HEWLETT PACKARD CO
Form 10-Q
March 10, 2009

QuickLinks -- Click here to rapidly navigate through this document

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended: January 31, 2009

Or

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

For the transition period from to

Commission file number 1-4423

HEWLETT-PACKARD COMPANY

(Exact name of registrant as specified in its charter)

Delaware	**94-1081436**
(State or other jurisdiction of incorporation or organization)	(I.R.S. employer identification no.)
3000 Hanover Street, Palo Alto, California	**94304**
(Address of principal executive offices)	(Zip code)

(650) 857-1501

(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 (the "Exchange Act") 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 ý No o

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.

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

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

The number of shares of HP common stock outstanding as of February 28, 2009 was 2,396,613,014 shares.

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES
INDEX

Forward-Looking Statements

This Quarterly Report on Form 10-Q, including "Management's Discussion and Analysis of Financial Condition and Results of Operations" in Item 2 of Part I of this report, contains forward-looking statements that involve risks, uncertainties and assumptions. If the risks or uncertainties ever materialize or the assumptions prove incorrect, the results of Hewlett-Packard Company and its consolidated subsidiaries ("HP") may differ materially from those expressed or implied by such forward-looking statements and assumptions. All statements other than statements of historical fact are statements that could be deemed forward-looking statements, including but not limited to any projections of revenue, margins, expenses, tax provisions, earnings, cash flows, benefit obligations, share repurchases, acquisition synergies, currency exchange rates or other financial items; any statements of the plans, strategies and objectives of management for future operations, including the execution of cost reduction programs and restructuring and integration plans; any statements concerning expected development, performance or market share relating to products or services; any statements regarding future economic conditions or performance; any statements regarding pending investigations, claims or disputes; any statements of expectation or belief; and any statements of assumptions underlying any of the foregoing. Risks, uncertainties and assumptions include macroeconomic and geopolitical trends and events; the execution and performance of contracts by HP and its customers, suppliers and partners; the challenge of managing asset levels, including inventory; the difficulty of aligning expense levels with revenue changes; assumptions related to pension and other post-retirement costs; expectations and assumptions relating to the execution and timing of cost reduction programs and restructuring and integration plans; the possibility that the expected benefits of business combination transactions may not materialize as expected; the resolution of pending investigations, claims and disputes; and other risks that are described herein, including but not limited to the items discussed in "Factors that Could Affect Future Results" set forth in "Management's Discussion and Analysis of Financial Condition and Results of Operations" in Item 2 of Part I of this report, and that are otherwise described from time to time in HP's Securities and Exchange Commission reports, including HP's Annual Report on Form 10-K for the fiscal year ended October 31, 2008. HP assumes no obligation and does not intend to update these forward-looking statements.

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements.

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Consolidated Condensed Statements of Earnings

(Unaudited)

	Three months ended January 31	
	2009	2008[1]
	In millions, except per share amounts	
Net revenue:		
Products	$ 18,623	$ 23,120
Services	10,088	5,257
Financing income	89	90
Total net revenue	28,800	28,467
Costs and expenses:		
Cost of products	14,164	17,334
Cost of services	7,819	4,028
Financing interest	86	82
Research and development	732	898
Selling, general and administrative	2,893	3,296
Amortization of purchased intangible assets	412	206
In-process research and development charges	6	
Restructuring charges	146	10
Acquisition-related charges	48	
Total operating expenses	26,306	25,854
Earnings from operations	2,494	2,613
Interest and other, net	(232)	72
Earnings before taxes	2,262	2,685
Provision for taxes	408	552
Net earnings	$ 1,854	$ 2,133
Net earnings per share:		
Basic	$ 0.77	$ 0.83
Diluted	$ 0.75	$ 0.80
Cash dividends declared per share	$ 0.16	$ 0.16
Weighted-average shares used to compute net earnings per share:		
Basic	2,410	2,560
Diluted	2,464	2,655

(1) Certain pursuit-related costs previously reported as Cost of products have been realigned retroactively to Selling, general and administrative expenses due to the organizational realignments occurring within HP's service offerings portfolio.

The accompanying notes are an integral part of these Consolidated Condensed Financial Statements.

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Consolidated Condensed Balance Sheets

	January 31, 2009	October 31, 2008
	In millions, except par value	
	(Unaudited)	
ASSETS		
Current assets:		
Cash and cash equivalents	$ 11,189	$ 10,153
Short-term investments	66	93
Accounts receivable	14,769	16,928
Financing receivables	2,316	2,314
Inventory	7,629	7,879
Other current assets	12,912	14,361
Total current assets	48,881	51,728
Property, plant and equipment	10,774	10,838
Long-term financing receivables and other assets	10,111	10,468
Goodwill	32,429	32,335
Purchased intangible assets	7,439	7,962
Total assets	$ 109,634	$ 113,331
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Notes payable and short-term borrowings	$ 10,199	$ 10,176
Accounts payable	11,231	14,138
Employee compensation and benefits	2,951	4,159
Taxes on earnings	699	869
Deferred revenue	6,591	6,287
Accrued restructuring	1,034	1,099
Other accrued liabilities	14,282	16,211
Total current liabilities	46,987	52,939
Long-term debt	10,259	7,676
Other liabilities	12,801	13,774
Commitments and contingencies		
Stockholders' equity:		
Preferred stock, $0.01 par value (300 shares authorized; none issued)		
Common stock, $0.01 par value (9,600 shares authorized; 2,405 and 2,415 shares issued and outstanding, respectively)	24	24
Additional paid-in capital	13,978	14,012
Retained earnings	26,165	24,971
Accumulated other comprehensive loss	(580)	(65)
Total stockholders' equity	39,587	38,942
Total liabilities and stockholders' equity	$ 109,634	$ 113,331

The accompanying notes are an integral part of these Consolidated Condensed Financial Statements.

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Consolidated Condensed Statements of Cash Flows

(Unaudited)

	Three months ended January 31	
	2009	**2008**
	In millions	
Cash flows from operating activities:		
Net earnings	$ 1,854	$ 2,133
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Depreciation and amortization	1,214	749
Stock-based compensation expense	154	157
Provision for bad debt and inventory	168	78
In-process research and development charges	6	
Restructuring charges	146	10
Acquisition-related charges	48	
Deferred taxes on earnings	(63)	361
Excess tax benefit from stock-based compensation	(13)	(88)
Other, net	(17)	6
Changes in operating assets and liabilities:		
Accounts and financing receivables	1,780	1,007
Inventory	156	54
Accounts payable	(2,889)	(659)
Taxes on earnings	300	(92)
Restructuring	(209)	(31)
Other assets and liabilities	(1,509)	(498)
Net cash provided by operating activities	1,126	3,187
Cash flows from investing activities:		
Investment in property, plant and equipment	(828)	(611)
Proceeds from sale of property, plant and equipment	152	88
Purchases of available-for-sale securities and other investments		(20)
Maturities and sales of available-for-sale securities and other investments	46	106
Payments made in connection with business acquisitions, net	(345)	(264)
Net cash used in investing activities	(975)	(701)
Cash flows from financing activities:		
Issuance (repayment) of commercial paper and notes payable, net	57	(899)
Issuance of debt	2,016	16
Payment of debt	(69)	(105)
Issuance of common stock under employee stock plans	299	554
Repurchase of common stock	(1,238)	(3,324)
Excess tax benefit from stock-based compensation	13	88
Dividends	(193)	(206)
Net cash provided by (used in) financing activities	885	(3,876)
Increase (decrease) in cash and cash equivalents	1,036	(1,390)
Cash and cash equivalents at beginning of period	10,153	11,293
Cash and cash equivalents at end of period	$11,189	$ 9,903

Supplemental schedule of noncash investing and financing activities:				
Issuance of options assumed in business acquisitions	$		$	(4)
Purchase of assets under financing arrangement	$	264	$	

The accompanying notes are an integral part of these Consolidated Condensed Financial Statements.

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements

(Unaudited)

Note 1: Basis of Presentation and Significant Accounting Policies

In the opinion of management, the accompanying Consolidated Condensed Financial Statements of Hewlett-Packard Company and its consolidated subsidiaries ("HP") contain all adjustments, including normal recurring adjustments, necessary to present fairly HP's financial position as of January 31, 2009, and its results of operations and cash flows for the three months ended January 31, 2009 and 2008. The Consolidated Condensed Balance Sheet as of October 31, 2008 is derived from the October 31, 2008 audited financial statements. Certain reclassifications have been made to prior-year amounts in order to conform to the current year presentation.

The results of operations for the three months ended January 31, 2009 are not necessarily indicative of the results to be expected for the full year. The information included in this Quarterly Report on Form 10-Q should be read in conjunction with "Risk Factors," "Legal Proceedings," "Management's Discussion and Analysis of Financial Condition and Results of Operations," "Quantitative and Qualitative Disclosures About Market Risk" and the Consolidated Financial Statements and notes thereto included in Items 1A, 3, 7, 7A and 8, respectively, of the Hewlett-Packard Company Annual Report on Form 10-K for the fiscal year ended October 31, 2008.

The preparation of financial statements in accordance with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in HP's Consolidated Condensed Financial Statements and accompanying notes. Actual results could differ materially from those estimates. HP has expanded its significant accounting policy disclosures beginning this quarter to include the following summary of its existing policy relating to loss contingencies. This summary previously has appeared, and continues to appear, as part of HP's disclosure regarding litigation and contingencies in Note 15.

HP is involved in various lawsuits, claims, investigations and proceedings that arise in the ordinary course of business. In accordance with Statement of Financial Accounting Standards ("SFAS") No. 5, "Accounting for Contingencies," HP records a provision for a liability when it believes it is both probable that a liability has been incurred and the amount can be reasonably estimated. Significant judgment is required to determine both probability and the estimated amount. HP reviews these provisions at least quarterly and adjusts these provisions to reflect the impact of negotiations, settlements, rulings, advice of legal counsel, and updated information. Litigation is inherently unpredictable and is subject to significant uncertainties, some of which are beyond HP's control.

Accounting Pronouncements

As previously reported in HP's 2008 Annual Report on Form 10-K, HP recognized the funded status of its benefit plans at October 31, 2007 in accordance with the recognition provisions of SFAS No. 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans An Amendment of Financial Accounting Standards Board ("FASB") Statements No. 87, 88, 106 and 132(R)" ("SFAS 158"). In addition to the recognition provisions, SFAS 158 also requires companies to measure the funded status of the plan as of the date of their fiscal year end, effective for fiscal years ending after December 15, 2008. HP will adopt the measurement provisions of SFAS 158 effective October 31, 2009 for the HP pension and post retirement plans. HP does not expect the adoption of the measurement provisions of SFAS 158 will have a material effect on its consolidated results of operations and financial condition.

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 1: Basis of Presentation and Significant Accounting Policies (Continued)

In February 2008, the FASB issued FASB Staff Position ("FSP") SFAS 157-2, "Effective Date of FASB Statement No. 157" ("FSP SFAS 157-2"). FSP SFAS 157-2 delays the effective date of SFAS No. 157, "Fair Value Measurements" ("SFAS 157") to fiscal years beginning after November 15, 2008 for all nonfinancial assets and nonfinancial liabilities, except those that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually). As a result of adoption of FSP SFAS 157-2, HP will adopt SFAS 157 for all nonfinancial assets and nonfinancial liabilities in the first quarter of fiscal 2010. Although HP will continue to evaluate the application of SFAS 157 to nonfinancial assets and nonfinancial liabilities, HP does not expect the adoption of SFAS 157 with respect to nonfinancial assets and nonfinancial liabilities will have a material impact on its consolidated results of operations and financial condition.

In December 2007, the FASB issued SFAS No. 141 (revised 2007), "Business Combinations" ("SFAS 141(R)"). SFAS 141(R) expands the definition of a business and a business combination; requires recognition of assets acquired, liabilities assumed, and contingent consideration at their fair value on the acquisition date; requires acquisition-related expenses and restructuring costs to be recognized separately from the business combination and expensed as incurred; requires in-process research and development to be capitalized at fair value as an intangible asset; and requires that changes in accounting for deferred tax asset valuation allowances and acquired income tax uncertainties after the measurement period be recognized as a component of provision for taxes. SFAS 141(R) also establishes disclosure requirements to enable the evaluation of the nature and financial effects of the business combination. SFAS 141(R) is effective for fiscal years beginning on or after December 15, 2008 and will be adopted by HP in the first quarter of fiscal 2010. HP is currently evaluating the potential impact of the adoption of SFAS 141(R) on its consolidated results of operations and financial condition, which will be largely dependent on the size and nature of the business combinations completed after the adoption of this statement. Among other potential impacts, HP currently believes that the adoption of SFAS 141(R) will result in the recognition of certain types of expenses in its results of operations that are currently capitalized pursuant to existing accounting standards.

In December 2007, the FASB issued SFAS No. 160, "Noncontrolling Interests in Consolidated Financial Statements an amendment of Accounting Research Bulletin No. 51" ("SFAS 160"). SFAS 160 establishes accounting and reporting standards for ownership interests in subsidiaries held by parties other than the parent, the amount of consolidated net income attributable to the parent and to the noncontrolling interest, changes in a parent's ownership interest, and the valuation of retained noncontrolling equity investments when a subsidiary is deconsolidated. SFAS 160 also establishes disclosure requirements that clearly identify and distinguish between the interests of the parent and the interests of the noncontrolling owners. SFAS 160 is effective for fiscal years beginning after December 15, 2008 and will be adopted by HP in the first quarter of fiscal 2010. HP is currently evaluating the potential impact, if any, of the adoption of SFAS 160 on its consolidated results of operations and financial condition.

In March 2008, the FASB issued SFAS No. 161, "Disclosures about Derivative Instruments and Hedging Activities, an amendment of FASB Statement No. 133" ("SFAS 161"). SFAS 161 applies to all derivative instruments and related hedged items accounted for under SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" ("SFAS 133"). SFAS 161 requires entities to provide greater transparency about how and why an entity uses derivative instruments, how derivative

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 1: Basis of Presentation and Significant Accounting Policies (Continued)

instruments and related hedged items are accounted for under SFAS 133 and its related interpretations, and how derivative instruments and related hedged items affect an entity's financial position, results of operations and cash flows. SFAS 161 is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008 and will be adopted by HP in the second quarter of fiscal 2009. HP will present the required disclosures in the prescribed format on a prospective basis upon adoption. HP does not expect the adoption of SFAS 161 will have a material effect on its consolidated results of operations and financial condition.

In May 2008, the FASB issued FSP Accounting Principles Board ("APB") 14-1 "Accounting for Convertible Debt Instruments That May Be Settled in Cash upon Conversion (Including Partial Cash Settlement)" ("FSP APB 14-1"). FSP APB 14-1 requires the issuer of certain convertible debt instruments that may be settled in cash (or other assets) on conversion to separately account for the liability (debt) and equity (conversion option) components of the instrument in a manner that reflects the issuer's non-convertible debt borrowing rate. FSP APB 14-1 is effective for fiscal years beginning after December 15, 2008 on a retroactive basis and will be adopted by HP in the first quarter of fiscal 2010. HP currently does not have any outstanding convertible debt instruments that are subject to the provisions of FSP APB 14-1. However, HP's U.S. dollar zero-coupon convertible notes that were redeemed in full in March 2008 are subject to the provisions of FSP APB 14-1. As a result, upon adoption of FSP APB 14-1 in the first quarter of fiscal 2010, HP's fiscal 2008 consolidated results of operations and financial condition will be affected on a retroactive basis. HP does not expect the adoption of FSP APB 14-1 will have a material effect on its consolidated results of operations and financial condition.

In June 2008, the FASB issued FSP Emerging Issues Task Force ("EITF") 03-6-1, "Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities" ("FSP EITF 03-6-1"). FSP EITF 03-6-1 clarifies that share-based payment awards that entitle their holders to receive nonforfeitable dividends or dividend equivalents before vesting should be considered participating securities. HP has granted and is expected to continue to grant restricted stock that contain non-forfeitable rights to dividends and will be considered participating securities upon adoption of FSP EITF 03-6-1. As participating securities, HP will be required to include these instruments in the calculation of HP's basic earnings per share ("EPS"), and it will need to calculate basic EPS using the "two-class method." Restricted stock is currently included in HP's dilutive EPS calculation using the treasury stock method. The two-class method of computing EPS is an earnings allocation formula that determines EPS for each class of common stock and participating security according to dividends declared (or accumulated) and participation rights in undistributed earnings. FSP EITF 03-6-1 is effective for fiscal years beginning after December 15, 2008 on a retrospective basis and will be adopted by HP in the first quarter of fiscal 2010. HP is currently evaluating the potential impact, if any, the adoption of FSP EITF 03-6-1 will have on its calculation of EPS.

In November 2008, the FASB ratified EITF Issue No. 08-7, "Accounting for Defensive Intangible Assets" ("EITF 08-7"). EITF 08-7 applies to defensive intangible assets, which are acquired intangible assets that the acquirer does not intend to actively use but intends to hold to prevent its competitors from obtaining access to them. As these assets are separately identifiable, EITF 08-7 requires an acquiring entity to account for defensive intangible assets as a separate unit of accounting. Defensive intangible assets must be recognized at fair value in accordance with SFAS 141(R) and SFAS 157.

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 1: Basis of Presentation and Significant Accounting Policies (Continued)

EITF 08-7 is effective for defensive intangible assets acquired in fiscal years beginning on or after December 15, 2008 and will be adopted by HP in the first quarter of fiscal 2010. HP is currently evaluating the potential impact, if any, of the adoption of EITF 08-7 on its consolidated results of operations and financial condition.

In December 2008, the FASB issued FSP SFAS 132(R)-1, "Employer's Disclosures about Postretirement Benefit Plan Assets" ("FSP SFAS 132(R)-1"). FSP SFAS 132(R)-1 requires additional disclosures about assets held in an employer's defined benefit pension or other postretirement plan. FSP SFAS 132(R)-1 is effective for fiscal years ending after December 15, 2009 and will be adopted by HP in the first quarter of fiscal 2010. HP will present the required disclosures in the prescribed format on a prospective basis upon adoption. HP does not expect the adoption of FSP SFAS 132(R)-1 will have a material effect on its consolidated results of operations and financial condition.

Recently Adopted Accounting Pronouncements

During the first quarter of fiscal 2009, HP adopted the following accounting standards, none of which had a material effect on its consolidated results of operations during such period or financial condition at the end of such period:

- SFAS No. 157;
- FSP SFAS 157-1, "Application of FASB Statement No. 157 to FASB Statement No. 13 and Other Accounting Pronouncements that Address Fair Value Measurements for Purposes of Lease Classification or Measurement under Statement 13" ("FSP SFAS 157-1");
- FSP SFAS 157-2;
- FSP SFAS 157-3, "Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active" ("FSP SFAS 157-3");
- SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities Including an amendment of FASB Statement No. 115" ("SFAS 159"); and
- EITF 07-3, "Accounting for Nonrefundable Advance Payments for Goods or Services Received for Use in Future Research and Development Activities."

See Note 8 for additional information pertaining to SFAS 157, FSP SFAS 157-1, FSP SFAS 157-2, FSP SFAS 157-3 and SFAS 159.

Note 2: Stock-Based Compensation

HP's stock-based compensation plans include incentive compensation plans and an employee stock purchase plan. Incentive compensation plans include principal option plans as well as various stock option plans assumed through acquisitions. Principal option plans include performance-based restricted units ("PRU"), stock options and restricted stock awards. HP accounts for its stock-based compensation plans under SFAS No. 123(R), "Share-Based Payment".

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 2: Stock-Based Compensation (Continued)

Total stock-based compensation expense for the three months ended January 31, 2009 and 2008 was as follows:

	Three months ended January 31	
	2009	2008
	In millions	
Cost of sales	$ 52	$ 36
Research and development	17	20
Selling, general and administrative	85	101
Acquisition-related charges	6	
Stock-based compensation expense before income taxes[(1)]	160	157
Income tax benefit	(48)	(47)
Total stock-based compensation expense after income taxes	$ 112	$ 110

---

(1) For the three months ended January 31, 2009, $6 million of stock-based compensation expense before income taxes was included in acquisition-related charges in the accompanying Consolidated Condensed Statements of Cash Flows.

Performance-based Restricted Units

In fiscal 2008, HP implemented a program that provides for the issuance of PRUs representing hypothetical shares of HP common stock that may be issued under the Hewlett-Packard Company 2004 Stock Incentive Plan.

Under the PRU program, a target number of units are awarded at the beginning of each three-year performance period. The number of shares released at the end of the performance period will range from zero to two times the target number depending on performance during the period. The performance metrics of the PRU program are (a) annual targets based on cash flow from operations as a percentage of revenue, and (b) an overall "modifier" based on Total Shareholder Return ("TSR") relative to the S&P 500 over the three-year performance period. TSR is calculated using the quarterly average performance of the S&P 500 during the three-year performance period.

As the cash flow goals are considered performance conditions, the expense for these awards, net of estimated forfeitures, will be recorded over the three-year performance period based on the number of shares that are expected to be earned based on the achievement of the cash flow goals during the performance period.

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 2: Stock-Based Compensation (Continued)

HP estimates the fair value of a target PRU share using the Monte Carlo simulation model, as the TSR modifier contains a market condition. The following weighted-average assumptions were used to determine the fair values of the PRU awards:

	Three months ended January 31	
	2009[1]	**2008**
Weighted-average fair value of grants	$ 40.56	$ 40.21
Expected volatility[2]	35%	26%
Risk-free interest rate	1.34%	3.13%
Dividend yield	0.88%	0.70%
Expected life in months	30	33

(1) Reflects the weighted-average fair value for the second year of the three-year performance period applicable to PRUs granted in fiscal 2008 and for the first year of the three-year performance period applicable to PRUs granted in fiscal 2009. The estimated fair value of a target share for the third year for PRUs granted in fiscal 2008 and for the second and third years for PRUs granted in fiscal 2009 will be determined when the annual cash flow goals are approved, and the expense will be amortized over the remainder of the applicable three-year performance period.

(2) HP uses historic volatility for PRU awards as implied volatility cannot be used when simulating multivariate prices for companies in the S&P 500.

Outstanding PRUs as of January 31, 2009 and October 31, 2008 and changes during the three months ended January 31, 2009 were as follows (shares in thousands):

	Three months ended January 31, 2009	Fiscal 2008
Beginning units outstanding	10,965	
Granted	13,854	8,783
Change in units due to performance and market conditions	(661)	2,492
Forfeited	(230)	(310)
Ending units outstanding	23,928	10,965
Vested		
Units assigned a fair value	11,963	5,292

At January 31, 2009, there was $320 million of unrecognized pre-tax stock-based compensation expense related to PRUs with an assigned fair value, which HP expects to recognize over the remaining weighted-average period of 2.2 years.

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 2: Stock-Based Compensation (Continued)

Stock Options

HP estimated the fair value of stock options using the Black-Scholes option pricing model with the following weighted-average assumptions and weighted-average fair values:

	Three months ended January 31	
	2009	**2008**
Weighted-average fair value of grants	$ 14.22	$ 16.59
Implied volatility	51%	35%
Risk-free interest rate	1.79%	3.38%
Dividend yield	0.95%	0.65%
Expected life in months	60	60

Option activity as of January 31, 2009 and changes during the three months ended January 31, 2009 were as follows:

	Shares (in thousands)	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value (in millions)
Outstanding at October 31, 2008	307,728	$ 34		
Granted and assumed through acquisitions	1,160	$ 22		
Exercised	(5,677)	$ 24		
Forfeited/cancelled/expired	(11,555)	$ 67		
Outstanding at January 31, 2009	291,656	$ 32	3.1	$ 1,942
Vested and expected to vest at January 31, 2009	288,980	$ 32	3.1	$ 1,929
Exercisable at January 31, 2009	252,591	$ 32	2.7	$ 1,754

The aggregate intrinsic value in the table above represents the total pre-tax intrinsic value that option holders would have received had all option holders exercised their options on January 31, 2009. The aggregate intrinsic value is the difference between HP's closing stock price on the last trading day of the first quarter of fiscal 2009 and the exercise price, multiplied by the number of in-the-money options. Total intrinsic value of options exercised for the three months ended January 31, 2009 was $65 million.

At January 31, 2009, there was $364 million of unrecognized pre-tax stock-based compensation expense related to stock options, which HP expects to recognize over the remaining weighted-average period of 1.4 years.

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 2: Stock-Based Compensation (Continued)

Restricted Stock Awards

Non-vested restricted stock awards as of January 31, 2009 and changes during the three months ended January 31, 2009 were as follows:

	Shares (in thousands)	Weighted-Average Grant Date Fair Value
Non-vested at October 31, 2008	12,930	$ 44
Granted	474	$ 35
Vested	(1,075)	$ 42
Forfeited	(373)	$ 40
Non-vested at January 31, 2009	11,956	$ 44

At January 31, 2009, there was $226 million of unrecognized pre-tax stock-based compensation expense related to non-vested restricted stock awards, which HP expects to recognize over the remaining weighted-average period of 1.2 years.

Changes to the Employee Stock Purchase Plan

HP sponsors the Hewlett-Packard Company 2000 Employee Stock Purchase Plan, also known as the Share Ownership Plan (the "ESPP"), pursuant to which eligible employees may contribute up to 10% of base compensation, subject to certain income limits, to purchase shares of HP's common stock. Employees purchase stock pursuant to the ESPP semi-annually at a price equal to 85% of the fair market value on the purchase date. HP recognizes expense based on a 15% discount from fair market value. Effective May 1, 2009, HP will discontinue offering the 15% discount.

Note 3: Net Earnings Per Share

HP calculates basic earnings per share using net earnings and the weighted-average number of shares outstanding during the reporting period. Diluted EPS includes any dilutive effect of outstanding restricted stock, stock options, restricted stock units and convertible debt.

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 3: Net Earnings Per Share (Continued)

The reconciliation of the numerators and denominators of the basic and diluted EPS calculations was as follows:

	Three months ended January 31	
	2009	2008
	In millions, except per share amounts	
Numerator:		
Net earnings	$ 1,854	$ 2,133
Adjustment for interest expense on zero-coupon subordinated convertible notes, net of taxes		2
Net earnings, adjusted	$ 1,854	$ 2,135
Denominator:		
Weighted-average shares used to compute basic EPS	2,410	2,560
Effect of dilutive securities:		
Dilution from employee stock plans	54	87
Zero-coupon subordinated convertible notes		8
Dilutive potential common shares	54	95
Weighted-average shares used to compute diluted EPS	2,464	2,655
Net earnings per share:		
Basic	$ 0.77	$ 0.83
Diluted	$ 0.75	$ 0.80

HP excludes options with exercise prices that are greater than the average market price from the calculation of diluted EPS because their effect would be anti-dilutive. In the first quarter of fiscal 2009 and 2008, HP excluded 107 million shares and 35 million shares, respectively, from its diluted EPS calculation. Also, in accordance with SFAS 123R, HP excluded from the calculation of diluted EPS options to purchase an additional 1 million shares and 30 million shares in the first quarter of fiscal 2009 and 2008, respectively, whose combined exercise price, unamortized fair value and excess tax benefits were greater in each of those periods than the average market price for HP's common stock because their effect would be anti-dilutive. As disclosed in Note 2, HP granted PRU awards representing at target approximately 14 million shares and 9 million shares, respectively. HP includes the shares underlying PRU awards in the calculation of diluted EPS when they become contingently issuable per SFAS No. 128, "Earnings per Share," and excludes such shares when they are not contingently issuable. Accordingly, HP has included 2 million shares underlying the PRU awards granted in fiscal 2008 when calculating diluted EPS as those shares became contingently issuable upon the satisfaction of the cash flow from operations condition with respect to the first year of the performance period applicable to those awards. HP has excluded all other shares underlying the fiscal 2008 awards and all shares underlying the fiscal 2009 awards as those shares are not contingently issuable.

In October and November 1997, HP issued U.S. dollar zero-coupon subordinated convertible notes due 2017 (the "LYONs"), the outstanding principal amount of which was redeemed in March 2008. The

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 3: Net Earnings Per Share (Continued)

LYONs were convertible at the option of the holders at any time prior to maturity, unless previously redeemed or otherwise purchased. For purposes of calculating diluted earnings per share above, the interest expense (net of tax) associated with the LYONs was added back to net earnings, and the shares issuable upon conversion of the LYONs were included in the weighted-average shares used to compute diluted earnings per share for periods that the LYONs were outstanding.

Note 4: Balance Sheet Details

Balance sheet details were as follows:

Accounts and Financing Receivables

	January 31, 2009	October 31, 2008
	In millions	
Accounts receivable	$ 15,355	$ 17,481
Allowance for doubtful accounts	(586)	(553)
	$ 14,769	$ 16,928
Financing receivables	$ 2,360	$ 2,355
Allowance for doubtful accounts	(44)	(41)
	$ 2,316	$ 2,314

HP has revolving trade receivables-based facilities permitting it to sell certain trade receivables to third parties on a non-recourse basis. The aggregate maximum capacity under these programs was $569 million as of January 31, 2009. HP sold $549 million of trade receivables during the first quarter of fiscal 2009. As of January 31, 2009, HP had $167 million available under these programs.

Inventory

	January 31, 2009	October 31, 2008
	In millions	
Finished goods	$ 4,831	$ 5,219
Purchased parts and fabricated assemblies	2,798	2,660
	$ 7,629	$ 7,879

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 4: Balance Sheet Details (Continued)

Other Current Assets

	January 31, 2009	October 31, 2008
	In millions	
Prepaid expenses	$ 2,505	$ 1,636
Other current assets	10,407	12,725
	$ 12,912	$ 14,361

Note 5: Acquisitions

In the first quarter of fiscal 2009, HP completed the acquisition of Lefthand Networks, Inc., a leading provider of storage virtualization and solutions for approximately $347 million including direct transaction costs and the assumption of certain liabilities in connection with the transaction. HP recorded $273 million to goodwill, $95 million to purchased intangibles and $6 million to in-process research and development charges ("IPR&D") related to this acquisition. Lefthand Networks is being integrated into HP's Enterprise Storage and Servers segment within the Technology Solutions Group. HP does not expect goodwill recorded with respect to this acquisition to be deductible for tax purposes. HP has not presented pro forma results of operations because this acquisition is not material to HP's consolidated results of operations.

Acquisition of Electronic Data Systems Corporation ("EDS")

As previously disclosed in its Consolidated Financial Statements for the fiscal year ended October 31, 2008, on August 26, 2008, HP completed its acquisition of EDS. The purchase price for EDS was $13.0 billion, comprised of $12.7 billion cash paid for outstanding common stock, $328 million for the estimated fair value of stock options and restricted stock units assumed, and $36 million for direct transaction costs. Of the total purchase price, a preliminary estimate of $10.5 billion has been allocated to goodwill, $4.5 billion has been allocated to amortizable intangible assets acquired and $2.0 billion has been allocated to net tangible liabilities assumed in connection with the acquisition. HP also expensed $30 million for IPR&D charges.

The purchase price allocation as of the date of the acquisition reflects various preliminary estimates and analyses, including preliminary work performed by third-party valuation specialists, and is subject to change during the purchase price allocation period (generally one year from the acquisition date) as valuations are finalized.

HP has evaluated and continues to evaluate certain pre-acquisition contingencies related to EDS that existed as of the acquisition date. Additional information, which existed as of the acquisition date but was at that time unknown to HP, may become known to HP during the remainder of the purchase price allocation period, and may result in goodwill adjustments. If these pre-acquisition contingencies become probable in nature and estimable after the end of the purchase price allocation period, amounts would be recorded for such matters in HP's results of operations.

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 5: Acquisitions (Continued)

Pro forma results for EDS acquisition

The following table presents the unaudited results of HP (including EDS) for the three months ended January 31, 2009 and the unaudited pro forma results for the three months ended January 31, 2008. The unaudited pro forma financial information for the three months ended January 31, 2008 combines the results of operations of HP and EDS as though the companies had been combined as of the beginning of fiscal 2008. The pro forma financial information is presented for informational purposes only and is not indicative of the results of operations that would have been achieved if the acquisition and related borrowings had taken place at the beginning of fiscal 2008. The unaudited pro forma results presented include amortization charges for acquired intangible assets, eliminations of intercompany transactions, restructuring charges, IPR&D charges, adjustments for incremental stock-based compensation expense related to the unearned portion of EDS stock options and restricted stock units assumed, adjustments for depreciation expense for property, plant and equipment, adjustments to interest expense and related tax effects.

In millions, except per share data	Three months ended January 31 2009	2008
	Unaudited	
Revenue	$28,800	$33,748
Net Income	$ 1,854	$ 1,521
Basic net income per share	$ 0.77	$ 0.59
Diluted net income per share	$ 0.75	$ 0.57

Note 6: Goodwill and Purchased Intangible Assets

Goodwill

Goodwill allocated to HP's business segments as of January 31, 2009 and changes in the carrying amount of goodwill for the three months ended January 31, 2009 are as follows:

	Services	Enterprise Storage and Servers	HP Software	Personal Systems Group	Imaging and Printing Group	HP Financial Services	Corporate Investments	Total
				In millions				
Balance at October 31, 2008	$16,284	$ 4,745	$ 6,162	$ 2,493	$ 2,463	$ 144	$ 44	$32,335
Goodwill acquired during the period		273						273
Goodwill adjustments	(172)		(5)		(2)			(179)
Balance at January 31, 2009	$16,112	$ 5,018	$ 6,157	$ 2,493	$ 2,461	$ 144	$ 44	$32,429

During the three months ended January 31, 2009, HP recorded a reduction of approximately $300 million to goodwill as a result of currency translation related to EDS's foreign subsidiaries whose functional currency is not the U.S. dollar. The reduction to goodwill was partially offset by adjustments of approximately $130 million to the estimated fair values of EDS's intangible assets and net liabilities acquired.

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 6: Goodwill and Purchased Intangible Assets (Continued)

Purchased Intangible Assets

HP's purchased intangible assets associated with completed acquisitions are composed of:

	January 31, 2009			October 31, 2008		
	Gross	Accumulated Amortization	Net	Gross	Accumulated Amortization	Net
	In millions					
Customer contracts, customer lists and distribution agreements	$ 6,488	$ (2,402)	$4,086	$ 6,530	$ (2,176)	$4,354
Developed and core technology and patents	4,131	(2,318)	1,813	4,189	(2,147)	2,042
Product trademarks	242	(124)	118	253	(109)	144
Total amortizable purchased intangible assets	10,861	(4,844)	6,017	10,972	(4,432)	6,540
Compaq trade name	1,422		1,422	1,422		1,422
Total purchased intangible assets	$12,283	$ (4,844)	$7,439	$12,394	$ (4,432)	$7,962

For the three months ended January 31, 2009, HP recorded a reduction of approximately $100 million to purchased intangibles as a result of currency translation related to EDS's foreign subsidiaries whose functional currency is not the U.S. dollar. In addition, HP also recorded an adjustment of approximately $90 million to the estimated fair value of EDS's intangible assets acquired.

Estimated future amortization expense related to finite lived purchased intangible assets at January 31, 2009 is as follows:

Fiscal year:	In millions
2009 (remaining 9 months)	$ 1,084
2010	1,300
2011	1,002
2012	810
2013	673
Thereafter	1,148
Total	$ 6,017

Note 7: Restructuring Charges

Fiscal 2008 Restructuring Plan

In connection with the acquisition of EDS on August 26, 2008, HP's management approved and initiated a restructuring plan to streamline the combined company's services business and to better align the structure and efficiency of that business with HP's operating model. The restructuring plan is expected to be implemented over the next four years and will include changes to the combined company's workforce as well as changes to corporate overhead functions, such as real estate, IT and procurement.

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 7: Restructuring Charges (Continued)

In the fourth quarter of fiscal 2008, HP recorded a liability of approximately $1.8 billion related to this restructuring plan. Approximately $1.5 billion of the liability was associated with pre-acquisition EDS and was recorded to goodwill, and the remaining approximately $0.3 billion was associated with HP and was recorded as a restructuring charge. The liability consisted mainly of severance costs to eliminate approximately 25,000 positions, costs to vacate duplicate facilities and costs associated with early termination of certain contractual obligations. For the three months ended January 31, 2009, HP recorded a net charge of $150 million, due primarily to adjustments for severance and facilities costs. As of January 31, 2009, over 9,000 positions have been eliminated.

HP expects the majority of the restructuring costs to be paid out by the end of fiscal 2009. In future quarters, HP expects to record an additional charge of approximately $115 million related to severance costs and the cost to vacate duplicative facilities.

Prior Fiscal Year Plans

Restructuring plans initiated prior to 2008 are substantially complete and HP expects to record only minor revisions to these plans as necessary.

Summary of Restructuring Plans

The adjustments to the accrued restructuring expenses related to all of HP's restructuring plans described above for the three months ended January 31, 2009 were as follows:

							As of January 31, 2009	
	Balance, October 31, 2008	Three months ended January 31, 2009 charges (reversals)	Goodwill adjustments	Cash payments	Non-cash settlements and other adjustments	Balance, January 31, 2009	Total costs and adjustments to date	Total expected costs and adjustments
	In millions							
Fiscal 2008 HP/EDS Plan:								
Severance	$ 1,444	$ 149	$ 15	$ (196)	$ (25)	$ 1,387	$ 1,699	$ 1,777
Infrastructure	248	1	9	(3)	(4)	251	263	300
Total severance and other restructuring activities	$ 1,692	$ 150	$ 24	$ (199)	$ (29)	$ 1,638	$ 1,962	$ 2,077
Prior fiscal year plans	77	(4)		(10)		63	6,344	6,344
Total restructuring plans	$ 1,769	$ 146	$ 24	$ (209)	$ (29)	$ 1,701	$ 8,306	$ 8,421

At January 31, 2009 and October 31, 2008, HP included the long-term portion of the restructuring liability of $667 million and $670 million, respectively, in Other liabilities, and the short-term portion in Accrued restructuring in the accompanying Consolidated Condensed Balance Sheets.

Workforce Rebalancing

As part of HP's ongoing business operations, HP incurred workforce rebalancing charges for severance and related costs within certain business segments during the first three months of fiscal 2009. Workforce rebalancing activities are considered part of normal operations as HP continues to

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 7: Restructuring Charges (Continued)

optimize its cost structure. Workforce rebalancing costs are included in HP's business segment results, and HP expects to incur additional workforce rebalancing costs in the future.

Note 8: Fair Value

Effective November 1, 2008, HP adopted the effective portions of SFAS 157 as highlighted in Note 1. The adoption did not have a material impact on our financial statements and did not result in any changes to the opening balance of retained earnings as of November 1, 2008.

SFAS 157 establishes a new framework for measuring fair value and expands related disclosures. The SFAS 157 framework requires fair value to be determined based on the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants.

The valuation techniques required by SFAS 157 are based upon observable and unobservable inputs. Observable or market inputs reflect market data obtained from independent sources, while unobservable inputs reflect HP's assumptions about market participant assumptions based on best information available. Observable inputs are the preferred source of values. In accordance with SFAS 157, these two types of inputs create the following fair value hierarchy:

Level 1 - Quoted prices (unadjusted) for identical instruments in active markets.

Level 2 - Quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3 - Prices or valuations that require management inputs that are both significant to the fair value measurement and unobservable.

The following section describes the valuation methodologies HP uses to measure its financial assets and liabilities at fair value.

Cash Equivalents: HP holds money market funds investing mainly in treasury bills, which are classified under level 1. HP also invests in time deposits, commercial paper and treasury bills, which are classified under level 2.

Investments: HP holds time deposits, corporate and foreign government notes and bonds, asset-backed securities, and common stock and equivalents. In general, and where applicable, HP uses quoted prices in active markets for identical assets or liabilities to determine fair value. If quoted prices in active markets for identical assets or liabilities are not available to determine fair value, then HP uses quoted prices for similar assets and liabilities or inputs that are observable either directly or indirectly. If quoted prices for identical or similar assets are not available, HP uses internally developed valuation models, whose inputs include bid prices, and third party valuations utilizing underlying assets assumptions.

Derivative Instruments: HP mainly holds non-speculative forwards, swaps and options to hedge certain foreign currency and interest rate exposures. HP uses quoted prices in an active market for identical derivative assets and liabilities that are traded on exchanges and, when active market quotes

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 8: Fair Value (Continued)

are not available, HP uses industry standard valuation models, such as the Black-Scholes model. Where applicable, these models project future cash flows and discount the future amounts to a present value using market-based observable inputs including interest rate curves, credit risk, foreign exchange rates, and forward and spot prices for currencies. In certain cases, market-based observable inputs are not available and, in those cases, HP uses management judgment to develop assumptions which are used to determine fair value.

Other Liabilities: HP has a liability to company executives as part of the executive deferred compensation plan. The liability is linked to a group of mutual funds and indexes and is classified under level 1.

The following table presents HP's assets and liabilities that are measured at fair value on a recurring basis at January 31, 2009:

	Fair Value Measured Using			Total
	Level 1	Level 2	Level 3	Balance
	In millions			
Assets				
Cash Equivalents	$ 388	$7,688	$	$ 8,076
Investment Securities	19	80	50	149
Derivatives		2,093	1	2,094
Total	$ 407	$9,861	$ 51	$ 10,319
Liabilities				
Derivatives	$	$ (322)	$	$ (322)
Other Liabilities	(290)			(290)
Total	$(290)	$ (322)	$	$ (612)

The following table presents the changes in level 3 instruments measured on a recurring basis for the three months ended January 31, 2009. The majority of the level 3 balances consist of investment

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 8: Fair Value (Continued)

securities classified as available-for-sale with changes in fair value recorded in other comprehensive income.

	Fair Value Measured Using Significant Unobservable Inputs (Level 3)		
	Investment Securities	Derivative Instruments	Total
	In millions		
Beginning balance at November 1, 2008	$ 64	$ (1)	$ 63
Total losses (realized/unrealized):			
Included in earnings[1]	(2)		(2)
Included in other comprehensive income	(11)	1	(10)
Purchases, issuances, and settlements	(1)	1	
Ending balance at January 31, 2009	$ 50	$ 1	$ 51
The amount of total losses for the period included in earnings attributable to the change in unrealized losses relating to assets still held as of January 31, 2009	$ (2)	$	$ (2)

(1) Included in Interest and other, net in the accompanying Consolidated Condensed Statements of Earnings.

HP measures certain assets including cost and equity method investments, at fair value on a nonrecurring basis. These assets are recognized at fair value when they are deemed to be other-than-temporarily impaired. As of January 31, 2009, assets with a total fair value of $29 million were included in the level 3 hierarchy. HP recorded an impairment charge of $5 million during the first quarter of fiscal 2009.

HP reviews the carrying values of the investments when events and circumstances warrant and considers all available evidence in evaluating when declines in fair value are other-than-temporary. The fair values of the investments are determined based on valuation techniques using the best information available, which may include quoted market prices, market comparables, and discounted cash flow projections. An impairment charge is recorded when the cost of the investment exceeds its fair value and is determined to be other-than-temporary.

Effective November 1, 2008, HP also adopted SFAS 159, which allows an entity to choose to measure certain financial instruments and liabilities at fair value on a contract-by-contract basis. Subsequent fair value measurement for the financial instruments and liabilities an entity chooses to measure at fair value will be recognized in earnings. As of January 31, 2009, HP did not elect such option for any eligible financial instruments and liabilities.

Note 9: Financing Receivables and Operating Leases

Financing receivables represent sales-type and direct-financing leases resulting from the marketing of HP's and third-party products. These receivables typically have terms from two to five years and are usually collateralized by a security interest in the underlying assets. Financing receivables also include

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 9: Financing Receivables and Operating Leases (Continued)

billed receivables from operating leases. The components of net financing receivables, which are included in financing receivables and long-term financing receivables and other assets, were as follows:

	January 31, 2009	October 31, 2008
	In millions	
Minimum lease payments receivable	$ 5,385	$ 5,338
Allowance for doubtful accounts	(97)	(90)
Unguaranteed residual value	244	254
Unearned income	(492)	(466)
Financing receivables, net	5,040	5,036
Less current portion	(2,316)	(2,314)
Amounts due after one year, net	$ 2,724	$ 2,722

Equipment leased to customers under operating leases was $2.4 billion at January 31, 2009 and $2.3 billion at October 31, 2008 and is included in machinery and equipment. Accumulated depreciation on these operating leases was $0.6 billion at January 31, 2009 and $0.5 billion at October 31, 2008.

Note 10: Guarantees

Guarantees and Indemnifications

In the ordinary course of business, HP may provide certain clients, principally governmental entities, with subsidiary performance guarantees and/or financial performance guarantees, which may be backed by standby letters of credit or surety bonds. In general, HP would be liable for the amounts of these guarantees in the event HP or HP's subsidiaries' nonperformance permits termination of the related contract by the client, the likelihood of which HP believes is remote. HP believes that the company is in compliance with the performance obligations under all material service contracts for which there is a performance guarantee.

As a result of the acquisition of EDS, HP acquired certain service contracts supported by client financing or securitization arrangements. Under specific circumstances involving non performance resulting in service contract termination or failure to comply with terms under the financing arrangement, HP would be required to acquire certain assets. HP considers the possibility of its failure to comply to be remote and the asset amounts involved to be immaterial.

In the ordinary course of business, HP enters into contractual arrangements under which HP may agree to indemnify the third party to such arrangement from any losses incurred relating to the services they perform on behalf of HP or for losses arising from certain events as defined within the particular contract, which may include, for example, litigation or claims relating to past performance. Such indemnification obligations may not be subject to maximum loss clauses. Historically, payments made related to these indemnifications have been immaterial.

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 10: Guarantees (Continued)

Warranty

HP provides for the estimated cost of product warranties at the time it recognizes revenue. HP engages in extensive product quality programs and processes, including actively monitoring and evaluating the quality of its component suppliers; however, product warranty terms offered to customers, ongoing product failure rates, material usage and service delivery costs incurred in correcting a product failure, as well as specific product class failures outside of HP's baseline experience, affect the estimated warranty obligation. If actual product failure rates, repair rates or any other post sales support costs differ from these estimates, revisions to the estimated warranty liability would be required.

The changes in HP's aggregate product warranty liabilities for the three months ended January 31, 2009 were as follows:

	In millions
Product warranty liability at October 31, 2008	$ 2,614
Accruals for warranties issued	672
Adjustments related to pre-existing warranties (including changes in estimates)	(102)
Settlements made (in cash or in kind)	(663)
Product warranty liability at January 31, 2009	$ 2,521

Note 11: Borrowings

Notes Payable and Short-Term Borrowings

Notes payable and short-term borrowings, including the current portion of long-term debt, were as follows:

	January 31, 2009		October 31, 2008	
	Amount Outstanding	Weighted-Average Interest Rate	Amount Outstanding	Weighted-Average Interest Rate
	In millions			
Commercial paper	$ 7,213	1.0%	$ 7,146	2.7%
Current portion of long-term debt	2,654	3.8%	2,674	4.3%
Notes payable to banks, lines of credit and other	332	3.0%	356	5.3%
	$ 10,199		$ 10,176	

Notes payable to banks, lines of credit and other includes deposits associated with HP's banking-related activities of approximately $247 million and $262 million at January 31, 2009 and October 31, 2008, respectively.

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 11: Borrowings (Continued)

Long-Term Debt

Long-term debt was as follows:

	January 31, 2009	October 31, 2008
	In millions	
U.S. Dollar Global Notes		
2002 Shelf Registration Statement:		
$500 issued at discount to par of 99.505% in June 2002 at 6.5%, due July 2012	$ 499	$ 499
2006 Shelf Registration Statement:		
$600 issued at par in February 2007 at three-month USD LIBOR plus 0.11%, due March 2012	600	600
$900 issued at discount to par of 99.938% in February 2007 at 5.25%, due March 2012	900	900
$500 issued at discount to par of 99.694% in February 2007 at 5.4%, due March 2017	499	499
$1,000 issued at par in June 2007 at three-month USD LIBOR plus 0.01%, due June 2009	1,000	1,000
$1,000 issued at par in June 2007 at three-month USD LIBOR plus 0.06%, due June 2010	1,000	1,000
$750 issued at par in March 2008 at three-month USD LIBOR plus 0.40%, due September 2009	750	750
$1,500 issued at discount to par of 99.921% in March 2008 at 4.5%, due March 2013	1,499	1,499
$750 issued at discount to par of 99.932% in March 2008 at 5.5%, due March 2018	750	750
$2,000 issued at discount to par of 99.561% in December 2008 at 6.125%, due March 2014	1,991	
	9,488	7,497
EDS Senior Notes		
$700 issued October 1999 at 7.125%, due October 2009	709	712
$1,100 issued June 2003 at 6.0%, due August 2013	1,148	1,150
$300 issued October 1999 at 7.45%, due October 2029	316	316
	2,173	2,178
Other, including capital lease obligations, at 3.75%-9.14%, due in calendar year 2008-2029	816	597
Fair value adjustment related to SFAS No. 133	436	78
	12,913	10,350
Less: current portion	(2,654)	(2,674)
Total long-term debt	$ 10,259	$ 7,676

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 11: Borrowings (Continued)

HP may redeem some or all of the Global Notes as set forth in the above table at any time at the redemption prices described in the prospectus supplements relating thereto. The Global Notes are senior unsecured debt.

HP registered the sale of up to $3.0 billion of debt or global securities, common stock, preferred stock, depositary shares and warrants under a shelf registration statement in March 2002 (the "2002 Shelf Registration Statement"). The 2002 Shelf Registration Statement expired on December 1, 2008, and, accordingly, HP is no longer able to issue any additional securities under this Registration Statement.

In May 2006, HP filed a shelf registration statement (the "2006 Shelf Registration Statement") with the Securities and Exchange Commission ("SEC") to enable HP to offer and sell, from time to time, in one or more offerings, an unlimited amount of debt securities, common stock, preferred stock, depositary shares and warrants. As of January 31, 2009, HP had $9.0 billion of global notes issued under the 2006 Shelf Registration Statement. On December 5, 2008, HP issued $2.0 billion of global notes under the 2006 Shelf Registration Statement. The global notes issued in December 2008 are due in March 2014, bear interest at a fixed interest rate of 6.125% per annum and were issued at a discount to par of 99.561%. HP used the net proceeds from these offerings for general corporate purposes and the repayment of short-term commercial paper, some of which was issued in connection with its acquisition of EDS. On February 26, 2009, HP issued an additional $2.8 billion of global notes under the 2006 Shelf Registration Statement. The global notes include $275 million of floating rate notes due February 2011 issued at par, $1.0 billion of notes due February 2012 with a fixed rate of 4.25% per annum issued at a discount to par of 99.956% and $1.5 billion of notes due June 2014 with a fixed rate of 4.75% per annum issued at a discount to par of 99.993%. HP used the net proceeds from these offerings for general corporate purposes and the repayment of short-term commercial paper, some of which was issued in connection with its acquisition of EDS.

In May 2008, the Board of Directors approved increasing the capacity of HP's U.S. commercial paper program by $10.0 billion to $16.0 billion. HP's subsidiaries are authorized to issue up to an additional $1.0 billion of commercial paper, of which $500 million of capacity is currently available to be used by Hewlett-Packard International Bank PLC, a wholly-owned subsidiary of HP, for its Euro Commercial Paper/Certificate of Deposit Programme.

In October 2008, HP registered for the Commercial Paper Funding Facility ("CPFF") provided by the Federal Reserve Bank of New York. The facility enables HP to issue three-month unsecured commercial paper through a special purpose vehicle of the Federal Reserve at a rate established by the CPFF program, which is currently equal to a spread over the three-month overnight index swap rate. The maximum amount of commercial paper that HP may issue at any time through this program is $10.4 billion less the total principal amount of all other outstanding commercial paper that HP has issued. As of January 31, 2009, HP had not issued any commercial paper under the CPFF program. In February 2009, the Federal Reserve extended the CPFF program through October 30, 2009.

HP has a $2.9 billion five-year credit facility expiring in May 2012. In February and July 2008, HP entered into additional 364-day credit facilities of $3.0 billion and $8.0 billion, respectively. The February 2008 credit facility expired in February 2009, at which time HP entered into a new $3.5 billion 364-day credit facility. Commitment fees, interest rates and other terms of borrowing under the credit facilities vary based on HP's external credit ratings. The credit facilities are senior unsecured committed

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 11: Borrowings (Continued)

borrowing arrangements primarily to support the issuance of U.S. commercial paper. Under the terms of the July 2008 $8.0 billion 364-day credit facility, the amount of credit available declines in an amount equal to the proceeds of any future issuance of long-term debt by HP. In December 2008 and February 2009, HP issued $2.0 billion and $2.8 billion, respectively, in global notes, which resulted in a reduction in the amount of credit available under the July 2008 credit facility to $3.2 billion.

HP also maintains uncommitted lines of credit from a number of financial institutions that are available through various foreign subsidiaries. The amount available for use as of January 31, 2009 was approximately $1.4 billion.

Included in Other, including capital lease obligations, are borrowings that are collateralized by certain financing receivable assets. As of January 31, 2009, the carrying value of the assets approximated the carrying value of the borrowings of $6.8 million.

At January 31, 2009, HP had up to approximately $10.7 billion of available borrowing resources, including $9.3 billion under credit facilities that support primarily its commercial paper programs and approximately $1.4 billion under other programs. HP also may issue an unlimited amount of additional debt securities, common stock, preferred stock, depositary shares and warrants under the 2006 Shelf Registration Statement.

Note 12: Income Taxes

Provision for Taxes

HP's effective tax rate was 18.0% and 20.6% for the three months ended January 31, 2009 and January 31, 2008, respectively. HP's effective tax rate generally differs from the U.S. federal statutory rate of 35% due to the tax rate benefits of certain earnings from HP's operations in lower-tax jurisdictions throughout the world. HP has not provided U.S. taxes for such earnings because HP plans to reinvest those earnings indefinitely outside the United States. There were no material discrete items affecting the tax rate for the three months ended January 31, 2009 and January 31, 2008, respectively.

During the first three months of fiscal 2009, the amount of gross unrecognized tax benefits determined in accordance with Financial Interpretation No. 48, "Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109" ("FIN 48") increased by $171 million to $2.5 billion, of which up to $758 million would affect HP's effective tax rate if realized. HP recognizes interest expense and penalties on unrecognized tax benefits within income tax expense. During the first three months of fiscal 2009, there was no material change in the amount of accrued net interest and penalties.

HP is subject to income tax in the United States and over sixty foreign countries and is subject to routine corporate income tax audits in many of these jurisdictions. In addition, HP is subject to numerous ongoing audits by state and foreign tax authorities. HP has received from the Internal Revenue Service ("IRS") Notices of Deficiency for its fiscal 1999, 2000 and 2003 tax years and Revenue Agent's Reports ("RAR's") for its fiscal 2001 and 2002 tax years. The IRS began an audit of HP's 2004 and 2005 income tax returns in 2007. With respect to major foreign and state tax jurisdictions, HP is no longer subject to tax authority examinations for years prior to 1999. HP believes that adequate reserves have been provided for all open tax years.

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 12: Income Taxes (Continued)

HP engages in continuous discussion and negotiation with taxing authorities regarding tax matters in the various jurisdictions. HP does not expect complete resolution of any IRS audit cycle within the next 12 months. However, it is reasonably possible that certain foreign and state tax issues may be concluded in the next 12 months, including issues involving transfer pricing and other matters. Accordingly, HP believes it is reasonably possible that its existing unrecognized tax benefits may be reduced by an amount up to $320 million within the next twelve months.

The breakdown between current and long-term deferred tax assets and deferred tax liabilities was as follows:

	January 31, 2009	October 31, 2008
	In millions	
Current deferred tax assets	$ 3,515	$ 3,920
Current deferred tax liabilities	(76)	(97)
Long-term deferred tax assets	989	792
Long-term deferred tax liabilities	(2,558)	(3,162)
Total deferred tax assets net of deferred tax liabilities	$ 1,870	$ 1,453

Note 13: Stockholders' Equity

Stock Repurchase Program

HP's share repurchase program authorizes both open market and private repurchase transactions. In the first quarter of fiscal 2009, HP completed share repurchases of approximately 22 million shares. Repurchases of approximately 34 million shares were settled for $1.2 billion, which included approximately 14 million shares repurchased in transactions that were executed in fiscal 2008 but settled in the first quarter of fiscal 2009. HP had approximately 2 million shares purchased in the first quarter of fiscal 2009 but that will be settled in the second quarter of fiscal 2009. HP paid $3.3 billion in connection with share repurchases of 72 million shares during the three months ended January 31, 2008.

As of January 31, 2009, HP had remaining authorization of approximately $7.9 billion for future share repurchases under the $8.0 billion repurchase authorization approved by HP's Board of Directors on September 19, 2008.

Comprehensive Income

The changes in the components of other comprehensive income, net of taxes, were as follows:

	Three months ended January 31	
	2009	2008
	In millions	
Net earnings	$ 1,854	$ 2,133
Change in net unrealized loss on available-for-sale securities	(7)	(1)
Change in net unrealized gain on cash flow hedges	(206)	85
Change in cumulative translation adjustment	(382)	(2)
Change in unrealized components of defined benefit plans	80	(27)
Comprehensive income	$ 1,339	$ 2,188

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 13: Stockholders' Equity (Continued)

The components of accumulated other comprehensive loss, net of taxes, were as follows:

	January 31, 2009	October 31, 2008
	In millions	
Net unrealized loss on available-for-sale securities	$ (19)	$ (12)
Net unrealized gain on cash flow hedges	596	802
Cumulative translation adjustment	(1,145)	(763)
Unrealized components of defined benefit plans	(12)	(92)
Accumulated other comprehensive loss	$ (580)	$ (65)

Note 14: Retirement and Post-Retirement Benefit Plans

Acquisition of EDS

On August 26, 2008, EDS became a wholly owned subsidiary of HP. EDS sponsors qualified and non-qualified defined benefit pension plans covering substantially all of its employees. The majority of the EDS defined benefit pension plans are noncontributory. In most plans, employees become fully vested upon attaining two to five years of service, and benefits are based on many factors, which differ by country, but the most significant are years of service and earnings. The projected unit credit cost method is used for actuarial purposes. Following the acquisition of EDS, HP announced that it was modifying the EDS U.S. qualified and non-qualified plans for employees accruing benefits under the programs. Effective January 1, 2009, EDS employees in the U.S. ceased accruing pension benefits. The final pension benefit amount will be based on pay and service through December 31, 2008.

Modifications to Defined Contribution Plans

HP offers various defined contribution plans for U.S. and non-U.S. employees. As disclosed in our Consolidated Financial Statements for the fiscal year ended October 31, 2008, HP matches employee contributions to the HP 401(k) Plan with cash contributions up to a maximum of 6% of eligible compensation for U.S. employees hired prior to August 1, 2008 and up to a maximum of 4% of eligible compensation for U.S. employees hired on or after August 1, 2008. Further, effective January 1, 2009, U.S. employees participating in the EDS 401(k) Plan became eligible for a 4% HP matching contribution on eligible compensation.

Effective April 1, 2009, HP matching contributions under both the HP 401(k) Plan and the EDS 401(k) Plan will be changed to a quarterly, discretionary, performance-based match of up to a maximum of 4% of eligible compensation for all U.S. employees, which will be determined each fiscal quarter based on business results. HP matching contributions will vary from 0% to 100% of the maximum 4% match, based on factors such as quarterly earnings, market share growth, and performance relative to market and economic conditions. The first quarterly match under this new formula will be determined as of July 31, 2009 covering an extended period of April 1, 2009 through July 31, 2009.

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 14: Retirement and Post-Retirement Benefit Plans (Continued)

HP's net pension and post-retirement benefit costs were as follows:

	Three months ended January 31					
	U.S. Defined Benefit Plans		Non-U.S. Defined Benefit Plans		Post-Retirement Benefit Plans	
	2009	2008	2009	2008	2009	2008
	In millions					
Service cost	$ 6	$ 8	$ 77	$ 62	$ 3	$ 7
Interest cost	148	59	153	106	18	20
Expected return on plan assets	(133)	(64)	(165)	(165)	(8)	(10)
Amortization and deferrals:						
Actuarial (gain) loss	(13)	(9)	20		1	5
Prior service benefit			(2)	(2)	(19)	(14)
Net periodic benefit (gain) cost	8	(6)	83	1	(5)	8
Curtailment gain						
Special termination benefits			1	1		
Net benefit (gain) cost	$ 8	$ (6)	$ 84	$ 2	$ (5)	$ 8

Employer Contributions and Funding Policy

HP previously disclosed in its Consolidated Financial Statements for the fiscal year ended October 31, 2008 that it expected to contribute approximately $360 million to its non-U.S. pension plans and approximately $35 million to cover benefit payments to U.S. non-qualified plan participants in fiscal 2009. In addition, HP expected to pay approximately $70 million to cover benefit claims for HP's post-retirement benefit plans. HP's funding policy is to contribute cash to its pension plans so that it meets at least the minimum contribution requirements, as established by local government and funding and taxing authorities.

As of January 31, 2009, HP has made $157 million of contributions to non-U.S. pension plans, paid $15 million to cover benefit payments to U.S. non-qualified plan participants, and paid $12 million to cover benefit claims under post-retirement benefit plans. HP presently anticipates making additional contributions of approximately $235 million to its non-U.S. pension plans and approximately $20 million to its U.S. non-qualified plan participants and expects to pay up to $55 million to cover benefit claims under post-retirement benefit plans during the remainder of fiscal 2009. HP's pension and other post-retirement benefit costs and obligations are dependent on various assumptions. Differences between expected and actual returns on investments will be reflected as unrecognized gains or losses, and such gains or losses will be amortized and recorded in future periods. Poor financial performance of asset markets in any year could lead to increased contributions in certain countries and increased future pension plan expense. Asset gains or losses are determined at the measurement date and amortized over the remaining service life or life expectancy of plan participants. HP's next expected measurement date is October 31, 2009.

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 15: Litigation and Contingencies

HP is involved in lawsuits, claims, investigations and proceedings, including those identified below, consisting of intellectual property, commercial, securities, employment, employee benefits and environmental matters that arise in the ordinary course of business. In accordance with SFAS No. 5, "Accounting for Contingencies", HP records a provision for a liability when management believes that it is both probable that a liability has been incurred and the amount of the loss can be reasonably estimated. HP believes it has adequate provisions for any such matters. HP reviews these provisions at least quarterly and adjusts these provisions to reflect the impact of negotiations, settlements, rulings, advice of legal counsel, and other information and events pertaining to a particular case. Based on its experience, HP believes that any damage amounts claimed in the specific matters discussed below are not a meaningful indicator of HP's potential liability. Litigation is inherently unpredictable. However, HP believes that it has valid defenses with respect to legal matters pending against it. Nevertheless, it is possible that cash flows or results of operations could be materially affected in any particular period by the unfavorable resolution of one or more of these contingencies or because of the diversion of management's attention and the creation of significant expenses.

Pending Litigation, Proceedings and Investigations

Copyright levies. As described below, proceedings are ongoing against HP in certain European Union ("EU") member countries, including litigation in Germany, seeking to impose levies upon equipment (such as multifunction devices ("MFDs"), personal computers ("PCs") and printers) and alleging that these devices enable producing private copies of copyrighted materials. The total levies due, if imposed, would be based upon the number of products sold and the per-product amounts of the levies, which vary. Some EU member countries that do not yet have levies on digital devices are expected to implement similar legislation to enable them to extend existing levy schemes, while some other EU member countries are expected to limit the scope of levy schemes and applicability in the digital hardware environment. HP, other companies and various industry associations are opposing the extension of levies to the digital environment and advocating compensation to rights holders through digital rights management systems.

VerwertungsGesellschaft Wort ("VG Wort"), a collection agency representing certain copyright holders, instituted non-binding arbitration proceedings against HP in June 2001 in Germany before the arbitration board of the Patent and Trademark Office. The proceedings relate to whether and to what extent copyright levies for photocopiers should be imposed in accordance with copyright laws implemented in Germany on MFDs that allegedly enable the production of copies by private persons. Following unsuccessful arbitration, VG Wort filed a lawsuit against HP in May 2004 in the Stuttgart Civil Court in Stuttgart, Germany seeking levies on certain MFDs sold from 1997 to 2001. On December 22, 2004, the court held that HP is liable for payments regarding MFDs sold in Germany, and ordered HP to pay VG Wort an amount equal to 5% of the outstanding levies claimed, plus interest, on MFDs sold in Germany up to December 2001. VG Wort appealed this decision. On July 6, 2005, the Stuttgart Court of Appeals ordered HP to pay VG Wort levies based on the published tariffs for photocopiers in Germany (which range from EUR 38.35 to EUR 613.56 per unit), plus interest, on MFDs sold in Germany up to December 2001. HP appealed the Stuttgart Court of Appeals' decision to the Bundesgerichtshof (the German Federal Supreme Court). On January 30, 2008, the German Federal Supreme Court held that the MFDs covered by this lawsuit were photocopiers within the meaning of the German copyright law that was in effect until December 31, 2007, and, therefore, are subject to the levies on photocopiers established by that law. HP has filed a claim with the German Federal Constitutional Court challenging that ruling.

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 15: Litigation and Contingencies (Continued)

On September 26, 2005, VG Wort filed an additional lawsuit against HP in the Stuttgart Civil Court in Stuttgart, Germany seeking levies on MFDs sold in Germany between 1997 and 2001, as well as for MFDs sold from 2002 onwards. On July 26, 2007, the court issued a decision following the ruling of the Stuttgart Court of Appeals with respect to the initial VG Wort lawsuit as described above. HP has appealed the decision. HP has submitted comments on the German Federal Supreme Court judgment in the initial VG Wort lawsuit seeking levies on MFDs described above as required by the court.

In July 2004, VG Wort filed a separate lawsuit against HP in the Stuttgart Civil Court seeking levies on printers. On December 22, 2004, the court held that HP is liable for payments regarding all printers using ASCII code sold in Germany but did not determine the amount payable per unit. HP appealed this decision in January 2005 to the Higher Regional Court of Baden Wuerttemberg. On May 11, 2005, the Higher Regional Court issued a decision confirming that levies are due. On June 6, 2005, HP filed an appeal to the German Federal Supreme Court in Karlsruhe. On December 6, 2007, the German Federal Supreme Court issued a judgment that printers are not subject to levies under the existing law. The court issued a written decision on January 25, 2008, and VG Wort subsequently filed an application with the German Federal Supreme Court under Section 321a of the German Code of Civil Procedure contending that the court did not consider their arguments. On May 9, 2008, the German Federal Supreme Court denied VG Wort's application. In addition, VG Wort has filed a claim with the German Federal Constitutional Court challenging the ruling that printers are not subject to levies. HP has submitted unsolicited arguments to the latter court, and VG Wort has been directed to provide comments with respect to those arguments.

In September 2003, VG Wort filed a lawsuit against Fujitsu Siemens Computer GmbH ("FSC") in Munich State Court seeking levies on PCs. This is an industry test case in Germany, and HP has agreed not to object to the delay if VG Wort sues HP for such levies on PCs following a final decision against FSC. On December 23, 2004, the Munich State Court held that PCs are subject to a levy and that FSC must pay 12 euros plus compound interest for each PC sold in Germany since March 2001. FSC appealed this decision in January 2005 to the Higher Regional Court of Bavaria. On December 15, 2005, the Higher Regional Court affirmed the Munich State Court decision. FSC filed an appeal with the German Federal Supreme Court in February 2006. On October 2, 2008, the German Federal Supreme Court issued a judgment that PCs were not photocopiers within the meaning of the German copyright law that was in effect until December 31, 2007 and, therefore, not subject to the levies on photocopiers established by that law. VG Wort has filed a claim with the German Federal Constitutional Court challenging that ruling.

On December 29, 2005, ZPU, a joint association of various German collection societies, instituted non-binding arbitration proceedings against HP before the arbitration board of the Patent and Trademark Office demanding reporting of every PC sold by HP in Germany from January 2002 through December 2005 and seeking a levy of 18.42 euros plus tax for each PC sold during that period. HP filed a notice of defense in connection with these proceedings in February 2006, and an arbitration hearing was held in December 2006. On August 3, 2007, the arbitration board issued a ruling proposing a levy of 15 euros plus tax for each PC sold during that period. HP has rejected the ruling of the arbitration board, and the arbitration proceedings have concluded. ZPU has filed a claim with the appeals court in Munich to which HP has responded. A hearing date has been set by the court for February 18, 2010.

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 15: Litigation and Contingencies (Continued)

Based on industry opposition to the extension of levies to digital products, HP's assessments of the merits of various proceedings and HP's estimates of the units impacted and levies, HP has accrued amounts that it believes are adequate to address the matters described above. However, the ultimate resolution of these matters and the associated financial impact on HP, including the number of units impacted, the amount of levies imposed and the ability of HP to recover such amounts through increased prices, remains uncertain.

Sky Subscribers Services Limited and British Sky Broadcasting Limited v. EDS and EDS Limited (UK) is a lawsuit filed on August 17, 2004 by Sky Subscribers Services Limited and British Sky Broadcasting Limited against Electronic Data Systems Corporation ("EDS"), a company that HP acquired in August 2008, and EDS Limited (UK) ("EDS UK"), one of EDS's subsidiaries, alleging deceit, negligent misrepresentation, negligent misstatement and breach of contract. The claims arose out of a customer relationship management project that was awarded to EDS in 2000, the principal objective of which was to develop a customer call center in Scotland. EDS's main role in the project was as systems integrator. On November 12, 2004, EDS and EDS UK filed their defense and counterclaim denying the claims and seeking damages for monies owed under the contract. The trial of this action commenced on October 15, 2007, and final arguments concluded on July 30, 2008. At trial, the plaintiffs claimed damages in excess of £700 million, and EDS and EDS UK counterclaimed for damages of approximately £5 million. A decision from the court is expected in early 2009.

Skold, et al. v. Intel Corporation and Hewlett-Packard Company is a lawsuit in which HP was joined on June 14, 2004 that is pending in state court in Santa Clara County, California. The lawsuit alleges that HP (along with Intel) misled the public by suppressing and concealing the alleged material fact that systems that use the Intel Pentium 4 processor are less powerful and slower than systems using the Intel Pentium III processor and processors made by a competitor of Intel. The plaintiffs seek unspecified damages, restitution, attorneys' fees and costs, and certification of a nationwide class. On February 27, 2009, the court denied without prejudice plaintiffs' motion for nationwide class certification for a third time.

Inkjet Printer Litigation. As described below, HP is involved in several lawsuits claiming breach of express and implied warranty, unjust enrichment, deceptive advertising and unfair business practices where the plaintiffs have alleged, among other things, that HP employed a "smart chip" in certain inkjet printing products in order to register ink depletion prematurely and to render the cartridge unusable through a built-in expiration date that is hidden, not documented in marketing materials to consumers, or both. The plaintiffs have also contended that consumers received false ink depletion warnings and that the smart chip limits the ability of consumers to use the cartridge to its full capacity or to choose competitive products.

A consolidated lawsuit captioned *In re HP Inkjet Printer Litigation* is pending in the United States District Court for the Northern District of California where the plaintiffs are seeking class certification, restitution, damages (including enhanced damages), injunctive relief, interest, costs, and attorneys' fees. On January 4, 2008, the court heard plaintiffs' motions for class certification and to add a class representative and HP's motion for summary judgment. On July 25, 2008, the court denied all three motions. Plaintiffs have indicated an intention to seek certification of a class of California consumers only.

A lawsuit captioned *Blennis v. HP* was filed on January 17, 2007 in the United States District Court for the Northern District of California where the plaintiffs are seeking class certification,

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 15: Litigation and Contingencies (Continued)

restitution, damages (including enhanced damages), injunctive relief, interest, costs, and attorneys' fees.

Four class actions against HP and its subsidiary, Hewlett-Packard (Canada) Co., are pending in Canada, one commenced in British Columbia in February 2006, two commenced in Quebec in April 2006 and May 2006, respectively, and one commenced in Ontario in June 2006, where the plaintiffs are seeking class certification, restitution, declaratory relief, injunctive relief and unspecified statutory, compensatory and punitive damages.

Baggett v. HP is a consumer class action filed against HP on June 6, 2007 in the United States District Court for the Central District of California alleging that HP employs a technology in its LaserJet color printers whereby the printing process shuts down prematurely, thus preventing customers from using the toner that is allegedly left in the cartridge. The plaintiffs also allege that HP fails to disclose to consumers that they will be unable to utilize the toner remaining in the cartridge after the printer shuts down. The complaint seeks certification of a nationwide class of purchasers of all HP LaserJet color printers and seeks unspecified damages, restitution, disgorgement, injunctive relief, attorneys' fees and costs.

Rich v. HP is a consumer class action filed against HP on May 22, 2006 in the United States District Court for the Northern District of California. The suit alleges that HP designed its color inkjet printers to unnecessarily use color ink in addition to black ink when printing black and white images and text. The plaintiffs seek injunctive and monetary relief on behalf of a nationwide class.

On December 27, 2001, *Cornell University* and the *Cornell Research Foundation, Inc.* filed a complaint, amended on September 6, 2002, against HP in United States District Court for the Northern District of New York alleging that HP's PA-RISC 8000 family of microprocessors, and servers and workstations incorporating those processors, infringe a patent assigned to Cornell Research Foundation, Inc. that describes a way of executing microprocessor instructions. The complaint sought declaratory and injunctive relief and unspecified damages. The patent at issue in this litigation, United States Patent No. 4,807,115, expired on February 21, 2006. Therefore, the plaintiffs are no longer entitled to seek injunctive relief against HP. This matter was tried between May 19 and May 30, 2008, and, on May 30, 2008, a jury returned a verdict in favor of the plaintiffs in the amount of $184 million. The court has not yet entered a final judgment, and it will not do so until after it rules on HP's equitable defenses and HP's post-trial motions to vacate the judgment and/or to reduce the amount of damages awarded by the jury. Depending on the outcome of HP's defenses and post-trial motions, HP may file an appeal with the Federal Circuit Court of Appeals.

CSIRO Patent Litigation. *Microsoft Corporation, Hewlett-Packard Company, et al. v. Commonwealth Scientific and Industrial Research Organisation of Australia* is an action filed by HP and two other plaintiffs on May 9, 2005, in the District Court for the Northern District of California seeking a declaratory judgment against Commonwealth Scientific and Industrial Research Organisation of Australia ("CSIRO") that HP's products employing the IEEE 802.11a and 802.11g wireless protocol standards do not infringe CSIRO's United States Patent No. 5,487,069 relating to wireless transmission of data at frequencies in excess of 10GHz. On September 22, 2005, CSIRO filed an answer and counterclaims alleging that all HP products which employ those wireless protocol standards infringe the CSIRO patent and seeking damages, including enhanced damages and attorneys' fees and costs, and an injunction against sales of infringing products. On December 12, 2006, CSIRO successfully moved to have the case transferred to the District Court of the Eastern District of Texas. In March 2009, the

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 15: Litigation and Contingencies (Continued)

parties reached an understanding to settle the matter and dismiss the pending lawsuit. The proposed settlement provides for HP to pay CSIRO an amount of money that is immaterial to HP in exchange for protection from claims of infringement of the patent at issue, including all United States and worldwide continuations and counterparts of that patent, in the form of a combination of licenses and covenants not to sue. The parties are in the process of preparing a definitive settlement agreement.

The United States of America, ex rel. Norman Rille and Neal Roberts v. Hewlett-Packard Company, et al. In 2004, two private individuals filed a civil "*qui tam*" complaint under the False Claims Act in the United States District Court for the Eastern District of Arkansas containing generalized allegations that HP and several other companies participated in an industry-wide practice of using partnership and alliance programs to make improper payments and cause the submission of false claims in connection with contracts to provide products and services to the federal government. On April 12, 2007, the U.S. Department of Justice intervened in the *qui tam* action and filed a complaint against HP (and several other companies in separate actions) on behalf of the United States containing allegations that HP violated the False Claims Act and the Anti-Kickback Act of 1986 by providing millions of dollars in kickbacks to its alliance partners, including "influencer fees" and "new business opportunity rebates." The U.S. complaint further alleges that HP violated the False Claims Act and the Anti-Kickback Act, breached its federal government contracts, induced the federal government to make payments to HP that HP was not entitled to receive under those contracts, and was unjustly enriched by expressly or impliedly making false statements, records or certifications to the federal government that it complied with and would continue to comply with the Anti-Kickback Act and by submitting claims to the government that allegedly were inflated because they included the amounts of the influencer fees and new business opportunity rebates. The U.S. complaint seeks treble damages plus civil penalties in connection with the alleged violations of the False Claims Act, double damages plus civil penalties in connection with the alleged violations of the Anti-Kickback Act and disgorgement of profits earned in connection with the breach of contract and unjust enrichment claims.

Leak Investigation Proceedings. As described below, HP is or has been the subject of various governmental inquiries concerning the processes employed in an investigation into leaks of HP confidential information to members of the media that concluded in May 2006:

In August 2006, HP was informally contacted by the Attorney General of the State of California requesting information concerning the processes employed in the leak investigation. On December 7, 2006, HP announced that it entered into an agreement with the California Attorney General to resolve civil claims arising from the leak investigation, including a claim made by the California Attorney General in a Santa Clara County Superior Court action filed on December 7, 2006, that HP committed unfair business practices under California law in connection with the leak investigation. As a result of this agreement, which includes an injunction, the California Attorney General will not pursue civil claims against HP or its current and former directors, officers and employees. Under the terms of the agreement, HP paid a total of $14.5 million and agreed to implement and maintain for five years a series of measures designed to ensure that HP's corporate investigations are conducted in accordance with California law and the company's high ethical standards. Of the $14.5 million, $13.5 million has been used to create a Privacy and Piracy Fund to assist California prosecutors in investigating and prosecuting consumer privacy and information piracy violations, $650,000 was used to pay statutory damages and $350,000 reimbursed the California Attorney General's office for its investigation costs. There was no finding of liability against HP as part of the settlement.

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 15: Litigation and Contingencies (Continued)

Beginning in September 2006, HP received requests from the Committee on Energy and Commerce of the U.S. House of Representatives (the "Committee") for records and information concerning the leak investigation, securities transactions by HP officers and directors, including an August 25, 2006, securities transaction by Mark Hurd, HP's Chairman and Chief Executive Officer, and related matters. HP has responded to those requests. In addition, Mr. Hurd voluntarily gave testimony to the Committee regarding the leak investigation on September 28, 2006.

In September 2006, HP was informally contacted by the U.S. Attorney for the Northern District of California requesting similar information concerning the processes employed in the leak investigation. HP has responded to that request.

Beginning in September 2006, HP has received requests from the Division of Enforcement of the Securities and Exchange Commission for records and information and interviews with current and former HP directors and officers relating to the leak investigation, the resignation of Thomas J. Perkins from HP's Board of Directors, HP's May 22, 2006 and September 6, 2006 filings with the SEC on Form 8-K, stock repurchases by HP and securities transactions by its officers and directors that occurred between May 1 and October 1, 2006, and HP's policies, practices and approval of securities transactions. In May 2007, HP consented to the entry of an order by the SEC ordering HP to cease and desist from committing or causing violations of the public reporting requirements of the Securities Exchange Act of 1934, as amended. HP has been advised by the staff of the Division of Enforcement that the staff has completed its investigation and does not intend to recommend that any other SEC enforcement action be brought in connection with these matters.

In September 2006, HP received a request from the U.S. Federal Communications Commission for records and information relating to the processes employed in the leak investigation. HP has responded to that request.

In addition, four stockholder derivative lawsuits have been filed in California purportedly on behalf of HP stockholders seeking to recover damages for alleged breach of fiduciary duty and to require HP to improve its corporate governance and internal control procedures as a result of the activities of the leak investigation: *Staehr v. Dunn, et al.* was filed in Santa Clara County Superior Court on September 18, 2006; *Worsham v. Dunn, et al.* was filed in Santa Clara County Superior Court on September 14, 2006; *Tansey v. Dunn, et al.* was filed in Santa Clara County Superior Court on September 20, 2006; and *Hall v. Dunn, et al.* was filed in Santa Clara County Superior Court on September 25, 2006. On October 19, 2006, the Santa Clara County Superior Court consolidated the four California cases under the caption *In re Hewlett-Packard Company Derivative Litigation*. The consolidated complaint filed on November 19, 2006, also seeks to recover damages in connection with sales of HP stock alleged to have been made by certain current and former HP officers and directors while in possession of material non-public information. Two additional stockholder derivative lawsuits, *Pifko v. Babbio, et al.*, filed on September 19, 2006, and *Gross v. Babbio, et al.*, filed on November 21, 2006, were filed in Chancery Court, County of New Castle, Delaware; both seek to recover damages for alleged breaches of fiduciary duty and to obtain an order instructing the defendants to refrain from further breaches of fiduciary duty and to implement corrective measures that will prevent future occurrences of the alleged breaches of fiduciary duty. On January 24, 2007, the Delaware court consolidated the two cases under the caption *In re Hewlett-Packard Company Derivative Litigation* and subsequently stayed the proceedings, as the parties had reached a tentative settlement. The HP Board of Directors appointed a Special Litigation Committee consisting of

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 15: Litigation and Contingencies (Continued)

independent Board members authorized to investigate, review and evaluate the facts and circumstances asserted in these derivative matters and to determine how HP should proceed in these matters. On December 14, 2007, HP and the plaintiffs in the California and Delaware derivative actions entered into an agreement to settle those lawsuits. Under the terms of the settlement, HP agreed to continue certain corporate governance changes until December 31, 2012 and to pay the plaintiffs' attorneys' fees. The California court granted final approval to the settlement on March 11, 2008 and subsequently granted plaintiffs' counsel's fee application and dismissed the action. On June 12, 2008, the Delaware court granted final approval to the settlement and the plaintiffs' application for attorneys' fees and also dismissed the action. Because neither the dismissal of the California nor the Delaware derivative action was thereafter appealed, both cases are now concluded.

Concluded Litigation

Schorsch v. HP was a consumer class action filed against HP on October 28, 2003 in Illinois state court alleging that HP had included an electrically erasable programmable read only memory (EEPROM) chip in certain of its LaserJet printers that prematurely advises the user that the drum kit needs replacing in violation of Illinois state law. The plaintiffs subsequently filed an amended complaint seeking to expand the class from purchasers of drum kits to purchasers of all HP printer consumables that contain EEPROM chips. The plaintiffs sought certification of an Illinois-only class and seeks unspecified damages, attorneys' fees and costs. The action was dismissed by the court with prejudice on December 20, 2008.

Environmental

HP is subject to various federal, state, local and foreign laws and regulations concerning environmental protection, including laws addressing the discharge of pollutants into the air and water, the management and disposal of hazardous substances and wastes, the cleanup of contaminated sites, the content of its products and the recycling, treatment and disposal of its products including batteries. In particular, HP faces increasing complexity in its product design and procurement operations as it adjusts to new and future requirements relating to the chemical and materials composition of its products, their safe use, the energy consumption associated with those products and product take-back legislation. HP could incur substantial costs, its products could be restricted from entering certain jurisdictions, and it could face other sanctions, if it were to violate or become liable under environmental laws or if its products become non-compliant with environmental laws. HP's potential exposure includes fines and civil or criminal sanctions, third-party property damage or personal injury claims and clean up costs. The amount and timing of costs under environmental laws are difficult to predict.

HP is party to, or otherwise involved in, proceedings brought by U.S. or state environmental agencies under the Comprehensive Environmental Response, Compensation and Liability Act ("CERCLA"), known as "Superfund," or state laws similar to CERCLA. HP is also conducting environmental investigations or remediations at several current or former operating sites pursuant to administrative orders or consent agreements with state environmental agencies.

HP is also subject to legislation in an increasing number of jurisdictions that makes producers of electrical goods, including computers and printers, financially responsible for specified collection, recycling, treatment and disposal of past and future covered products (sometimes referred to as "product take-back legislation"). For example, the European Union ("EU") adopted the Waste

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 15: Litigation and Contingencies (Continued)

Electrical and Electronic Equipment Directive in January 2003. That directive makes producers of electrical goods, including computers and printers, financially responsible for specified collection, recycling, treatment and disposal of past and future covered products. The EU member states were obliged to make producers participating in the market financially responsible for implementing these responsibilities.

Note 16: Segment Information

Description of Segments

HP is a leading global provider of products, technologies, software, solutions and services to individual consumers, small and medium sized businesses ("SMBs"), and large enterprises including the public and education sectors. HP's offerings span personal computing and other access devices; imaging and printing-related products and services; enterprise information technology ("IT") infrastructure, including enterprise storage and server technology; software that optimizes business technology investments; financial services including leasing; and multi-vendor customer services, including technology support and maintenance, consulting and integration, information technology and business process outsourcing services and application services.

HP and its operations are organized into seven business segments for financial reporting purposes: Services, Enterprise Storage and Servers ("ESS"), HP Software, the Personal Systems Group ("PSG"), the Imaging and Printing Group ("IPG"), HP Financial Services ("HPFS"), and Corporate Investments. HP's organizational structure is based on a number of factors that management uses to evaluate, view and run its business operations, which include, but are not limited to, customer base, homogeneity of products and technology. The business segments disclosed in the accompanying Consolidated Condensed Financial Statements are based on this organizational structure and information reviewed by HP's management to evaluate the business segment results. Services, ESS and HP Software are reported collectively as a broader Technology Solutions Group ("TSG"). In order to provide a supplementary view of HP's business, aggregated financial data for TSG is presented herein.

HP has reclassified segment operating results for fiscal 2008 and fiscal 2007 to conform to certain fiscal 2009 organizational realignments. None of the changes impacts HP's previously reported consolidated net revenue, earnings from operations, net earnings or net earnings per share. Future changes to this organizational structure may result in changes to the business segments disclosed. A description of the types of products and services provided by each business segment follows.

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 16: Segment Information (Continued)

Technology Solutions Group.

Each of the business segments within TSG is described in detail below.

Services, formerly HP Services, was renamed after the reorganization of the business units subsequent to the acquisition of EDS. Services provides consulting, outsourcing, and technology services across infrastructure, applications, and business process domains. Services delivers to its clients by leveraging investments in consulting and support professionals, infrastructure technology, applications, standardized methodologies, and global supply and delivery. It is divided into four main business units: applications services ("AS"), infrastructure technology outsourcing ("ITO"), business process outsourcing ("BPO") and technology services ("TS"). AS provides a full lifecycle of service offerings to support diverse client requirements, including transformation and modernization services, applications development and applications management. ITO offers four service lines: data center services, workplace services, security compliance and continuity services, and networking services. BPO is powered by a platform of underlying infrastructure technology, applications and standardized methodologies. It includes four main service lines: enterprise shared services, customer relationship management, financial process management services and administrative services. TS provides services and warranty support across HP's product lines. TS also provides multivendor support to products and environments that are consistent with HP's stated growth strategy. TS specializes in proactive mission-critical support, datacenter transformation and infrastructure services for storage and server environments, as well as unified communication environments and networks. TS offers product support in the form of installation and startup services, hardware and software support, education and training, warranty extensions and replacement parts. Service and support offerings from TS are available in the form of service contracts, pre-packaged offerings or on an individual basis and are available from HP directly or through HP authorized channel partners.

Enterprise Storage and Servers provides storage and server products. The various server offerings range from entry-level servers to high-end scalable servers, including Superdome servers. Industry standard servers include primarily entry-level and mid-range ProLiant servers, which run primarily Windows®[1], Linux and Novell operating systems and leverage Intel Corporation ("Intel") and Advanced Micro Devices ("AMD") processors. The business spans a range of product lines, including pedestal-tower servers, density-optimized rack servers and HP's BladeSystem family of server blades. Business critical systems include Itanium®[2]-based Integrity servers running on HP-UX, Windows®, Linux, OpenVMS and NonStop operating systems, including the high-end Superdome servers and fault-tolerant Integrity NonStop servers. Business critical systems also include the Reduced Instruction Set Computing ("RISC")-based servers with the HP 9000 line running on the HP-UX operating system, HP AlphaServers running on both Tru64 UNIX®[3] and OpenVMS, and MIPs-based NonStop servers. HP's StorageWorks offerings include entry-level, mid-range and high-end arrays, storage area networks ("SANs"), network attached storage ("NAS"), storage management software, and virtualization technologies, as well as tape drives, tape libraries and optical archival storage.

---

(1) Windows® is a registered trademark of Microsoft Corporation.

(2) Itanium® is a registered trademark of Intel Corporation.

(3) UNIX® is a registered trademark of The Open Group.