006). See also Alan Murray, *H-P Board Clash over Leaks Triggers Angry Resignation*, WALL ST. J., Sept. 6, 2006, at A1, available at [http://online.wsj.com/article/SB115749453036454340.html?mod=home\\_whats\\_news\\_us](http://online.wsj.com/article/SB115749453036454340.html?mod=home_whats_news_us). A chronology of the key events is also available. See *Tracking the H-P Controversy*, WSJ.COM, 2006, <http://online.wsj.com/public/resources/documents/info-hptime0609.html>.

granting interviews or providing comments to the press.<sup>11</sup> Moreover, even if a director sincerely believes that management's policies are misguided, the solution is not to leak confidential information to the press; instead, the director should work to change management's policies or management.<sup>12</sup> What confluence of events caused at least one HP director to breach his obligation to maintain the confidentiality of corporate information?<sup>13</sup> What, in turn, drove the board chair to think it was acceptable conduct to spy on her fellow directors? As described by HP's CEO Mark Hurd, when he was called before Congress to testify about these events: "What began as a proper and serious inquiry of leaks to the press of sensitive company information [from within the HP board] became a rogue investigation that violated [HP's] own principles and values."<sup>14</sup>

Hewlett-Packard presents a cautionary tale of the damage caused by distrust and dissension within the boardroom. At the March 14, 2008 symposium, eight scholars tackled the broader issues suggested by the HP story to explore the causes of dysfunctional boards and attempt to formulate some possible cures. I am proud to introduce the participants' Articles, each of which is an important contribution to the scholarship in this area. In this introduction, I will summarize the papers and periodically return to the HP story to relate their analysis to its facts.

In starting off the symposium, Professor Gevurtz provides two important reminders: first, complaints about board performance are neither new nor limited to U.S. corporations<sup>15</sup> and, second, the quintessential question—what is the function of boards?—remains unanswered.<sup>16</sup> Accordingly, he suggests that perhaps the best solution is

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11. HP STANDARDS OF BUSINESS CONDUCT § 8.5 (2006) [hereinafter SBC 2006], available at [http://media.corporate-ir.net/media\\_files/irol/71/71087/corpgov/sbcbrochure2006.pdf](http://media.corporate-ir.net/media_files/irol/71/71087/corpgov/sbcbrochure2006.pdf). See also HP STANDARDS OF BUSINESS CONDUCT 7–8, 14 (2008), available at <http://www.hp.com/hpinfo/globalcitizenship/csr/sbcbrochure.pdf>.

12. SBC 2006, *supra* note 11, at 22–23.

13. Other corporations have also suffered from leaky boards. In 2007, Dow Chemical announced that it had fired two senior executives, one of whom was a director, for allegedly engaging in unauthorized talks to sell the company. See Jeffrey Ball, Dennis K. Berman, & Joann S. Lublin, *Officials Fired at Dow Chemical for Secret Talks*, WALL ST. J., Apr. 13, 2007, at A1, available at [http://online.wsj.com/article\\_print/SB117638449048167683.html](http://online.wsj.com/article_print/SB117638449048167683.html).

14. Hearing, *supra* note 6, at 728 (testimony of Mark Hurd, President, Chief Executive Officer, and Chairman of the Board, Hewlett-Packard, Co.). Describing it as a "rogue investigation" may be self-serving, as Miriam Baer points out. See Miriam Hechler Baer, *Corporate Policing and Corporate Governance: What Can We Learn from Hewlett Packard's Pretexting Scandal?*, 77 U. CIN. L. REV. 523, 531, 535 (2008).

15. Franklin A. Gevurtz, *The Function of "Dysfunctional" Boards*, 77 U. CIN. L. REV. 391 (2008).

16. *Id.* at 398 (reviewing with skepticism the classic explanations: managing, monitoring, and mediating).

to take a minimalist approach toward the question of the board's function. Professor Gevurtz goes back to the board's origins in the English trading companies as a way of providing political legitimacy through a representative body and argues that, rather than being dysfunctional, the internal strife among the HP directors might simply have reflected dissension among the shareholders that had to be worked through.

Four articles deal with various attributes of directors as they relate to the optimal composition and appropriate functions of the board. They present a number of thorny questions, including:

- How can the board identify and deal with common pathologies of corporate leaders;
- What is the impact of racial, ethnic and gender diversity on the board;
- What is the appropriate balance between expert and generalist directors;
- What is the appropriate role for the board—advisor or supervisor, or some mix of the two.

Professor Barnard identifies five recurring pathologies among corporate leaders—narcissism, over-optimism, fear, anger and depression—and considers the impact of these pathologies on the leader's organization.<sup>17</sup> While she acknowledges that some of these pathologies may contribute to a corporate leader's success, unchecked dysfunction at the top can nevertheless have harmful consequences for the organization. For example, Professor Barnard suggests that defensiveness and inflexibility inspired by fear may have caused Fiorina to undertake the Compaq merger alone—a deal that may have been beyond her competence to manage.<sup>18</sup>

Professor Barnard sets forth a number of solutions. Specifically, she proposes that the board of directors, consistent with its oversight responsibility, should (1) understand how pathologies may influence CEO behavior, (2) recognize whether the corporation's CEO is behaving pathologically and assess the negative impact on the organization, and, most importantly (3) determine an appropriate plan for dealing with the effects of the pathology. In addition, because directors may have difficulty in identifying pathologies that they themselves may be prone to, boards should institute, as a regular agenda item, a “pathology audit” for senior executives.<sup>19</sup>

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17. Jayne W. Barnard, *Narcissism, Over-Optimism, Fear, Anger and Depression: The Interior Life of Corporate Leaders*, 77 U. CIN. L. REV. 405 (2008).

18. *Id.* at 424 & n.115.

19. *Id.* at 428.

Professors Broome and Krawiec next discuss preliminary findings from their initial interviews with twenty-four public company board members,<sup>20</sup> conducted as part of a larger qualitative study on the impact of board diversity on corporate performance. Their preliminary findings are consistent with past research showing that corporations have sought out females and minorities for the purpose of increasing board diversity. In examining why corporations think diversity on the board is important, the authors focus on the rationale frequently mentioned in the interviews: signaling theory. Specifically, corporations may add diversity to their boards to send a message to relevant audiences. The message may be targeted to the workforce (equal opportunity in the workplace), consumers (attention to the needs of women and minorities in product and service development), or, more abstractly, to the general public, to demonstrate that the corporation is “progressive” or “forward-looking.” The authors note, however, that signaling can be intentionally deceptive if the costs of mimicking are low.<sup>21</sup>

In his review of the empirical literature in financial accounting, Professor Cunningham focuses on the attributes or skills that directors should bring to the task.<sup>22</sup> After placing in historical context the ascendancy of independence as the director’s most important attribute, despite the lack of evidence showing a strong correlation between independence and improved corporate performance, the author sets forth the emerging appeal for expertise, particularly accounting expertise as a result of Enron and other financial accounting scandals, and Sarbanes-Oxley Act of 2002 (SOX).<sup>23</sup> Professor Cunningham notes that the empirical evidence shows a strong positive correlation between independence and financial reporting quality when accounting experts serve on audit committees. This evidence suggests that the law should encourage, if not require, the appointment of accounting experts to audit committees and should encourage their active engagement in real earnings management. The judicial response, however, has been to the contrary. While courts consistently defer to the judgment, and protect the business decisions, of incompetent independent directors, they provide no safe harbor for directors who contribute their expertise to the decision-making process and, in fact, may penalize them for their

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20. Lissa Lamkin Broome & Kimberly D. Krawiec, *Signaling Through Board Diversity: Is Anyone Listening?*, 77 U. CIN. L. REV. 431 (2008).

21. *Id.* at 449–50.

22. Lawrence A. Cunningham, *Rediscovering Board Expertise: Legal Implications of the Empirical Literature*, 77 U. CIN. L. REV. 465 (2008).

23. Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, § 301, 116 Stat. 745, 775 (codified as amended at 15 U.S.C. § 78j-1(m)(2) (2007)).

expertise. Returning to a theme introduced by Professor Gevurtz, Professor Cunningham concludes by noting the lack of consensus as to “what independent directors are supposed to do.”<sup>24</sup>

Professor Frankel observes that one important condition for a well-functioning board is for the directors to understand and agree upon the board’s objectives and roles.<sup>25</sup> Her paper examines two different roles for the board—advisors to the CEO or supervisors of the CEO—and the importance of the board’s establishing the appropriate balance between them within the corporation’s culture. Frequently, however, these understandings are assumed and only worked through in times of corporate crisis. In addition, because of its dependence on management for information, the board must trust the CEO far more than the CEO must trust the board. Professor Frankel notes that the strength of the HP culture, exemplified not by the board but by the employees, allowed the corporation to survive its crisis.

The HP story suggests that the efforts to diversify the HP board (with respect to both gender and expertise) contributed to its dysfunctionality. Patricia Dunn, the nonexecutive Chair, was invited to join the board in 1998 (one year before Carly Fiorina became CEO) as a “fresh face” and because of her financial and corporate governance expertise.<sup>26</sup> At the time she joined the board, the only other woman on the 14-person board was a member of the Packard family.<sup>27</sup> Dunn was described as bringing a “careful, rules-based approach to life.”<sup>28</sup> As such, she was a contrast to wealthy venture capitalist Tom Perkins, another HP director, described as a “boisterous Silicon Valley legend, in love with fast cars, large sailboats and getting his own way.”<sup>29</sup> Dunn said that she was appointed non-executive chair in 2005 because she “was one of the few directors who was still talking to everyone.”<sup>30</sup> Since she saw her role as moving the board from a “founder’s board” to a “modern fully professional board,” perhaps it is not surprising that conflicts developed between

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24. Cunningham, *supra* note 22, at 499.

25. Tamar Frankel, *Corporate Boards of Directors: Advisors or Supervisors?*, 77 U. CIN. L. REV. 501 (2008).

26. George Anders & Alan Murray, *Behind H-P Chairman's Fall, Clash with a Powerful Director*, WALL ST. J., Oct. 9, 2006, at A1, available at <http://online.wsj.com/article/SB116036136420086488.html>.

27. Dunn had been CEO at Barclay Global Investors, an international institutional investment manager. Hewlett-Packard Co., 1999 Proxy Statement (Form DEF 14A), at 6 (1998), available at <http://www.sec.gov/Archives/edgar/data/47217/0001047469-99-000720.txt>.

28. Anders & Murray, *supra* note 26.

29. *Id.*

30. *Id.*

Dunn and Perkins and that a “respect gap” existed.<sup>31</sup> According to another HP director, Perkins’s behavior toward Dunn was “chairman abuse.”<sup>32</sup>

Dunn testified that, prior to the identification of Keyworth as the source of the 2006 leak, Perkins pressured her not to disclose the name of the leaker to the full board and that Perkins felt betrayed when, against his wishes, the board was told it was Keyworth.<sup>33</sup> Perkins was also upset that he was not told the identity of the leaker in advance of the board meeting. Instead, before the board meeting, Dunn shared the information with the audit committee, which oversees the Standards of Business Conduct, and not with the nominating and governance committee, which was headed by Perkins.<sup>34</sup> Dunn believed this was “very sensitive” because Perkins and Keyworth were close friends and allies on the board. Although the board requested Keyworth to resign, he refused to do so. Perkins, however, resigned in protest over the identification of Keyworth; Perkins’s subsequent public disclosure of the questionable investigative tactics set in motion the public outcry that led to Dunn’s downfall.

The HP board’s dysfunctionality may also have stemmed, in part, from its failure to achieve agreement on the board as to its appropriate role. Keyworth and Perkins, as longtime HP directors deeply versed in the technology, appeared to disparage the importance of corporate governance and financial expertise that Dunn represented, contributing to a board culture prone to “destructive criticism, personality clashes and infighting.”<sup>35</sup>

With the final two papers, the symposium turns to the board’s role to ensure the corporation’s compliance with the law. Professor Baer uses the HP pretexting scandal to explore the largely unexplored conflict between corporate policing and corporate governance.<sup>36</sup> Building on both corporate governance and law enforcement scholarship, she sets forth the tension between corporate governance norms and the board’s responsibility to oversee its internal compliance department, a tension that is exacerbated in the post-SOX era where government expects corporations to be its partner in ferreting out corporate crime. Dunn’s description, when she defended the investigative techniques used to

31. *Id.*

32. *Id.*

33. Hearing, *supra* note 6, at 64–68 (prepared statement of Patricia C. Dunn, Former Chairman of the Board, Hewlett-Packard Co.).

34. *Id.* See Murray, *supra* note 10.

35. Frankel, *supra* note 25, at 513.

36. Baer, *supra* note 14, at 535–36.



discover the source of the board leak as “old-fashioned detective work,”<sup>37</sup> accurately describes public law enforcement practices that routinely use deception to obtain information. The use of deception and spying on corporate directors does not, however, (to state the obvious) promote the values of loyalty, trust, and transparency that are considered fundamental to good corporate governance. Nevertheless, in the face of pressure to determine the source of the leaks, perhaps it should not be so surprising that Dunn condoned the use of deceptive tactics routinely used in police investigations. Moreover, as corporate compliance departments increasingly are viewed as “private attorneys general,” boards may feel similar pressure in the face of government demands to cooperate in their investigations. Beyond the pretexting scandal, Professor Baer observes that there are currently “no universally enforceable standards for corporate internal investigations and few mechanisms in place to monitor corporate investigations.”<sup>38</sup> For those who take corporate governance seriously, this raises the disturbing likelihood that the HP pretexting scandal is not likely to be an isolated problem. Boards will only become more dysfunctional if directors feel the need to spy and deceive each other.

Finally, Professor Henning examines how boards respond to threats of corporate criminal liability.<sup>39</sup> In reviewing four recent instances (Enron, Chiquita, United Healthcare and Staples), he finds that responses by boards are frequently insufficient to effect a change in the corporate culture that would prevent future violations. He recommends that, in dealing with charges of serious wrongdoing, the board should appoint a special committee of truly independent directors to manage the crisis and follow the procedures set forth in *Zapata Corp. v. Maldonado*<sup>40</sup> in order to promote a well-considered and thorough response.

With the development of the modern corporation, corporate boards have been the locus of corporate authority, and particularly since the 1980s, boards and their performance have been under intense scrutiny. Nevertheless, corporate law has not developed a consistent theory for what boards are supposed to do; instead, it sends mixed messages about the functions and expectations of boards and the appropriate people to sit on them. The HP saga illustrates some of the dilemmas faced by directors confronted by these competing pressures.

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37. Hearing, *supra* note 6, at 62 (prepared statement of Patricia C. Dunn, Former Chairman of the Board, Hewlett-Packard Co.).

38. Baer, *supra* note 14, at 572.

39. Peter J. Henning, *Board Dysfunction: Dealing with the Threat of Corporate Criminal Liability*, 77 U. CIN. L. REV. 585 (2008).

40. 430 A.2d 779 (Del. 1981).