

IN THE UNITED STATES DISTRICT COURT  
FOR THE NORTHERN DISTRICT OF GEORGIA  
ATLANTA DIVISION

JOHN MIZZARO, on behalf of himself and : CIVIL ACTION NO.  
all others similarly situated : 1:06-CV-1151-ODE

v. :

HOME DEPOT, INC., ROBERT L. NARDELLI, : JURY TRIAL DEMANDED  
CAROL B. TOME, KENNETH G. LANGONE, :  
BERRY R. COX, JOHN L. CLENDENIN, AND :  
LARRY M. MERCER :

BRUCE B. BELDOFF, on behalf of himself and : CIVIL ACTION NO.  
all others similarly situated : 1:06-CV-1349-ODE

v. :

HOME DEPOT, INC., ROBERT L. NARDELLI, : JURY TRIAL DEMANDED  
CAROL B. TOME, KENNETH G. LANGONE, :  
BERRY R. COX, JOHN L. CLENDENIN, AND :  
LARRY M. MERCER :

M. BRAD BICKERSTAFF, on behalf of himself : CIVIL ACTION NO.  
and all others similarly situated : 1:06-CV-1197-ODE

v. :

HOME DEPOT, INC., ROBERT L. NARDELLI, : JURY TRIAL DEMANDED  
CAROL B. TOME, KENNETH G. LANGONE, :  
BERRY R. COX, JOHN L. CLENDENIN, AND :  
LARRY M. MERCER :

(Captions continued on next page)

PAUL COBLE on behalf of himself  
and all others similarly situated,

v.

HOME DEPOT, INC., ROBERT L. NARDELLI,  
CAROL B. TOME, KENNETH G. LANGONE,  
BERRY R. COX, JOHN L. CLENDENIN, AND  
LARRY M. MERCER

: CIVIL ACTION NO.  
: 1:06-CV-1616-ODE  
:  
:  
:

JURY TRIAL DEMANDED

ROBERT D. JAFFEE AS TRUSTEE OF THE  
ROBERT D. JAFFEE REVOCABLE TRUST,  
on behalf of himself and all others similarly  
situated

v.

HOME DEPOT, INC., ROBERT L. NARDELLI,  
CAROL B. TOME, KENNETH G. LANGONE,  
BERRY R. COX, JOHN L. CLENDENIN, AND  
LARRY M. MERCER

: CIVIL ACTION NO.  
: 1:06-CV-1617-ODE  
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JURY TRIAL DEMANDED

**AMENDED CLASS ACTION COMPLAINT**

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Lead Plaintiff Bucks County  
Retirement Board*

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Lead Plaintiff Bucks County  
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Lead Plaintiff, Bucks County Retirement Board (“Bucks County” or “Lead Plaintiff”), brings this action as a class action individually and on behalf of all other persons or entities that purchased The Home Depot, Inc. (“Home Depot” or the “Company”) common stock during the period May 29, 2001 through and including February 22, 2005 (the “Class Period”).

Lead Plaintiff’s information and belief is based on, *inter alia*, an investigation made by and through its undersigned counsel, which included, among other things, a review of (1) Home Depot’s public filings with the Securities and Exchange Commission (“SEC”); (2) analyst research reports; (3) transcripts of Home Depot investor conference calls; (4) press releases and media reports related to the Company’s operations and financial results; (5) interviews and consultations with former Home Depot Company employees; (6) allegations made in “whistleblower” complaints brought by former Company employees in connection with fraudulent conduct alleged herein; (7) statements of current and former employees reported by the media; and (8) various documents related to the Company’s return-to-vendor practices.

Lead Plaintiff’s investigation into the facts and circumstances alleged herein is continuing, as are an investigation by the SEC, whistleblower

actions filed by former Home Depot employees, and an internal investigation by the Company. Therefore, it is likely that additional facts related to the claims set forth below may be revealed.

Many of the facts supporting the allegations contained herein are known only to the defendants or are exclusively within their custody or control. Lead Plaintiff believes that further substantial evidentiary support will exist for the allegations in this Complaint after Lead Plaintiff has a reasonable opportunity for discovery.

### **NATURE OF THE ACTION**

1. During the Class Period, the defendants named in this Action artificially inflated the Company's financial results by processing billions of dollars of fraudulent return-to-vendor ("RTV") chargebacks. The scheme entailed misleading investors into believing that Home Depot was meeting or exceeding Wall Street's published estimates for the Company's quarterly and yearly earnings growth targets when, in reality, the Company "made its numbers" only by processing fraudulent RTV chargebacks in an accounting scheme that violated the most basic Generally Accepted Accounting Principles ("GAAP").

2. The pervasiveness, magnitude and duration of the accounting fraud are extraordinary. According to current and former Home Depot employees, Home Depot stores across the country processed fraudulent RTV chargebacks in a scheme orchestrated by the Company's most senior management. The scheme allowed the Company to collect billions of dollars in fraudulent RTV chargebacks that by some accounts amounted to roughly ten percent of the Company's annual pre-tax earnings. The scheme began as early as 2000, and perhaps much earlier.

3. While the pervasiveness, magnitude and duration of the accounting fraud are extraordinary, the story behind it is not. The illicit scheme allowed the Company to sell merchandise at 100% pure profit because the RTV chargeback offset the cost, or to conceal merchandise that was missing from the Company's inventory because of theft, damage or in-store use and that would otherwise be written-down, having an adverse impact on the Company's earnings and gross margins.

4. Aware of the existence of the fraud, the defendants sought to overhaul the RTV system at least as early as the summer of 2003 to "reinforce desired behaviors" and to track the "true defective rate" of supposedly defective merchandise subject to RTV chargebacks. However,

the defendants deliberately ignored the misconduct until the Company finally rolled-out the overhauled RTV system in October 2004, which essentially put an end to the fraud.

5. With the immediate and material loss of fraudulent RTV revenue, on February 22, 2005 (the last day of the Class Period), the Company disclosed that 2004 fourth quarter revenue and earnings growth had fallen short of historical levels, but omitted any reference to the extent to which the absence of improper RTV revenue had adversely affected the Company's financial results.

6. Following the February 22, 2005 earnings release, the Company's share price declined precipitously. On February 18, 2005 (the last trading day prior to the February 22, 2005 release), the price of Home Depot's shares closed at \$42.02 per share. On February 22, 2005, the price of Home Depot shares closed at \$40.28. By the close of trading on February 23, 2005, Home Depot's per share price had fallen to \$39.75, an over 5% drop from February 18, 2005. By the close of trading on April 28, 2005, Home Depot's shares had plummeted to \$35.09 per share, representing a decline of over 16% and a market capitalization loss of \$16.5 billion.

7. In the wake of the stock price fall, a number of former Home Depot employees, including the former director of Home Depot's Northwest Division responsible for over 300 stores, have come forward and revealed the Company's astonishing scheme to "cook the books." Former employees have recounted the scheme and many reported that the order to "cook the books" came directly from Company management, pointing to, *inter alia*, an April 2002 company memorandum that encouraged store managers to "boost chargebacks."

8. The Company's fraudulent RTV practices are now the focus of an SEC investigation, as well as the subject of at least two whistleblower actions brought by former employees.

9. Lead Plaintiff and members of the Class have suffered substantial damages as a direct and proximate result of the fraud alleged herein.

### **JURISDICTION AND VENUE**

10. The Court has jurisdiction over the subject matter of this action pursuant to Section 27 of the Securities Exchange Act of 1934 (the "Exchange Act"), 15 U.S.C. § 78aa, and 28 U.S.C. §§ 1331 and 1337. The claims arise under Sections 10(b) and 20(a) of the Exchange Act, 15 U.S.C.

§§ 78j(b) and 78t(a), and the rules and regulations promulgated thereunder, including SEC Rule 10b-5, 17 C.F.R. § 240.10b-5.

11. Venue is proper in this District pursuant to Section 27 of the Exchange Act and 28 U.S.C. § 1391(b). Many of the acts and transactions giving rise to the violations of law complained of herein, including the preparation and dissemination to the public of materially false and misleading public filings, occurred in this District. Further, at all relevant times herein, Home Depot maintained its principal executive offices in this District, at 2455 Paces Ferry Road, N.W., Atlanta, Georgia 30339.

12. In connection with the wrongful acts and conduct alleged herein, the defendants directly or indirectly used the means and instrumentalities of interstate commerce, including the United States mails and the facilities of a national securities exchange.

## **PARTIES**

### **A. Lead Plaintiff**

13. Lead Plaintiff, Bucks County Retirement Board, is a public pension fund organized for the benefit of various current and retired employees of Bucks County, Pennsylvania. Lead Plaintiff is located in Doylestown, Pennsylvania, and during the Class Period purchased 71,175

shares of Home Depot common stock for approximately \$2,656,561, as set forth in the certification that Lead Plaintiff previously filed with the Court. Lead Plaintiff suffered damages as a result of the violations of the federal securities laws alleged herein when the value of its holdings dropped as a direct and proximate result of the fraud that is particularized below. By Order entered September 26, 2006, the Court appointed Bucks County Retirement Board as a preliminary lead plaintiff in this Action pursuant to 15 U.S.C. § 78u-4.

**B. Defendants**

14. Defendant Home Depot is a Delaware corporation with its principal executive offices located at 2455 Paces Ferry Road, N.W., Atlanta, Georgia. The Company files quarterly and annual reports with the SEC, and its common stock is listed and traded on the New York Stock Exchange (“NYSE”) under the symbol “HD.” Home Depot is a component of the Standard & Poor’s 500 Index and Dow Jones 30 Industrial Average. At the end of Home Depot’s fiscal year 2005, the Company reportedly operated 2,042 stores that sold a wide assortment of building materials, home improvement and lawn and garden products, and offered a variety of installation services.

15. **Robert L. Nardelli (“Nardelli”).** Defendant Nardelli has been President and Chief Executive Officer (“CEO”) of Home Depot since December 2000, and Chairman of the Board since January 2002. Throughout the Class Period, Nardelli signed the Company’s annual reports filed with the SEC on Form 10-K and made numerous statements on conference calls, investor meetings, press releases and interviews, as more particularly set forth below. At all times relevant herein, Nardelli was responsible for reviewing the Company’s annual, quarterly and periodic reports filed with the SEC, and during the Class Period certified that he had reviewed each of the annual reports filed with the SEC and that they fairly presented, in all material respects, the Company’s financial conditions and operating results.

16. On August 26, 2002, pursuant to Order No. 4-460 of the Securities and Exchange Commission, Nardelli executed a “Statement Under Oath of Principal Executive Officer and Principal Financial Officer Regarding Facts and Circumstances Relating to Exchange Act Filings.” In this statement, Nardelli attested that he had reviewed the Company’s annual report for the fiscal year ended February 3, 2002 as filed with the SEC on Form 10-K on April 19, 2002 (“2001 Form 10-K”), and that it did not

contain untrue statements of material fact or omit to state material facts necessary to make the statements made, in light of the circumstances under which they were made, not misleading. He also attested that he had “reviewed the contents of this statement with the Company's audit committee.”

17. **Carol B. Tomé (“Tomé”).** Defendant Tomé has been Executive Vice President and Chief Financial Officer (“CFO”) of Home Depot since May 2001. Tomé was the Company’s Senior Vice President of Finance from February 2000 to May 2001, and Vice President and Treasurer from 1995 until 2000. As CFO, Tomé was responsible for all corporate finance matters, including financial reporting, planning and analysis.

18. Throughout the Class Period, Tomé signed the Company’s annual reports filed with the SEC on Form 10-K and made numerous statements on conference calls, investor meetings, press releases and interviews related to the Company’s financial results and operations, as more particularly set forth below. Throughout the Class Period, Tomé was responsible for reviewing the Company’s annual, quarterly and periodic reports filed with the SEC, that certified that she had reviewed the

Company's annual reports and that they fairly presented, in all material respects, the Company's financial conditions and operating results.

19. On August 26, 2002, pursuant to Order No. 4-460 of the Securities and Exchange Commission, Tomé executed a "Statement Under Oath of Principal Executive Officer and Principal Financial Officer Regarding Facts and Circumstances Relating to Exchange Act Filings." In this statement, Tomé attested that she had reviewed the 2001 Form 10-K and that it did not contain untrue statements of a material fact or omit to state material facts necessary to make the statements made, in light of the circumstances under which they were made, not misleading. She also attested that she had "reviewed the contents of this statement with the Company's audit committee."

20. **Larry M. Mercer ("Mercer")**. Defendant Mercer served as Home Depot's Executive Vice President of Store Operations during the Class Period until he left the Company in August 2002. In that capacity, Mercer was responsible for overseeing Home Depot's retail operations. Following his retirement, Defendant Mercer served as an advisor to Nardelli until February 2004.

21. In April 2002, while employed as the Company's Executive Vice President of Store Operations, Mercer wrote and circulated a memorandum to Home Depot store managers that addressed "missed RTV dollars." According to an August 4, 2005 article that appeared in *The New York Post*, the memorandum discussed "specific categories, such as the electrical and flooring departments, that had the greatest opportunity to boost chargebacks, and estimated that on a companywide basis Home Depot was missing out on more than \$59 million in credits." Mercer actively participated in the scheme, plan and course of conduct that defrauded Lead Plaintiff and the other Class members during the Class Period.

22. **Kenneth G. Langone ("Langone").** Defendant Langone was a co-founder of Home Depot and, according to the Company's Definitive Proxy Statement filed with the SEC on April 11, 2005 (the "2005 Proxy Statement"), beneficially owned over 17 million shares of Home Depot stock during the Class Period.

23. Langone has been a member of the Company's Board of Directors since 1978 and served as Home Depot's "Lead Director" throughout the Class Period. According to the 2005 Proxy Statement, as Lead Director, Langone (a) acted as a liaison between non-management

directors and Company management; (b) chaired the executive sessions of non-management directors; and (c) consulted with the Chairman of the Board on the agenda for Board meetings and other matters pertinent to the Company and the Board.

24. Throughout the Class Period, Langone was also a member of the “Executive Committee” and the “Nominating and Corporate Governance Committee” of the Company’s Board of Directors. According to each of the Company’s proxy statements filed with the SEC during the Class Period, the Nominating and Corporate Governance Committee is responsible for, *inter alia*, overseeing the Company’s corporate governance practices and procedures.

25. According to the 2005 Proxy Statement, Langone also served on the Audit Committee for the Board of Directors during (at least) fiscal year 2004. According to the Company's Audit Committee Charter (the “Charter”), which was appended to the Company’s 2004 Proxy Statement filed with the SEC on April 12, 2004 (the “2004 Proxy Statement”), the primary purposes of the Audit Committee is to “assist the Board of Directors in fulfilling its oversight of ... the integrity of the Company's financial statements” and “the performance of the Company's internal audit

function....” The Charter adds that “[i]n fulfilling its purpose, the [Audit] Committee shall review (a) the financial reports and other financial information of the Company; (b) the Company's systems of internal controls and procedures and disclosure controls and procedures; and (c) the Company's auditing, accounting and financial reporting processes generally.”

26. A June 2002 article in *Fortune* referred to Defendant Langone as “arguably the most powerful person at Home Depot.” Langone was reportedly responsible for recruiting Nardelli to become Home Depot’s CEO in 2000.

27. **Berry R. Cox (“Cox”).** Defendant Cox was a Director of Home Depot from 1978 until June 2005. In a statement issued in June 2005, Home Depot described Cox as “one of [Home Depot’s] original investors” and a “steadfast supporter of the company through each phase of our growth over the past 25 years.” From the beginning of the Class Period until August 2002, Defendant Cox served as the Chairman of Home Depot’s Audit Committee.

28. **John L. Clendenin (“Clendenin”).** Defendant Clendenin has been a Director of Home Depot since 1996. From August 2002 through

the end of the Class Period, Clendenin served as Chairman of Home Depot's Audit Committee.

29. As chairpersons of the Audit Committee during part of the Class Period, Cox and Clendenin had the responsibility to, among other things, monitor the Company's financial reporting processes and internal control systems and review the Company's financial statements prior to their public dissemination. Cox and Clendenin knew that Home Depot's public filings would incorporate and reference the Company's financial statements. Consequently, Cox and Clendenin had an obligation to ensure that those financial statements were not false and misleading as set forth below. Nevertheless, as detailed herein, because of Cox and Clendenin's knowing or severely reckless disregard of the truth, Home Depot published materially false and misleading financial statements during the Class Period.

30. Nardelli, Tomé, Mercer, Langone, Cox and Clendenin are at times collectively referred to herein as the "Individual Defendants." The Individual Defendants and Home Depot are collectively referred to as the "Defendants."

**GROUP PLEADING DOCTRINE**

31. By virtue of the Individual Defendants' positions within the Company, they had access to undisclosed adverse information about Home Depot's business, operations, operational trends, finances, and present and future business prospects. The Individual Defendants would ascertain such information through Home Depot's internal corporate documents (including the Company's operating plans, budgets and forecasts and reports of actual operations compared thereto), conversations and connections with other Home Depot corporate officers and employees, conversations and connections with vendors and customers, attendance at sales, management, and Board of Directors' meetings, including committees thereof, and through reports and other information provided to them in connection with their roles and duties as Home Depot officers or directors.

32. It is appropriate to treat the Individual Defendants collectively as a group for pleading purposes and to presume that the materially false, misleading and incomplete information conveyed in the Company's public filings and press releases as alleged herein was the result of the collective actions of the Individual Defendants. The Individual Defendants, by virtue of their high-level positions within the Company,

directly participated in the management of the Company, were directly involved in the day-to-day operations of the Company at the highest levels and were privy to confidential proprietary information concerning the Company and its business, operations, prospects, growth, finances, and financial condition, as alleged herein.

33. The Individual Defendants were involved in drafting, producing, reviewing, approving and/or disseminating the materially false and misleading statements and information alleged herein, including SEC filings, press releases, and other public documents, were aware of or recklessly disregarded the fact that materially false and misleading statements were being issued regarding the Company, and approved or ratified these statements, in violation of the federal securities laws.

34. As officers and/or directors and controlling persons of a publicly-held company whose common stock was, and is, registered with the SEC pursuant to the Exchange Act, and was traded on the NYSE, and governed by the provisions of the federal securities laws, the Individual Defendants each had a duty to promptly disseminate accurate and truthful information with respect to the Company's financial condition and performance, growth, operations, financial statements, business, markets,

management, earnings and present and future business prospects, and to correct any previously issued statements that had become materially misleading or untrue, so that the market price of the Company's publicly traded securities would be based upon truthful and accurate information. The Individual Defendants' material misrepresentations and omissions during the Class Period violated these specific requirements and obligations.

35. The Individual Defendants, by virtue of their positions of control and authority as officers or directors of the Company, were able to and did control the content of the various SEC filings, press releases and other public statements pertaining to the Company during the Class Period. The Individual Defendants were provided with copies of the documents alleged herein to be misleading prior to or shortly after their issuance and/or had the ability and/or opportunity to prevent their issuance or cause them to be corrected. Accordingly, they are responsible for the accuracy of the public reports and releases detailed herein.

### **CLASS ACTION ALLEGATIONS**

36. Lead Plaintiff brings this action as a class action pursuant to Federal Rules of Civil Procedure 23(a) and 23(b)(3) on behalf of a class consisting of all persons or entities who purchased Home Depot common

stock during the period May 29, 2001 through and including February 22, 2005 (the “Class Period”), and who suffered damages thereby (the “Class”). Excluded from the Class are (i) the Defendants; (ii) members of the family of each Individual Defendant; (iii) any person who was an officer or director of Home Depot during the Class Period; (iv) any firm, trust, corporation, officer, or other entity in which any Defendant has a controlling interest; and (v) the legal representatives, agents, affiliates, heirs, successors-in-interest or assigns of any such excluded party.

37. The members of the Class are so numerous that joinder of all members is impracticable. While the exact number of Class members is unknown to Lead Plaintiff at the present time and can only be ascertained from books and records maintained by Home Depot and/or its agent(s), Lead Plaintiff believes that there are, at a minimum, thousands of members of the Class who purchased Home Depot common stock during the Class Period. As of February 22, 2005, Home Depot had over 2 billion shares of common stock issued and outstanding. Throughout the Class Period, Home Depot common stock was actively traded on the NYSE, with more than 8.7 billion shares traded during the Class Period.

38. Lead Plaintiff will fairly and adequately protect the interests of the Class members and has retained counsel competent and experienced in class action and securities litigation. Lead Plaintiff has no interests antagonistic to or in conflict with the Class.

39. Lead Plaintiff's claims are typical of the claims of the Class members. Lead Plaintiff and all members of the Class purchased Home Depot common stock at artificially inflated prices and have sustained damages arising out of the same wrongful course of conduct.

40. Common questions of law and fact exist as to all members of the Class and predominate over any questions affecting members of the Class. Among the questions of law and fact common to the Class are:

- a. Whether the federal securities laws were violated by the Defendants' acts and omissions as alleged herein;
- b. Whether the Defendants participated in and pursued the common course of conduct and fraudulent scheme complained of herein;
- c. Whether the Defendants had knowledge of (or were reckless with respect to) the improper activities described herein;

- d. Whether the statements disseminated to the investing public, including investors in Home Depot, during the Class Period omitted and/or misrepresented material facts about Home Depot's true financial condition, business operations and future business prospects;
- e. Whether Defendants acted knowingly or recklessly in omitting to state and/or misrepresenting material facts;
- f. Whether the market price of Home Depot's securities during the Class Period was artificially inflated due to the non-disclosures and/or misrepresentations complained of herein; and
- g. Whether Lead Plaintiff and the other members of the Class have sustained damages and, if so, the appropriate measure thereof.

41. A class action is superior to other available methods for the fair and efficient adjudication of this controversy since joinder of all members of the Class is impracticable. Furthermore, as the damages suffered by the individual Class members may be relatively small, the expense and burden of individual litigation make it impossible for Class

members individually to redress for the wrongful conduct alleged herein. There will be no such difficulty in the management of this action as a class action.

42. The names and addresses of the record owners of the shares of Home Depot common stock purchased during the Class Period are available from Home Depot and/or its transfer agent(s). Notice can be provided to persons who purchased or otherwise acquired Home Depot common stock by a combination of published notice and first class mail, using techniques and forms of notice similar to those customarily used in other class actions arising under the federal securities laws.

### **SUBSTANTIVE ALLEGATIONS**

43. During the Class Period, Home Depot was a company driven in large part by a preoccupation with meeting or exceeding the estimates that Wall Street analysts published for its quarterly and year-end growth and earnings. The obsession began well before the Class Period and was exacerbated when Nardelli and Tomé became the Company's CEO and CFO, respectively. Ultimately, it drove the Individual Defendants to commit the misconduct complained of herein because only through the fraudulent RTV chargebacks, as particularized below, were the Individual Defendants

able to satisfy Wall Street expectations and make it appear as if they were successfully managing Home Depot's business and operations.

44. Numerous current and former Home Depot employees have reported that the Company artificially inflated its financial results during the Class Period through the fraudulent conduct alleged herein. The national media has reported the fraud and Home Depot has terminated numerous employees, including high-level employees, because of the fraud. The fraudulent conduct is also the subject of whistleblower actions that former employees filed against Home Depot, and has become the focus of an SEC investigation, as detailed below.

**Return-to-Vendor Chargebacks (“RTVs”)**

45. Prior to and throughout the Class Period, Home Depot entered into “vendor agreements” with product vendors which provided Home Depot with a credit or “chargeback” from the vendor when the vendor supplied Home Depot with defective merchandise, commonly referred to as a RTV chargeback in retail industry parlance. Home Depot employed RTV clerks whose sole function was to process RTV chargebacks.

46. Upon information and belief, the vendor agreements also included terms that permitted Home Depot, in certain circumstances, to

process a RTV chargeback for defective merchandise and then dispose of the merchandise (rather than return it to the vendor), commonly referred to as “destroy-in-field.” The circumstance that allowed Home Depot to process a RTV chargeback and then dispose of the supposedly defective merchandise generally depended on the value of the defective merchandise. As discussed in more detail below, current and former Home Depot employees described an “allowance” or “ceiling” under which Home Depot could process the RTV and dispose of predetermined amounts of the supposedly defective merchandise without the vendor’s inspection of the goods.

47. Allegations in the preceding paragraph are based upon information and belief, including, *inter alia*, (i) Home Depot’s “Supplier Buying Agreement” (Version 7.03); (ii) Home Depot’s “Supplier Reference Manual” (Version 3.0); (iii) a Home Depot letter to its suppliers dated April 23, 2004 and signed by John Costello, Executive Vice President Merchandising & Marketing, and John P. Campi (“Campi”), Vice President Global Sourcing & Supply Chain; (iv) a July 1, 2004 memo signed by Campi entitled “RTV Process Changes”; (v) a Home Depot 2004 list of “Frequently Asked Questions (FAQ) RTV Policy Agreement for Merchandise Suppliers”; (vi) a Home Depot summer 2003 publication

entitled “BEAR Requirements” (BEAR is an acronym for Back End Automation Re-engineering); (vii) an April 19, 2002 memo that Mercer prepared and circulated to Home Depot store managers related to increasing RTVs; (viii) media reports that detailed statements by current and former employees depicting the fraudulent RTV practices to artificially inflate the Company’s financial results; (ix) whistleblower complaints that Home Depot employees filed against the Company in connection with illicit RTV practices alleged herein; and (x) numerous interviews Class Counsel conducted with former Home Depot employees.

48. The accounting treatment for a legitimate RTV is straightforward. When an RTV chargeback is processed, the Company makes an adjustment to “cost of goods sold” in an amount that offsets or negates the original cost. Legitimate RTV chargebacks have no impact on a company’s financial results. At a minimum, an illegitimate RTV chargeback artificially inflates a company’s earnings and profit margins.

### **Shrink & Loss Prevention**

49. “Shrink” or “shrinkage” is industry jargon for merchandise that is missing because of shoplifting, employee theft, or merchandise that the store used or damaged. Shrink is a significant concern to virtually all

retailers because it has an immediate and adverse impact on operating income and profit margin.

50. According to a Home Depot career bulletin, the Company combats shrink by deploying “Loss Prevention Teams” that “develop and execute programs, processes and systems that proactively address all the issues of shrink impacting stores by focusing on theft and fraud, [and] operational accountability ....”

51. During the Class Period, Home Depot routinely performed inventory audits to determine whether the quantity of physical inventory on store shelves matched the booked inventory identified on the Company’s computers. Computerized booked inventory that exceeds physical inventory is “shrink.”

52. The proper accounting treatment for shrink is to write-down the missing product to zero, which cuts directly into a company’s earnings and operating margin because the company must bear the cost of the loss. In short, shrink reduces a company’s overall financial performance and thus a retail business has an incentive to reduce shrink.

**Fraudulent Use of RTVs to Reduce Shrink**

53. Before and during the Class Period, Defendants artificially inflated the Company's financial results by engaging in a companywide scheme to process fraudulent RTVs for merchandise that was not defective and not returned. After processing the fraudulent RTV, the store sold the non-defective merchandise to a customer at 100% pure profit (because the fraudulent RTV offset the cost of the merchandise), or the RTV would improperly cover-up shrink that would otherwise have to be written-down (adversely affecting earnings and operating margins).

**Former Employees Describe the Fraud**

54. According to a person that Home Depot employed from 1997 through 2003, who worked as the Company's Director of the Northwest Division and whose job responsibilities included oversight of 300 stores in 12 states and supervision of at least 26 district managers ("CW1"), the fraudulent misconduct alleged herein was "common place" at Home Depot throughout the course of his/her employment.

55. CW1 explained that vendors typically gave Home Depot a RTV chargeback for defective merchandise, such as broken light bulbs, and that some vendor agreements provided Home Depot with the right to process

the RTV chargeback (up to a certain value) and dispose of the defective merchandise “in field” as opposed to returning it to the vendor. CW1 said the Company abused the allowance and “cooked the books” by causing stores to process phony RTV chargebacks that artificially inflated the Company’s financial results.

56. CW1 said that, for example, a store would have 100 plumbing elbows in stock that were worth \$1 each and a vendor agreement that provided (i) a 5% allowance for damaged plumbing elbows, and (ii) a “destroy-in-field” provision that allowed Home Depot to discard the defective product without the vendor’s inspection. The RTV clerk would submit a phony RTV for a \$5 chargeback for five supposedly defective plumbing elbows, even though there were no defective plumbing elbows and thus the chargeback was not a legitimate claim. The five units would remain on the shelves but would be subtracted from the booked inventory when the RTV was processed, thereby creating a disparity between the physical inventory and the booked inventory. Home Depot would subsequently sell the entire 100 units for \$100, and receive the fraudulent \$5 credit from the vendor, thereby artificially inflating the Company’s financial results.

57. CW1 also described how, in addition to submitting phony RTVs for products that were not defective, there were other instances when a product was defective and an RTV chargeback was legitimate, but in addition to processing the chargeback and discarding the merchandise, the Company would also write-off the merchandise on its profit and loss statement in an improper accounting machination that CW1 described as a “double kiss.” In this illicit scheme, Home Depot would process a legitimate RTV chargeback that would be accounted for as an adjustment to cost of goods sold, discard the goods, but then record a separate improper write-off for the same amount.

58. This “double kiss” scheme allowed the Company to hide shrink when inventory was eventually counted because the product would have already been removed from inventory twice prior to an inventory count; first by virtue of the RTV chargeback and second by virtue of the write-down, hence the term “double kiss.”

59. The RTV fraud that artificially inflated Home Depot’s financial results extended far beyond the boundaries of Home Depot’s Northwest Division.

60. Class Counsel interviewed a former Home Depot employee (“CW2”) who worked from August 1999 through May 2001 as a RTV clerk at Home Depot stores in Flushing, East Meadow, Farmingdale and Copiague, all of which are located in New York. CW2 worked most frequently at the Flushing and East Meadow stores and was directly responsible for processing RTV chargebacks.

61. According to CW2, before and during that portion of the Class Period when he/she was employed at Home Depot, RTVs were “constantly inflated” in all of the stores where he/she worked. CW2 reported that the illicit practice occurred most frequently during or in conjunction with the inventory process (physical inventory counts). When inventory discrepancies occurred, the missing product was “supposed to get marked down to zero and taken out of the system” but instead department managers would bring a list of SKU’s (product barcode numbers) to the RTV clerk to process as fraudulent RTVs.

62. For example, CW2 said if 1,000 light bulbs were supposed to be on the shelf (according to the booked inventory system), and there were only 700 light bulbs, the department manager would tell the RTV clerk to enter 300 light bulbs into the system for credit in the form of an illicit

RTV chargeback. This occurred when the product was stolen, destroyed or misplaced, and thus an RTV chargeback would be improper. CW2 explained that by engaging in this fraudulent practice, the Company would not “take a hit in the markdowns” and instead would get a credit from the vendor in the form of a RTV chargeback. CW2 noted that some vendors had allotted an amount (in dollars) of chargebacks that would be accepted, sight unseen, and that the RTV clerks were ordered to maximize the chargebacks regardless of whether they were legitimate or not.

63. CW2 said that in light of the nature and prevalence of the misconduct, Company management must have known that the practice was occurring. He/she estimated that in the stores where he/she worked, 30 to 40 percent of all RTV chargebacks were fraudulent. CW2 estimated that the RTV chargebacks at the Flushing store averaged \$200,000 per month and at the East Meadow store averaged \$50,000 per month. Accordingly, the illicit chargebacks at just these two stores would average nearly \$1 million annually in pure profit.

64. According to another former employee (“CW3”) who worked as a receiving associate and later as a RTV clerk at a Colorado Home Depot store from May 2002 through June 2004, the illicit scheme of

processing phony RTV chargebacks occurred throughout his/her employment.

65. CW3 indicated that the electrical and plumbing departments were the worst offenders of the RTV chargeback system because the plumbing and electrical goods manufacturers/vendors typically did not inspect defective or damaged merchandise. CW3 recalled instances when department managers would hand him/her empty boxes that had contained goods that were presumably stolen from or used by the store and instructed him/her to enter them into the RTV system. CW3 explained that the practice was improper because the product was not defective or damaged and the Company should have included the loss as “shrink” rather than entering a RTV chargeback to a vendor.

66. CW3 said this improper practice was one of his/her problems with the position, and that he/she had an “ethical problem” with processing improper RTV chargebacks.

67. In addition to spanning the country, the fraudulent conduct predated the Class Period. According to a former employee (“CW4”) who worked as a RTV clerk at Home Depot stores in three different locations (Berlin, Enfield, and North Haven, Connecticut) from 1993 to 1996, and

whose job responsibilities included processing RTV chargebacks, management had instituted a quota which mandated that RTV clerks charge a certain dollar value of RTVs. CW4 said that to fulfill the quota Home Depot stores processed fraudulent RTVs throughout the period of his employment.

68. CW4 explained that if, for example, customers returned ten garden hoses that were defective, the vendor agreement with the garden hose supplier may provide that the garden hoses be “destroyed-in-field.” In such cases, the store would enter a RTV chargeback and discard the damaged garden hoses. CW4 said that many vendors had allotted a dollar amount per month to Home Depot to cover these returns. The RTV clerk would show the returned products to his supervisor and the receiving manager and then the product was “thrown away.” The RTV chargeback would be entered and credited to Home Depot through the vendor account.

69. According to CW4, in order to fulfill RTV chargeback quotas, RTV clerks would falsify the number of, in his/her example, garden hoses, and instead of the 10 returned garden hoses, the RTV clerk would process RTV chargebacks for 50 garden hoses and indicate that 50 garden hoses were “thrown away.” The store would sell the 40 non-defective

garden hoses as 100% pure profit or use them to offset shrink that otherwise would have had a negative impact on operating income and profit margins.

70. CW4 commented that in the case of an expensive item, such as a toilet, the vendor would likely inspect the damaged product and give approval before it could be discarded. However, he/she said that small, relatively inexpensive items, such as garden hoses, were not worth the vendor's time or money to send a representative to inspect the product and thus these products were subject to the fraudulent RTV practices.

71. According to another former Company employee ("CW5") who worked at Home Depot for 17 and a half years between 1986 and 2002 in seven different stores in California, as a department manager, a special order/installed sales expeditor auditor, operations manager, and eventually a store manager, RTVs were fraudulently processed to artificially inflate the Company's financial results.

72. CW5 said that RTV chargeback agreements differed with each vendor, but he/she recalled vendor agreements that had a \$25 per item and under "destroy-in-field" provision, meaning that an RTV chargeback could be processed up to the \$25 allowance for each item without returning the defective product to the vendor. In these cases, the RTV clerk would

destroy or throw away the product and process the related vendor chargeback.

73. According to CW5, it was Home Depot policy that store managers were allowed only so much shrink per inventory and that “after two bad inventories, they’re terminated.” CW5 explained that physical inventory had to match booked inventory with no more than a 1.5 percent shrink and that “any loss more than 1.5 percent would mean termination of the store manger and most likely termination of his/her team of managers.” CW5 explained that the stores recaptured shrink by processing fraudulent RTV chargebacks.

74. CW5 explained that the stores where he/she worked would distribute a list that identified what defective merchandise vendors would and would not take back, what the limit was, and what was “inspectable” by the vendor. CW5 said the Company’s goal was to reach (but not exceed) the limit of the vendors’ allotted RTVs, and that to reach this quota the Company stuffed the RTVs with merchandise that was not defective but instead was missing as a result of shrink.

75. Another former Home Depot employee (“CW6”) who worked as an assistant RTV clerk at Home Depot’s Taunton, Massachusetts

store from November 2003 through August 2005 recounted similar fraudulent misconduct.

76. CW6 reported that he quit the Company, in part, because of his concern over abusive RTV chargebacks. He/she also said that the main RTV clerk at the Taunton Home Depot store also quit the Company because he/she was uncomfortable with the improper RTV practices.

77. CW6 explained that he/she questioned the legitimacy of many RTV chargebacks that department managers asked him/her to process into the RTV system for store credit. CW6 believed that some of the items on the list were lost, stolen, or otherwise missing and did not qualify for vendor credit, and that the items should have been marked down as opposed to being processed as a RTV chargeback.

78. CW6 explained, by way of example, that he/she would question when 20 mosquito magnets would be processed as RTV chargebacks when they had not been returned as defective merchandise. CW6 said there were also instances when customers would return merchandise that was not defective, but the manager would nevertheless tell the RTV clerk to process a RTV chargeback to the vendor. According to CW6, this was improper and there should have been no chargeback. The

proper procedure would have been to enter the RTV chargeback only if there was a manufacturer defect, but, in this instance, the Company processed the RTV chargeback and the merchandise would be placed back onto the store shelves and sold as pure profit.

79. CW6 estimated that the Taunton Home Depot store had hundreds of thousands of dollars in chargebacks per month, that 10 to 20 percent of the chargebacks were “questionable,” and that this was common practice throughout his employment with the Company.

**The April 19, 2002 Mercer Memo**

80. On August 4, 2005, *The New York Post* published an article titled “Unhappy Returns – Home Depot Store Pushed Phony Claims: Ex-Staffer.” The article reported that *The New York Post* had obtained a copy of an April 19, 2002 internal Home Depot memo that Defendant Larry Mercer had circulated to the Company’s store managers.

81. According to *The New York Post*, the Mercer Memo discussed “missed RTV dollars” and pinpointed specific categories, such as the electrical and flooring departments, that had the greatest opportunity to “*boost chargebacks.*” (Emphasis added.) The Mercer Memo estimated that,

*on a companywide scale*, Home Depot could boost RTV chargebacks by more than \$59 million in credits.

82. CW5 told Class Counsel that he/she had a vivid recollection of the Mercer Memo, and that following its distribution every department manager spent an hour each week assisting the RTV clerk with processing RTV chargebacks. According to CW5, the store manager of the Signal Hills, California store told the assistant and department managers that “here’s a great opportunity to capture the loss,” which CW5 understood meant to increase RTV chargebacks, regardless of whether they were legitimate or not, in order to reduce shrink.

83. CW5 indicated that immediately following the Mercer Memo and continuing for the following five months that he/she worked for Home Depot, RTV chargebacks increased by approximately 25%.

#### **Budgeting for the Fraud**

84. According to CW1, in or around 2001, the Company published a Strategic Operating Plan (the “Plan”) that provided, *inter alia*, various initiatives and “Financial Performance Goals.” CW1 indicated that the “Loss Prevention” section of the Plan forecast that shrink within the

Northwest Division should be reduced from 2.04% in 2001 to 1.29% by 2004.

85. CW1 explained that to achieve the reduction, the Plan set forth a “Shrink Benefit Summary” that identified separate initiatives to reduce shrink. The initiatives included increased physical security, a loss prevention analyst and closed circuit-digital recording, but also contained a “Refunds>Returns/RTVs” line item that forecast a Refund>Returns/RTV benefit of \$4.32 million in 2002, \$12.16 million in 2003, and \$15.3 million by 2004. In effect, the Plan contemplated using RTV chargebacks to reduce shrink.

86. CW1 noted that the Plan also set forth “Financial Performance Goals” for the Northwest Division that included actual, estimated and targeted financial goals. According to CW1, this section of the Plan identified various components that comprised gross margins, which included “Vendor Income (Rebates).” CW1 noted that the planned “Vendor Income (Rebates)” accounted for 4.5% of gross margins in 2001, and were targeted to increase to 4.7% in 2002, 4.9% in 2003, and 5.2% by 2004.

87. According to CW1, the “Vendor Income (Rebates)” was initially “referred to as vendor income, [but] it was then changed and a word

was added to not draw any attention to it, the change was called Vendor Income (Rebates).” CW1 noted “we don’t do a lot of rebates at Home Depot, so it’s easy to see what they were doing,” the implication being that the Company accounted for the illicit RTVs as “Vendor Income (Rebates)” so that the actual artificially inflated earnings and operating margins would correspond with budgeted amounts.

### **An Internal Change**

88. In a decision to change course concerning the rampant fraudulent misconduct that pervaded Home Depot, the Company issued an internal memorandum on February 12, 2004 (the “February 12, 2004 Memo”) that addressed the fraud. According to an article that appeared in *The New York Post* on August 11, 2005, titled “Home Cooked Books – Depot Scam Widens,”

A senior Home Depot official had acknowledged that management has been aware of the problem for at least 19 months, when a memo dated February 12, 2004, was circulated by the corporate office that outlined procedures for collecting chargebacks from suppliers.

89. According to the article, the Company published the February 12, 2004 Memo to “*quell the concerns of several employees who*

*had complained that superiors were pressuring them to participate in the scheme. . . .”* (Emphasis added.)

### **The Implementation of BEAR**

90. As early as the summer of 2003, Home Depot began laying some of the groundwork that would later be used to overhaul the RTV system and eliminate the RTV chargeback fraud.

91. In the summer of 2003, the Company issued a “Partner Communication eNewsletter” (the “Newsletter”) signed by Jerry Edwards, Executive Vice President of Merchandising, and Wayne Gibson, Senior Vice President of Global Logistics. The Newsletter revealed a new initiative, identified as “Back-End Automation & Re-Engineering” or “BEAR” to overhaul the RTV system. According to the Newsletter, the Company was “finalizing business requirements and selecting a software vendor to enable our new Data Collection process for RTV policies.” The Newsletter asked vendors to supply information to Home Depot that would assist in the developing the BEAR software.

92. On July 1, 2004, Home Depot issued another memo (the July 1, 2004 Memo”) to its vendors entitled “RTV Process Changes” that was signed by John Campi, the Company’s Vice President Global Sourcing

& Supply Chain. The July 1, 2004 Memo stated, “The Home Depot has identified the Return-to-Vendor (RTV) process *as a critical focus area for 2004 and 2005.*” (Emphasis added.)

93. According to the July 1, 2004 Memo, “Planned changes to the RTV process include *more comprehensive policies*” and “*consistent, accurate RTV policy execution* in stores (*less disputes to process*).” (Emphasis added.) It also announced that “*the Home Depot RTV Associate and Supplier Representative [will] no longer [be] able to override negotiated policies.*” (Emphasis added.)

94. On November 11, 2004, the Company issued yet another memo (the “November 11, 2004 Memo”) to its vendors titled “BEAR RTV Pilot,” which summarized “the current status of the project as well as the RTV Pilot to begin on October 27, 2004.”

95. The November 11, 2004 Memo stated, “The enhanced integral reporting and metrics will help Home Depot to *reinforce desired behaviors* and allow performance tracking to drive future improvements.” (Emphasis added). The November 11, 2004 Memo reiterated that the BEAR system would provide “more consistent and accurate RTV execution in stores” and that there would be “*no store override of negotiated RTV*”

*policies.*” (Emphasis added.) Additionally, it stated that the BEAR system would “reduce[] time spent investigating/validating chargebacks and processing disputes,” and would provide “improved metrics and reporting to be generated upon rollout” that would “track supplier product performance (*i.e. true defective rate*).” (Emphasis added.)

### **Terminating the Fraud**

96. In the summer of 2003, the Company resolved that it was time to begin the process of curtailing the pervasive RTV fraudulent misconduct by overhauling the RTV system. However, the Defendants did not stop the misconduct, but instead deliberately turned a blind eye until October 2004 when the overhauled RTV system was rolled-out.

97. The cessation of the misconduct had an immediate and material effect on the Company’s financial results. In the fourth quarter of 2004, the Company’s revenue and earnings failed to exceed analysts’ expectations with regard to diluted earnings per share during the fourth quarter of 2004 (as it had done in its previous nine quarters), and its revenue and earnings growth fell short of historical levels.

98. On February 22, 2005, the Company reported a quarterly net profit of \$1.04 billion, meeting (but not exceeding) analysts' projections of

47 cents per share (the first time in nine quarters that the Company had failed to exceed analysts' estimates). The Company also announced that revenue and EBIT growth in the fourth quarter of fiscal 2004 fell short of historical levels (at 11.2% and 10.5% respectively – compared to fourth quarter fiscal 2003 growth of 14.5% and 37.8%, respectively).

99. Following Home Depot's issuance of the February 22, 2005 press release announcing the disappointing fourth quarter results, the Company's share price declined precipitously. At the close of trading on February 18, 2005 (the last trading day prior to the issuance of this press release), the price of Home Depot's shares was \$42.02 per share. On February 22, 2005, the price of Home Depot shares closed at \$40.28. By the close of trading on February 23, 2005, Home Depot's per share price had fallen to \$39.75, an over 5% drop from February 18, 2005. By the close of trading on April 28, 2005, Home Depot's shares had plummeted to \$35.09 per share, representing a decline of over 16% since February 18, 2005 and a market capitalization loss of \$16.5 billion.

### **POST CLASS PERIOD DEVELOPMENTS**

100. In addition to the allegations set forth above particularizing the fraudulent misconduct that pervaded the Company during the Class

Period, developments that occurred after the Class Period provide further evidence of the misconduct.

### **Whistleblower Actions**

101. On June 23, 2005, Michael Davis (“Davis”), a former Home Depot store employee, filed a complaint with the U.S. Department of Labor under the employee protection provisions of Title VIII of the Sarbanes-Oxley Act of 2002, Section 806 of the Corporate and Criminal Fraud Accountability Act of 2002, 18 U.S.C. § 1514A, et seq. (the “Whistleblower Complaint”).

102. According to the Whistleblower Complaint, a copy of which Class Counsel obtained, Davis began his employment with Home Depot on October 6, 1997. He worked in the Aspen Hill, Maryland store as a Loss Prevention Officer, and then became a RTV clerk on or about May 11, 2000. On December 7, 2004, Home Depot promoted him to Cross-Merchandiser until Home Depot terminated his employment on March 31, 2005.

103. The Whistleblower Complaint alleged that in late summer or early fall of 2000, Home Depot undertook a new process whereby RTV clerks were given Vendor Control Sheets made up by the store management and instructed to input various product codes (“SKU numbers”) for

quantities of merchandise that were never defective, damaged, or returned to the store. In the Whistleblower Complaint, Davis alleged that

*I was instructed to process false claims, making up quantities and inputting them into the system that were supposed to total a dollar amount just below the amount allowed by the vendor.* Claims in excess of the dollar amount would result in the vendor requesting that the store hold the so-called defective goods for inspection.

For example, say that Phillips Lighting Company allows \$1,000 per month as an allowance for damaged goods. The Aspen Hill store may have had only \$50 worth of defective goods, but management instructed RTV personnel to charge just below Phillips' \$1,000 ceiling.

\* \* \*

*As required by management,* RTV clerks were to input products that were not returned or damaged in any way, so as to generate more dollars for the store.

Shortly after I took over the RTV position, Assistant Managers Steve Diddle and Ted Neal explained this new process to me, which involved falsifying data....

*On a periodic basis, Company management would circulate memos telling personnel to use RTVs instead of markdowns.* These memos included lists of vendors, vendor numbers, disposition codes, and the amount that could be claimed without involvement of the representatives. *These memos came from* another

store, *the Atlanta home office*, and the Paramus, New Jersey office in some cases setting dollar value store goals, dollar value regional goals and a companywide goal of \$59 million.

\* \* \*

*Lists would be repeatedly updated and store management would press me to comply ... loss prevention managers and division loss prevention managers have laptops with RTV numbers and vendor lists. They compare stores and regions, telling managers to get in line.*

\* \* \*

The pressure increased in approximately January, 2004. Store Manager Bob Hommerfbocker began pressing Donnie Moyer and me as he was upset that RTV's generated on a weekly basis averaged between \$25,000 to \$30,000, when other stores were doing more ... *I was given a package from [District Loss Prevention Manager] Alan Wells explaining, on a company-wide basis, that RTV clerks could generate dollars for the store, the region, and companywide.* Month after month, I was pressed to get credits up from \$40,000 to \$50,000 per week so that inventory shrink could be cured and so that store managers could get bonuses.

\* \* \*

Late in 2004, after the store had a bad inventory, I was told by Assistant Manager Charles Wilson that store management was mad at me over my refusal to help process fraudulent RTV's...

(Emphasis added.)

104. According to an article that appeared in *The New York Post* on August 2, 2006 titled “He’s out at Home – Ex-Employee: Retail Giant is a Vendor Offender,” another Home Depot employee filed an action against Home Depot alleging illicit RTV practices.

105. The employee, Roger Fredrickson, who is 65 years of age, alleged that the Company retaliated against him for refusing to process fraudulent RTVs. In his complaint, Fredrickson asserted that he was retaliated against by store management who assigned him tasks that were too physically demanding for his age, including hauling shipping crates in 100-degree heat and unloading trucks without the assistance of a forklift.

#### **More Home Depot Employees Come Forward**

106. On August 11, 2005, *The New York Post* published an article titled “Home Cooked Books – Depot Scam Widens,” and reported that the fraudulent RTV practices (a) “went beyond a single [Home Depot] store” and (b) were “common practice at other locations” throughout the Company. According to the article, four current and former Company employees who “*worked in different areas of the company, spanning four states, including the [Home Depot] corporate headquarters in Atlanta,*” detailed a plan, which one referred to as “*washing the numbers,*” that “allowed stores to

*artificially boost profits.*” (Emphasis added.) According to the article, four current or former Home Depot employees said, “Store clerks . . . were pressured to overcharge suppliers for faulty goods, sometimes by inputting false product codes into the computer system, or incorrectly classifying the merchandise in other ways.” The article reported that the persons who were interviewed explained, “As a result, stores were able to collect money from suppliers that could be used to offset inventory shortfalls from theft or other mistakes and *boost profits.*” (Emphasis added.) Among other things, the article described the following:

One employee, “who said he had first-hand financial knowledge of a dozen stores,” noted that inflated vendor chargebacks could “account for less than 1 percent of a store's annual sales.” However, in view of the “thin margins in retailing,” that amount “is often enough to mean the difference between a store making or missing its numbers.”

This same person indicated that “the practice of inflating vendor chargebacks intensified after a change to employee compensation in 2001 that increased the amount of stock employees received as part of their bonus” (this provided employees with “an incentive to boost the stock price”). This person indicated that “[o]ne way” to enhance the price of the Company’s stock was “to use the extra money collected from suppliers to inflate store profits.”

Another individual, a former employee, “suggested” that the improper practices have been going on for “more than a decade.” Jonathan Faitsch asserted that he was instructed to manipulate “the amount of money collected from vendors at two Connecticut stores, where he worked from 1993 to 1995.”

107. On January 20, 2006, *The New York Post* published another article titled “Surplus Scam Seen – Home Depot Overcharge Charged.” The article noted that

A Home Depot store in Maryland wound up with \$1 million in excess inventory as a result of overcharging suppliers to cover the cost of damaged or defective merchandise, according to a former employee.

The former employee, Donald Moyer, discussed the surplus inventory during a deposition last week taken by Mark Schwartz, a Bryn Mawr, Pa., lawyer for another former Home Depot staffer, Michael Davis, who said he blew the whistle on the practice of inflating supplier payments, known as return-to-vendor credits.

\* \* \*

The excess inventory, which, according to Moyer, was discovered during a 2004 audit, shows how inflated return-to-vendor credits can lead to discrepancies between what is actually taking place at a store and what is recorded in financial records.

Though Moyer's comments related solely to a store in College Park, Md., other current and former employees have described similar situations at other Home Depot stores in different regions of the country.

\* \* \*

Every six months to a year, auditors physically count the inventory at a given store and compare their results to the amount on Home Depot's books, Moyer said.

Last year, auditors counting inventory at the Home Depot store in College Park, wound up with a startling result. The inventory at the store exceeded the amount recorded on Home Depot's books by \$1 million.

Usually, the reverse is true, accounting experts said.

“The book value tends to exceed a store's actual inventory due to theft and breakage,” said Edward Ketz, associate professor of accounting at Penn State University.

Moyer, who at the time was an operations manager at a neighboring store in Aspen Hill, Md., said that Home Depot's corporate office sent a team to investigate.

“They determined that the extra inventory was the result of inflated RTV dollars,” Moyer said.

Moyer described how the practice might work: An employee could charge a vendor for a light bulb

that is neither damaged nor defective, but in good condition.

On the books, that light bulb is recorded as having been returned to the vendor, lowering the store's inventory.

In reality, however, the light bulb remains on the store shelves, thereby giving rise to a discrepancy between the "physical" inventory and the "paper" inventory.

In general, such discrepancies can have a real impact on a store's reported profits, said Ketz, the accounting professor. Higher return-to-vendor credits help offset shrinkage, the loss of merchandise to theft or damage. "By lowering shrinkage, you lower cost of goods sold and thereby boost income," Ketz said.

Based on a rough projection of the College Park store's cost of goods sold, Ketz estimated that the \$1 million inventory discrepancy could have resulted in a 4 percent boost to profits.

108. On March 23, 2006, *The New York Post* published another article titled "Home Wrecker – Manager Claims Whistle-Blowing Led to Firing," and reported that another Home Depot employee had detailed the Company's fraudulent RTV practices:

In her 18 months as an operations manager at Home Depot, Ellen Sharp was known as a stickler for the rules, so much so that she said her superiors had taken to derisively calling her "Ms. Home Depot."

Sharp, 56, said that she suspects her desire to play by the rules resulted in her termination two weeks ago, after she wrote a letter to management voicing concerns over the way the company collects money from vendors to cover the cost of damaged merchandise.

The practice, known as return-to-vendor credits, has drawn scrutiny from other employees, including Michael Davis, who worked at the same store as Sharp and who is suing the home improvement giant for wrongful termination.

The issue has sparked an internal investigation by Home Depot management and has also caught the eye of the Securities and Exchange Commission, which has opened an informal inquiry into the matter.

\* \* \*

During weekly conference calls, Alan Wells, the district loss prevention manager suggested that return-to-vendor credits should equal about 3 percent of a store's weekly sales, according to Sharp, who participated in the conference calls.

\* \* \*

At Aspen Hill, however, return-to-vendor credits would normally total about 1 percent to 2 percent of the store's weekly sales, according to Sharp, who had direct oversight of processing these credits.

Sharp said that Robert Hommerbocker, the store manager, would urge her to do a better job of hitting 3 percent.

\* \* \*

Sharp eventually expressed her concerns in a letter to Hommerbocker dated March 1.

“As you know,” Sharp wrote, “I have always been very vocal with regard to the Return to Vendor (RTV) and markdown practices that occur in the Home Depot system.”

In the letter, a copy of which was made available to *The Post*, Sharp referred to a December incident, in which an employee placed RTV tags on \$3,400 worth of plumbing merchandise that he took from the sales floor.

109. On April 14, 2006, *The New York Post* published yet another article titled “Happy Returns – Home Depot’s Vendor \$\$ Jumped Before Audits,” which reported on developments in the Whistleblower Complaint that Davis filed against Home Depot. According to the article, Davis said “during the busy Christmas season, RTVs might rise to \$35,000 a week,” but Davis added, “In the weeks leading up to the stores’ bi-annual inventory audit – in October and February – RTV credits would soar to as much as \$80,000 a week.”

110. Another person who worked for Home Depot as a subcontractor recounted abusive RTV practices similar to the “double kiss” scheme that CW1 had detailed. According to an article in *The New York Post* on February 3, 2006, titled “Revolving Door – Home Depot was Paid 3 Times for Same Product,” Raymond Hammond, a former Home Depot subcontractor said that Home Depot employed practices that allowed it to get paid as many as three times for the same merchandise.

111. In an interview with *The New York Post*, Hammond said the practice applied to *all types of damaged or defective merchandise and happened routinely at the five Home Depot stores he worked* for in upstate New York from 1999 to 2001.

112. According to *The New York Post*, Hammond described a specific case involving a screen door that he was supposed to install at a client’s home. The door arrived at the job site damaged and Hammond returned it to a Home Depot store. The store charged Hammond \$105 to cover the wholesale cost of the door. The Home Depot clerk then filled out [the RTV] paperwork and the Home Depot store collected \$105 from the vendor who supplied the damaged door. Home Depot then placed the damaged door on the sales floor and sold for roughly \$105, a discount to the

retail price of \$160 because of the defects. All told, the Home Depot store collected \$315 for a door that cost it \$105, according to Hammond. *The New York Post* also reported that

Hammond said the practice was common knowledge among the subcontractors who worked for Home Depot in his region.

“On any given day, there might be a dozen contractors lined up outside Home Depot picking up product,” Hammond said. “We'd talk about damaged products and how Home Depot collects triple for the same item.”

113. There is a website on the Internet that is a discussion forum for retail workers. The address of the website is <http://www.retailworker.com/node/25244>. As of the date of the filing of this complaint that site contains a post from “BruisedOrange” dated June 11, 2006. In the post, BruisedOrange quotes from another post and added his/her own editorial comments. The post has the ring of truth and corroborates Lead Plaintiff’s allegations:

Everyone knows that we have been ripping off the vendors forever; American Moulding etc. Especially with the automatic RTV processing for sight unseen RTV vendors. [Loss Prevention Specialists] used to just bring lists to the cage and have the RTV clerk process them. You can "juice" a stores physical inventory 300K in a 6 month period by this practice. Multiply that out per store

per year. The amount of profit in question is staggering. I wonder how much more the stock will drop now. All thanks to Gilligan Nardelli and his criminal gang!

\* \* \*

### **Home Depot Terminates Employees**

114. In late January and early February 2006, two Home Depot executives left the Company. One of those employees, according to a February 3, 2006 article in *The New York Post* titled “Second Regional Exec Exits; Oversaw Inventory,” Chris Spaccaforo, a loss prevention manager for the Northern region, whose duties included, *inter alia*, “overseeing inventory management and shrinkage, the amount of merchandise lost to theft, damages or receiving mistakes.” As noted in this press report, “Shrinkage has been a focus point at Home Depot after a former employee, Michael Davis, accused the retailer of inflating charges to vendors to cover the cost of damaged or defective merchandise.” Mr. Spaccaforo’s departure came just weeks “after the president of the Northern region [Troy Rice] left the company for reasons that remain unclear.” On January 14, 2006, *The New York Post* published an article titled “Top Home Depot Exec Leaves,” and reported that in his position, Mr. Rice oversaw “operations for hundreds of [Home Depot] stores.”

115. On September 7, 2006, *The New York Post*, in an article titled “Home Fires Two: Internal Probe Hits Chargebacks,” reported that Home Depot had fired Lonny Holmes, the Loss Prevention Manager for the Mid-Atlantic Region, and Kevin Long, the Mid-Atlantic Region District Manager, and placed Natasha Williams, manager of the Hyattsville, Maryland store, and Robert Delissio, manager of a store in Washington D.C.’s Brentwood neighborhood, on “administrative leave.” The article also reported that the actions were “part of an ongoing internal investigation into allegations of improper vendor chargebacks....” The article also reported that

Auditors descended on stores in Washington, D.C., Virginia, Maryland, Pennsylvania and New York this summer. Investigators interrogated store employees, sometimes up to five hours at a stretch, and carted away documents, sources said.

\* \* \*

Williams, who has filed a separate discrimination lawsuit against Home Depot, said that about 20 people, mainly from Home Depot’s corporate office in Atlanta, visited the Hyattsville store on July 24 and questioned her for three or four hours about RTV practices.

A focal point was whether employees had been given a weekly percentage target for RTV claims.

116. According to the September 7, 2006 article, Williams told investigators that the target for RTV chargebacks was generally understood to be about 3 percent of sales. Williams reportedly told investigators “every Monday morning we had a conference call with management, and if you were below that percentage, you would be questioned.”

117. What is more, on October 16, 2006, *The New York Post* reported that the number of Home Depot employees terminated because of the probe into improper RTV chargebacks had swelled to ten. In an article titled “Home Purge Hits 5,” *The New York Post* wrote, “a sweeping internal investigation into a chargeback scandal at Home Depot has claimed five more casualties ....” According to the article, “all but one of the employees, who include four store managers and a district manager in Pennsylvania, Maryland, and Washington, D.C. were let go as a result of the on-going probe.” The article reported that a fifth employee was placed on leave, and that “[t]he recent blood-letting doubles to 10 the number of Home Depot employees who have lost their job as a result of the inquiry.” The article also reported, “Though much of the scrutiny has centered on the Mid-Atlantic region, concerns about Home Depot’s RTV practices ... are not limited to those areas.”

118. The October 16, 2006 article reported that a West Coast member of a RTV team, who asked not to be identified to protect his job, had said, “the questionable practices took place in stores in his region as well.” According to the article, one employee commented that a West Coast store “*once charged vendors for 400 percent more glass than the store actually sold to customers.*” (Emphasis added.)

### **SEC Investigation**

119. In January 2006, it was widely reported that the SEC had launched an “informal inquiry” into whether Home Depot used illicit RTV chargebacks from vendors to inflate the Company’s earnings. As set forth in an article appearing in *The New York Post* on January 12, 2006 titled “Screw Probe – SEC Eyes Supplier Payments to Home Depot”:

The Securities and Exchange Commission has opened an informal investigation into allegations of inflated payments that Home Depot collected from suppliers to cover the cost of damaged merchandise....

The payments, known as return-to-vendor charges, helped Home Depot pad store profit, according to current and former employees, who detailed the practice in two [prior] Post articles.

\* \* \*

The practice — one source called it “washing the numbers” — was done at multiple stores in different regions of the country, sources said.

\* \* \*

Suppliers have largely been unwilling to speak out for fear of losing Home Depot's business.

But one vendor — who sells to Home Depot stores throughout the country and who spoke on the condition of anonymity for fear of reprisals — said she suspected the practice was done on a national level, though not at all stores at all times.

120. On January 13, 2006, a reporter for CNBC noted the following with respect to the SEC's investigation of Home Depot's illicit RTV practices:

CNBC has learned that the Securities and Exchange Commission has ramped up its inquiry into allegations that it inflated what's known as “return to vendor” payments in stores throughout the country, a potentially huge blow to the nation's largest home merchandising company as Wall Street top cop examines whether the alleged fraud occurred on a nationwide basis.

Home Depot, with 2,000 stores nationwide, denies that it has done anything improper, but the SEC's investigation is serious. After asking the company to turn over documents in August [2005], the commission's enforcement staff in New York City, just last week asked for additional documents, this time from a former Home Depot employee, Michael Davis, who said he was fired from the

company for blowing the whistle on the practice. CNBC has learned that the probe is wider than originally thought; although Home Depot said it is nothing more than an “informal inquiry,” SEC is examining whether the practice that Davis has described occurs throughout the country.

\* \* \*

CNBC has learned that what has piqued the SEC’s interest is that Davis alleges that the practice just did not occur in the store he worked out of in suburban Washington DC. When he confronted management about what he thought was unethical behavior, he says he was told that this is standard practice throughout the Home Depot system. Davis says that he believes the improper charges amount to about \$25,000 a week out of the store where he worked. *That is about \$1.3 million. Extending that out to all the stores in the Home Depot empire and you are talking more than \$1 billion . . . .*

(Emphasis Added.)

### **FALSE AND MISLEADING STATEMENTS**

121. As detailed herein, during the Class Period, Defendants issued or caused to be issued materially false and misleading statements that deceived the investing public as to the Company’s financial performance and condition.

122. Many of the false and misleading statements set forth below were made in Form 10-Qs and Form 10-Ks that were certified by Defendant

Nardelli and Defendant Tomé in accordance with the Sarbanes-Oxley Act of 2002. By certifying those particular Form 10-Q's and Form 10-K's, Defendants Nardelli and Tomé represented, *inter alia*, that the quality and accuracy of the information contained therein concerning the Company's financial performance and condition was safeguarded by internal financial controls in place at the Company, which were designed to foster the development of reliable financial statements.

**A. Fiscal Year 2001**

**Form 10-Q for First Quarter of Fiscal Year 2001**

123. On or about May 29, 2001, Home Depot filed with the SEC a Form 10-Q for the first quarter of Fiscal Year 2001 (ending April 29, 2001). Defendants Nardelli and Tomé signed Home Depot's Form 10-Q for the first quarter of Fiscal Year 2001.

124. In that public filing, Home Depot reported that net sales for the first quarter of fiscal 2001 increased 9.8% to \$12.2 billion from \$11.1 billion for the first quarter of fiscal 2000. According to the Company, the sales increase was primarily attributable to new stores opened since the end of the first fiscal quarter of 2000 (1,178 stores open at the end of the first quarter of fiscal 2001 compared to 971 at the end of the first quarter of fiscal

2000). The Company further indicated that this increase in sales was partially offset by a 3% decline in comparable store-for-store sales.

125. The Company further stated that net earnings as a percent of sales were 5.2% for the first quarter of fiscal 2001, compared to 5.7% for the first quarter of fiscal 2000 and that this decrease was attributable to higher selling and store operating expenses as a percent of sales, which was partially offset by a higher gross profit rate. In addition, the Company indicated that diluted earnings per share were \$0.27 for both the first quarters of fiscal 2001 and fiscal 2000.

**August 14, 2001 Press Release**

126. On August 14, 2001, the Company issued a press release titled "The Home Depot Reports Record Second Quarter 2001 Earnings of \$924 Million." In relevant part, that press release stated:

The Home Depot (NYSE: HD), the world's largest home improvement retailer, today reported net earnings of \$924 million (\$0.39 per diluted share) for the second quarter of fiscal 2001, compared to net earnings of \$838 million (\$0.36 per diluted share) in the second quarter of fiscal 2000.

Sales for the second quarter of fiscal 2001 totaled \$14.6 billion, an increase of 16% from the second quarter of fiscal 2000. Comparable store sales for the second quarter of fiscal 2001 increased 1% from the same period last year.

127. Reacting to the foregoing announcement, one portfolio manager stated (in an August 15, 2001 press report appearing in the *Atlanta Journal-Constitution*): “Nardelli has done a lot of work on the nuts and bolts of the business . . . I think he’s on the right track.” An analyst from Credit Suisse First Boston was quoted in the *New York Times* as follows:

What you saw today from Home Depot is a company that is focused on fixing its internal act, meaning reducing expenses and bringing inventory down . . . Internal developments at Home Depot give us confidence that they’ll achieve their earnings, which is something that we can’t say about any other retailer.

**Form 10-Q for Second Quarter of Fiscal Year 2001**

128. On or about August 27, 2001, Home Depot filed with the SEC a Form 10-Q for the second quarter of Fiscal Year 2001 (ending July 29, 2001). Defendants Nardelli and Tomé signed Home Depot’s Form 10-Q for the second quarter of Fiscal Year 2001.

129. In that public filing, Home Depot reported that net sales for the second quarter of fiscal 2001 increased 15.5% to \$14.6 billion from \$12.6 billion for the second quarter of fiscal 2000. The Company further stated that for the first six months of fiscal 2001, sales had increased 12.8% to \$26.8 billion from \$23.7 billion for the comparable period in fiscal 2000.

130. Home Depot further indicated that net earnings as a percent of sales were 6.3% and 5.8% for the second quarter and first six months of fiscal 2001, respectively, compared with 6.6% and 6.2% for the second quarter and first six months of fiscal 2000, respectively. The Company also stated that diluted earnings per share were \$0.39 and \$0.66 for the second quarter and first six months of fiscal 2001, respectively, compared to \$0.36 and \$0.62 for the second quarter and first six months of fiscal 2000, respectively.

**November 13, 2001 Press Release**

131. On November 13, 2001, the Company issued a press release titled "The Home Depot Reports Record Third Quarter 2001 Earnings of \$778 Million." In relevant part, that press release stated:

The Home Depot (NYSE: HD), the world's largest home improvement retailer, today reported record net earnings of \$778 million (\$0.33 per diluted share) for the third quarter of fiscal 2001, an increase of 19.7% compared with net earnings of \$650 million (\$0.28 per diluted share) in the third quarter of fiscal 2000.

Sales for the third quarter of fiscal 2001 totaled \$13.3 billion, an increase of 15.1% from the third quarter of fiscal 2000. Comparable store sales for the third quarter of fiscal 2001 were flat with last year.

\* \* \*

The Home Depot indicated it expects to meet the current Wall Street earnings consensus of \$0.28 diluted earnings per share for the fourth quarter of fiscal 2001, resulting in earnings per share for the fiscal year of \$1.27, a 15% increase over fiscal 2000.

**Form 10-Q for Third Quarter of Fiscal Year 2001**

132. On or about November 28, 2001, Home Depot filed with the SEC a Form 10-Q for the third quarter of Fiscal Year 2001 (ending October 28, 2001). Defendants Nardelli and Tomé signed Home Depot's Form 10-Q for the third quarter of Fiscal Year 2001.

133. In that public filing, Home Depot reported that net sales for the third quarter of fiscal 2001 increased 15.1% to \$13.3 billion from \$11.5 billion for the third quarter of fiscal 2000. The Company also stated that for the first nine months of fiscal 2001, net sales increased 13.6% to \$40.1 billion from \$35.3 billion for the comparable period in fiscal 2000. According to the Company, the sales increase for both periods was attributable to new stores (1,295 stores were open at the end of the third quarter of fiscal 2001, compared with 1,064 at the end of the third quarter of fiscal 2000).

134. The Company stated that its net earnings as a percent of sales were 5.9% and 5.8% for the third quarter and first nine months of fiscal 2001, respectively, compared with 5.6% and 6.0% for the third quarter and first nine months of fiscal 2000, respectively. The Company further indicated that diluted earnings per share were \$0.33 and \$0.99 for the third quarter and first nine months of fiscal 2001, respectively, compared to \$0.28 and \$0.90 for the third quarter and first nine months of fiscal 2000, respectively.

**February 26, 2002 Press Release**

135. On February 26, 2002, the Company issued a press release titled "The Home Depot Record Earnings For 2001 Exceed \$3 Billion; Fourth Quarter Earnings Growth of 53%." In that press release, the Company reported "record net earnings" of \$3.0 billion (\$1.29 per diluted share) for fiscal 2001, an increase of 18% compared with net earnings of \$2.6 billion (\$1.10 per diluted share) in fiscal 2000. In addition, the Company indicated that sales for fiscal 2001 increased 17% to \$53.6 billion. The Company further reported that for the fourth quarter of 2001, net earnings increased "a record 53%" to \$710 million (\$0.30 per diluted share) from \$465 million (\$0.20 per diluted share) in the fourth quarter of 2000 and

that sales for the fourth quarter of fiscal 2001 totaled \$13.5 billion, an increase of 29% from the fourth quarter of fiscal 2000.

136. At that same time, Home Depot indicated that it expected to meet the current Wall Street earnings consensus of \$0.32 diluted earnings per share for the first quarter of fiscal 2002, an increase of 18%.

137. During a February 26, 2002 interview on the Fox News Channel with Neil Cavuto, Defendant Nardelli was upbeat regarding the recently announced financial results (and was optimistic regarding the Company's future):

CAVUTO: Bob, there are always those in the financial community who say lows [sic] is a better financial bet for you, that the multiple is not quite as high as yours, that it is an easier stock to get, that sort of thing, and that if you are going to make a building play or a homebuilding play, or just, you know, sort of like a typical consumer play, that is the vehicle you chase. What do you say?

NARDELLI: Well, here is what I say, Neil, is again, fourth-quarter earnings up 53 percent . . . If you look at the entire year, [Home Depot] reported \$3 billion in earnings. That was a record. If you look at our overall sales of \$53.6 billion, that is a record.

Take a look at our balance sheet, Neil. We finished the year with \$2.5 billion in cash, and I think that certainly speaks well for the economic conditions that we are in, with \$18 billion of assets. Our debt

to equity is under six, seven percent. We are a very strong company. We are well positioned to deliver into the future.

**Form 10-K for Fiscal Year 2001**

138. On or about April 19, 2002, Home Depot filed with the SEC a Form 10-K for Fiscal Year 2001 (ending February 3, 2002). Defendants Nardelli and Tomé signed Home Depot's Form 10-K for Fiscal Year 2001. In addition, Defendant Nardelli signed this Form 10-K on behalf of Defendant Langone, Defendant Cox and Defendant Clendenin "pursuant to powers of attorney, executed on behalf of each such [defendant]."

139. In that public filing, Home Depot reported that net sales for fiscal 2001 increased 17.1% to \$53.6 billion from \$45.7 billion in fiscal 2000 and that this increase was attributable to, among other things, the 204 new stores opened during fiscal 2001 and full year sales from the 204 new stores opened during fiscal 2000.

140. At this same time, the Company stated that its net earnings as a percent of sales were 5.7% for fiscal 2001 compared to 5.6% for fiscal 2000, reflecting an increased gross profit rate, which was partially offset by higher store operating expenses. According to the Company, diluted

earnings per share were \$1.29 for fiscal 2001 compared to \$1.10 for fiscal 2000.

141. The Company also reported, “In addition, we reduce our ending inventory value for estimated losses related to shrink. This estimate is determined based upon analysis of historical shrink losses and recent shrink trends.”

142. Defendants’ statements concerning Home Depot’s financial performance and condition relating to fiscal year 2001 as set forth above were each false and misleading when made because they misrepresented or omitted the following material adverse facts that the Defendants knew at the time the statements were made:

- a. That during fiscal year 2001, Home Depot was engaged in a scheme to inflate the Company’s earnings through fraudulent RTV practices;
- b. That during fiscal year 2001, Home Depot derived a material portion of its revenues and profits from fraudulent RTV practices;

- c. That the Company had failing and deficient internal controls and procedures and lacked any meaningful ability to accurately report its financial results;
- d. That the Company's improper RTV practices were in direct violation of its own code of conduct; and
- e. That the Company's illicit scheme *vis-à-vis* fraudulent RTV practices potentially subjected Home Depot to substantial regulatory fines, penalties and other legal action, thereby compromising the Company's overall financial condition and prospects.

**B. Fiscal Year 2002**

**May 21, 2002 Press Release**

143. On May 21, 2002, the Company issued a press release titled "The Home Depot Reports 35% First Quarter Earnings Growth to Record \$856 Million." In relevant part, that press release stated:

The Home Depot, the world's largest home improvement retailer, today reported record net earnings of \$856 million (\$0.36 per diluted share) for the first quarter of fiscal 2002, an increase of 35% compared with net earnings of \$632 million (\$0.27 per diluted share) in fiscal 2001 and \$.03 ahead of consensus. Sales for the quarter

increased 17% to \$14.3 billion and comparable store sales increased 5%.

“The Home Depot reported solid sales and earnings gains for the quarter, as our dedicated associates delivered great customer service and drove productivity improvements,” said Bob Nardelli, Chairman, President & CEO of The Home Depot.

\* \* \*

“The increasing strength of our balance sheet and improving fundamentals in sales and margins are allowing us to stay on strategy this year as we did last year and invest for the future as we continue to seek out new sources of growth and opportunity. During the quarter, we opened our first smaller, urban store in Brooklyn to a very strong customer response,” said Nardelli...

\* \* \*

The Home Depot indicated it expects to meet the current Wall Street earnings consensus of \$0.47 diluted earnings per share for the second quarter of fiscal 2002, an increase of 21%.

144. In a CBS Marketwatch report addressing these financial results, Defendant Tomé was quoted as having stated that “[t]he financial strength of Home Depot remains unsurpassed.” In that same report, Defendant Nardelli was quoted as having asserted that “[i]t's a very strong report and a tough act to follow.”

145. Following this earnings announcement, Merrill Lynch analyst Peter Caruso reiterated a “strong buy” recommendation on the Company’s stock, citing better quality results from sales and improving operating logistics. In this regard, Mr. Caruso said: “Home Depot is still showing comp store sales gains consistent with what it achieved in the early 1990's when it faced far less competition from Lowe's with a less mature store base.”

**Form 10-Q for First Quarter of Fiscal Year 2002**

146. On or about June 4, 2002, Home Depot filed with the SEC a Form 10-Q for the first quarter of Fiscal Year 2002 (ending May 5, 2002). Defendants Nardelli and Tomé signed Home Depot’s Form 10-Q for the first quarter of Fiscal Year 2002.

147. In that public filing, Home Depot reported that net sales for the first quarter of fiscal 2002 increased 17.1% to \$14.3 billion from \$12.2 billion for the first quarter of fiscal 2001. According to the Company, the sales increase was primarily attributable to new stores opened since the end of the first fiscal quarter of 2001 (1,386 stores open at the end of the first quarter of fiscal 2002, compared to 1,178 at the end of the first quarter of fiscal 2001) and a comparable store-for-store sales increase of 5%.

148. At this same time, the Company stated that net earnings as a percent of sales were 6.0% for the first quarter of fiscal 2002, compared to 5.2% for the first quarter of fiscal 2001. According to the Company, this increase was primarily attributable to a higher gross profit rate and a decrease in selling and store operating expenses as a percent of sales. The Company further indicated that diluted earnings per share were \$0.36 and \$0.27 for the first quarters of fiscal 2002 and 2001, respectively.

**August 20, 2002 Press Release**

149. On August 20, 2002, the Company issued a press release titled “The Home Depot Reports Record Second Quarter Earnings of \$1.2 Billion.” In relevant part, that press release stated:

The Home Depot, the world's largest home improvement retailer, today reported record net earnings of \$1.182 billion (\$0.50 per diluted share) for the second quarter of fiscal 2002, an increase of 28% compared with net earnings of \$924 million (\$0.39 per diluted share) in fiscal 2001 and \$.03 ahead of consensus. Sales for the quarter increased 12% to \$16.3 billion and comparable store sales increased 1%.

“The Home Depot reported solid sales and earnings gains for the quarter, as our dedicated associates delivered great service and we offered our loyal customers tremendous value in areas like kitchen and bath, plumbing, paint and flooring,” said Bob Nardelli, Chairman, President & CEO of

The Home Depot. “During the quarter, we accelerated the rollout of new product assortments in key merchandising areas such as appliances, flooring, and decorative lighting. The strength of Home Depot was evident as we earned over a billion dollars this quarter, becoming only the second retailer to do so.”

“The Home Depot has a record \$5.9 billion in cash on the balance sheet and more than \$20 billion in equity,” said Nardelli. “In the midst of continuing economic uncertainty, the strength of our balance sheet and operating performance allows us to stay on strategy with new product offerings and 200 new store openings this year. At the same time, we have the financial flexibility to implement the \$2 billion share repurchase program we first announced in mid-July, further demonstrating our confidence in the company.”

\* \* \*

The Home Depot indicated it expects to earn \$0.40 diluted earnings per share for the third quarter of fiscal 2002, an increase of 21%. The company also indicated that it is comfortable with the current consensus earnings estimate for fiscal 2002 of \$1.57 diluted earnings per share, a 25% increase over fiscal 2001 on a 52-week basis.

150. As noted in one press report addressing this quarterly earnings announcement:

While Home Depot could not match the 42 percent increase in second-quarter earnings posted by rival Lowe's . . . it keeps a strong hold as the No. 1

home improvement company in the nation, said Alan Rifkin, a Lehman Brothers analyst.

\* \* \*

“We are reporting the most profitable quarter in company history. No matter how you look at it . . . Home Depot’s leadership in the home improvement industry is unquestionable,” said Carol Tome, chief financial officer. “We continue to distance ourselves with the best balance sheet against our peers.”

Investors were pleased that Home Depot exceeded expectations and did not back down from ambitious revenue growth targets for the rest of the year, Rifkin said

“Word had gotten out that their business had been a little soft,” he said. “Investors are encouraged that they didn’t take their numbers down.”

151. Commenting upon these second quarter results, Nancy Aversa, a research analyst at Victory Capital Management in Cleveland, Ohio, stated, “I was very pleased with their quarter . . . I think we are seeing some of the benefits of their consolidation on the buying side.”

**Form 10-Q for Second Quarter of Fiscal Year 2002**

152. On or about August 26, 2002, Home Depot filed with the SEC a Form 10-Q for the second quarter of Fiscal Year 2002 (ending August 4, 2002). Defendants Nardelli and Tomé signed Home Depot’s Form 10-Q

for the second quarter of Fiscal Year 2002. Furthermore, both Defendant Nardelli and Defendant Tomé certified (in accordance with the Sarbanes-Oxley Act of 2002) that (a) to their knowledge, “the Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934”; and (b) “[t]he information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.”

153. In that public filing, Home Depot reported that net sales for the second quarter of fiscal 2002 increased 11.7% to \$16.3 billion from \$14.6 billion for the second quarter of fiscal 2001; and that for the first six months of fiscal 2002, sales increased 14.1% to \$30.6 billion from \$26.8 billion for the comparable period in fiscal 2001.

154. In addition, Home Depot further stated that net earnings as a percent of sales were 7.3% and 6.7% for the second quarter and first six months of fiscal 2002, respectively, compared with 6.3% and 5.8% for the second quarter and first six months of fiscal 2001, respectively. This increase as a percent of sales, according to the Company, was primarily attributable to higher gross profit margin and lower operating expenses. The Company also reported that diluted earnings per share were \$0.50 and \$0.86

for the second quarter and first six months of fiscal 2002, respectively, compared to \$0.39 and \$0.66 for the second quarter and first six months of fiscal 2001, respectively.

155. The Company also reported that gross profit as a percent of sales was 30.4% for the second quarter of fiscal 2002 (compared with 29.7% for the second quarter of fiscal 2001) and that for the first six months of fiscal 2002, gross profit as a percent of sales was 30.5% compared with 29.8% for the comparable period of fiscal 2001. According to the Company, “The gross profit rate increase for both periods was primarily attributable to improvements in shrink....”

**November 19, 2002 Press Release**

156. On November 19, 2002, the Company issued a press release titled “The Home Depot Reports Record Third Quarter Earnings of \$940 Million.” In relevant part, that press release stated:

The Home Depot (NYSE: HD), the world's largest home improvement retailer, today reported record net earnings of \$940 million, or \$0.40 per diluted share, for the third quarter of fiscal 2002, an increase of 21% compared with net earnings of \$778 million, or \$0.33 per diluted share, in fiscal 2001. Sales for the quarter increased 9% to \$14.5 billion and comparable store sales decreased 2%.

\* \* \*

The Home Depot reconfirmed that it expects to earn \$0.31 diluted earnings per share for the fourth quarter of fiscal 2002, an increase of 15% over the fourth quarter of 2001 on a 13-week basis. The company also indicated that it is comfortable with \$1.57 diluted earnings per share for the fiscal year, a 25% increase over fiscal 2001 on a 52-week basis.

157. Commenting upon the Company's earnings announcement, analyst Nathan Lewis of Jackson Securities noted that Home Depot had "performed quite well given the current economic climate."

**Form 10-Q for Third Quarter of Fiscal Year 2002**

158. On or about December 5, 2002, Home Depot filed with the SEC a Form 10-Q for the third quarter of Fiscal Year 2002 (ending November 3, 2002). Nardelli and Tomé signed Home Depot's Form 10-Q for the third quarter of Fiscal Year 2002. Furthermore, both Defendant Nardelli and Defendant Tomé certified (in accordance with the Sarbanes-Oxley Act of 2002) that, to their knowledge, (a) "the Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934"; and (b) "[t]he information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company."

159. In that public filing, Home Depot reported that net sales for the third quarter of fiscal 2002 increased 8.9% to \$14.5 billion from \$13.3 billion for the third quarter of fiscal 2001 and that for the first nine months of fiscal 2002, net sales increased 12.4% to \$45.0 billion from \$40.1 billion for the comparable period in fiscal 2001.

160. The filing also reported that net earnings as a percent of sales were 6.5% and 6.6% for the third quarter and first nine months of fiscal 2002, respectively, compared with 5.9% and 5.8% for the third quarter and first nine months of fiscal 2001, respectively, and that the increases as a percent of sales were primarily attributable to a higher gross profit margin. The Company also stated that diluted earnings per share were \$0.40 and \$1.26 for the third quarter and first nine months of fiscal 2002, respectively, compared to \$0.33 and \$0.99 for the third quarter and first nine months of fiscal 2001, respectively.

161. The Company reported that gross profit as a percent of sales was 31.6% for the third quarter of fiscal 2002 compared with 30.2% for the third quarter of fiscal 2001, and for the first nine months of fiscal 2002, gross profit as a percent of sales was 30.8% compared with 29.9% for the comparable period of fiscal 2001. The Company claimed, “gross profit rate

increase for both periods was primarily attributable to improvements in shrink....”

162. With respect to the issue of internal controls, the Company stated:

The Company maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed in the Company’s Securities Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission’s rules and forms, and that such information is accumulated and communicated to the Company’s management, including its Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

During the 90-day period prior to the date of this report, an evaluation was performed under the supervision and with the participation of the Company’s Disclosure Committee and management, including the Chief Executive Officer and the Chief Financial Officer, of the effectiveness of the design and operation of the Company’s disclosure controls and procedures. Based upon that evaluation, the Chief Executive Officer and the Chief Financial Officer concluded that the Company’s disclosure controls and procedures were effective. There have been no significant changes in the Company’s internal controls or in other factors that could significantly affect these controls, and no corrective actions taken with regard to significant deficiencies or material weaknesses in such controls, subsequent

to the date of our most recent evaluation of internal controls.

**February 25, 2003 Press Release**

163. On February 25, 2003, the Company published a press release titled, "The Home Depot Reports Record 2002 Earnings; EPS Grows 21% to \$1.56 on Sales of \$58.2 Billion." In that press release, Home Depot reported "record net earnings" of \$3.7 billion (\$1.56 per diluted share) for fiscal 2002, compared with net earnings of \$3.0 billion (\$1.29 per diluted share) in fiscal 2001. The Company further stated that sales for fiscal 2002 increased 9 percent to \$58.2 billion and that comparable store sales were flat. Home Depot further indicated in this press release that for the fourth quarter of fiscal 2002, net earnings reached \$686 million (\$0.30 per diluted share) compared with \$710 million (\$0.30 per diluted share) in the fourth quarter of 2001. While this \$0.30 per diluted share figure was unchanged from the fourth quarter of the prior year, it still was three cents above the First Call /Thomson financial estimate.

164. The Company further reported that sales for the fourth quarter of fiscal 2002 totaled \$13.2 billion, a 2 percent decline from the fourth quarter of fiscal 2001. However, the Company was quick to point out that "the fourth quarter of 2001 consisted of 14 weeks and the year included

53 weeks.” According to the Company, comparing similar 52-week periods for 2001 to 2002, sales for 2002 increased 11 percent and earnings per diluted share increased 24 percent. In addition, comparing equivalent 13-week periods for the fourth quarter, sales for 2002 increased 5 percent and earnings per diluted share increased 11 percent.

**Form 10-K for Fiscal Year 2002**

165. On or about April 21, 2003, Home Depot filed with the SEC a Form 10-K for Fiscal Year 2002 (ending February 2, 2003). Defendants Nardelli, Tomé, Langone, Cox, and Clendenin signed Home Depot’s Form 10-K for Fiscal Year 2002.

166. In that public filing, Home Depot reported that net sales for fiscal 2002 increased 8.8% to \$58.2 billion from \$53.6 billion in fiscal 2001 and that this increase was attributable to the 203 new stores opened during fiscal 2002 and full year sales from the 204 new stores opened during fiscal 2001. The Company further noted that this increase was partially offset by the net sales attributable to an additional week in fiscal 2001 of \$880 million. The Company also stated that net earnings for fiscal 2002 were \$3.7 billion, up from \$3.0 billion in fiscal 2001. The Company further reported that comparable store-for-store sales were flat in fiscal 2002.

167. At this same time, Home Depot further reported that gross profit as a percent of sales was 31.1% for fiscal 2002 compared to 30.2% for fiscal 2001 and that the rate increase was attributable to a reduction in the cost of merchandise sold which resulted from centralized purchasing, as the Company continued rationalizing vendor and sku assortments. The Company also claimed that its gross profit increase was in part attributable to “enhanced inventory control, resulting in lower shrink levels....”

168. With regard to the issue of internal controls, the Company reported as follows:

The Company maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed in the Company's Securities Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and that such information is accumulated and communicated to the Company's management, including the Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

During the 90-day period prior to the date of this report, an evaluation was performed under the supervision and with the participation of the Company's Disclosure Committee and management, including the Chief Executive Officer and the Chief Financial Officer, of the effectiveness of the design and operation of the

Company's disclosure controls and procedures. Based upon that evaluation, the Chief Executive Officer and the Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective. There have been no significant changes in the Company's internal controls or in other factors that could significantly affect these controls, and no corrective actions taken with regard to significant deficiencies or material weaknesses in such controls, subsequent to the date of our most recent evaluation of internal controls.

169. Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, Home Depot's Form 10-K, filed on or about April 21, 2003, included certifications signed by Defendants Nardelli and Tomé to the effect that the information contained in the Form 10-K fairly presented, in all material respects, the financial condition and results of operations of the Company.

170. Defendants' statements concerning Home Depot's financial performance and condition relating to fiscal year 2002 as set forth above were each false and misleading when made because they misrepresented or omitted the following material adverse facts that the Defendants knew at the time the statements were made:

- a. That during fiscal year 2002, Home Depot was engaged in a scheme to inflate the Company's earnings through fraudulent RTV practices;

- b. That during fiscal year 2002, Home Depot derived a material portion of its revenues and profits from fraudulent RTV practices;
- c. That the Company had failing and deficient internal controls and procedures and lacked any meaningful ability to accurately report its financial results;
- d. That the Company's improper RTV practices were in direct violation of its own code of conduct; and
- e. That the Company's illicit scheme *vis-à-vis* fraudulent RTV practices potentially subjected Home Depot to substantial regulatory fines, penalties and other legal action, thereby compromising the Company's overall financial condition and prospects.

**C. Fiscal Year 2003**

**Press Release of May 20, 2003**

171. On May 20, 2003, the Company published a press release titled "Home Depot Reports Record First Quarter Earnings; EPS Increased 8.3% to \$0.39 on Sales of \$15.1 Billion." In relevant part, that press release stated:

The Home Depot, the world's largest home improvement retailer, today reported record first quarter net earnings of \$907 million (\$0.39 per diluted share) for fiscal 2003, compared with net earnings of \$856 million (\$0.36 per diluted share) in fiscal 2002. Sales for the period increased 5.8 percent to \$15.1 billion and comparable store sales declined 1.6 percent.

\* \* \*

The Home Depot reaffirmed that it expects sales for fiscal 2003 to increase between 9 and 12 percent and earnings per diluted share to increase between 9 and 14 percent. Comparable sales are expected to be flat to slightly positive on the year....

172. The Company's announcement appeared to impress analysts. The Company's "same-store sales were pretty encouraging, especially with the bad weather," said Alan Rifkin, an analyst at Lehman Brothers in an article appearing in the *Atlanta Journal-Constitution* (Mr. Rifkin further noted that: "[i]t certainly shows, on a sequential basis, they're closing the gap with Lowe's"). Moreover, as noted in a *Financial Times* report dated May 21, 2003: "[t]he world's largest home improvement retailer . . . offered a more upbeat assessment on sales as a result of its store renovations and national marketing campaign, reporting first-quarter same-store revenues down 1.6 per cent - much less than the 2-4 per cent decline

Wall Street had predicted. These results could mark a turning point for Bob Nardelli, Home Depot's chief executive . . .” (emphasis added).

**Form 10-Q for First Quarter of Fiscal Year 2003**

173. On or about June 6, 2003, Home Depot filed with the SEC a Form 10-Q for the first quarter of Fiscal Year 2003 (ending May 4, 2003). Defendants Nardelli and Tomé signed Home Depot's Form 10-Q for the first quarter of Fiscal Year 2003. Furthermore, both Defendant Nardelli and Defendant Tomé certified (in accordance with the Sarbanes-Oxley Act of 2002) that, to their knowledge, (a) “the Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934”; and (b) “[t]he information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.”

174. In that public filing, Home Depot reported that net sales for the first quarter of fiscal 2003 increased 5.8% to \$15.1 billion from \$14.3 billion in the first quarter of fiscal 2002 and that the sales increase for the period was attributable to new stores opened since the end of the first quarter of fiscal 2002 (1,568 stores open at the end of the first quarter of fiscal 2003 compared with 1,386 at the end of the first quarter of fiscal 2002). The

Company further reported that comparable store-for-store sales decreased 1.6% in the first quarter of fiscal 2003.

175. The Company also reported that diluted earnings per share were \$0.39 for the first quarter of fiscal 2003 compared to \$0.36 for the first quarter of fiscal 2002, reflecting a favorable impact of approximately \$0.01 per diluted share as a result of the repurchase of the shares of the Company's common stock in fiscal 2002.

176. The Company further stated that gross profit increased 10.8% to \$4.8 billion in the first quarter of fiscal 2003 from \$4.4 billion for the first quarter of fiscal 2002 and that the gross profit rate as a percentage of sales increased to 32.0% in the first quarter of fiscal 2003 from 30.5% in the first quarter of fiscal 2002. The Company claimed that the gross profit rate increase was "primarily attributable to continued benefit from centralized purchasing as Home Depot rationalized vendors and improved assortments, improvements in shrink...."

177. With respect to the issue of internal controls, the Company stated:

The Company maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed in the Company's Securities Exchange Act reports is

recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and that such information is accumulated and communicated to the Company's management, including its Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

During the 90-day period prior to the date of this report, an evaluation was performed under the supervision and with the participation of the Company's Disclosure Committee and management, including the Chief Executive Officer and the Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures. Based upon that evaluation, the Chief Executive Officer and the Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective. There have been no significant changes in the Company's internal controls or in other factors that could significantly affect these controls, and no corrective actions taken with regard to significant deficiencies or material weaknesses in such controls, subsequent to the date of our most recent evaluation of internal controls.

### **August 19, 2003 Press Release**

178. On August 19, 2003, the Company published a press release titled "The Home Depot Reports Record Earnings of \$1.3 Billion; Positive 2.2% Same Store Sales; 12% Increase in Diluted EPS to \$0.56." In relevant part, that press release stated:

The Home Depot, the world's largest home improvement retailer, today reported record second quarter net earnings of \$1.3 billion (\$0.56 per diluted share) for fiscal 2003, compared with net earnings of \$1.2 billion (\$0.50 per diluted share) in the second quarter of fiscal 2002. Sales for the period increased 10.5 percent to \$18.0 billion and comparable store sales increased 2.2 percent.

\* \* \*

“Our financial strength remains unsurpassed in our industry, as we completed the quarter with \$5.3 billion in cash and almost \$22 billion in equity. This strength allows us to stay on strategy through continued investment in our stores, our associates, and our commitment to industry-leading customer service,” Nardelli said.

179. Commenting on the Company’s announced results for the quarter, Jim Luke of BB&T Asset Management (which owns stock in Home Depot) stated that the Company had “taken some very right steps to get back on track.” “Bob Nardelli is turning things around,” noted Wayne Bopp, an analyst with Fifth Third Bank, which also holds Home Depot shares.

**Form 10-Q for the Second Quarter of Fiscal Year 2003**

180. On or about September 5, 2003, Home Depot filed with the SEC a Form 10-Q for the second quarter of Fiscal Year 2003 (ending August 3, 2003). Defendants Nardelli and Tomé signed Home Depot’s Form 10-Q for the second quarter of Fiscal Year 2003. In addition, in connection with

this quarterly report, Defendants Nardelli and Tomé certified, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to their knowledge, the information contained in the report “fairly presents, in all material respects, the financial condition and results of operations of the Company.” Moreover, by certifying this report, Defendants Nardelli and Tomé represented, *inter alia*, that the quality and accuracy of the information contained therein concerning the Company's financial performance and condition was safeguarded by internal financial controls in place at the Company, which were designed to foster the development of reliable financial statements.

181. In that public filing, Home Depot reported that net sales for the second quarter of fiscal 2003 increased 10.5% to \$18.0 billion from \$16.3 billion in the second quarter of fiscal 2002 and that for the first six months of fiscal 2003, sales increased 8.3% to \$33.1 billion from \$30.6 billion for the comparable period in fiscal 2002. According to the Company, the sales increase for both periods was primarily attributable to new stores opened since the end of the second quarter of fiscal 2002 (1,607 stores open at the end of the second quarter of fiscal 2003 compared with 1,437 at the end of the second quarter of fiscal 2002).

182. The Company further announced that gross profit increased 13.3% to \$5.6 billion in the second quarter of fiscal 2003 from \$4.9 billion in the second quarter of fiscal 2002 and that gross profit increased 12.1% to \$10.4 billion for the first six months of fiscal 2003 from \$9.3 billion in the first six months of fiscal 2002.

183. The Company also announced that diluted earnings per share were \$0.56 and \$0.96 in the second quarter and first six months of fiscal 2003, respectively, compared to \$0.50 and \$0.86 in the second quarter and first six months of fiscal 2002, respectively. According to the Company, diluted earnings per share were favorably impacted by approximately \$0.02 and \$0.03 per diluted share in the second quarter and first six months of fiscal 2003, respectively, as a result of the repurchase of shares of Home Depot common stock in fiscal 2002.

184. With respect to the issue of internal controls, the Company stated that:

The Company maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed in the Company's reports under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and

that such information is accumulated and communicated to the Company's management, including its Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

The Company's Chief Executive Officer and Chief Financial Officer have evaluated the effectiveness of the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of the end of the period covered by this report. Based on such evaluation, such officers have concluded that, as of the end of the period covered by this report, the Company's disclosure controls and procedures are effective in alerting them on a timely basis to material information relating to the Company (including its consolidated subsidiaries) required to be included in the Company's reports filed or submitted under the Exchange Act.

### **November 18, 2003 Press Release**

185. On November 18, 2003, the Company published a press release titled "The Home Depot Reports Record Third Quarter Results Raises Full Year Earnings Guidance." In relevant part, this press release stated:

The Home Depot®, the world's largest home improvement retailer, today reported record third quarter net earnings of \$1.15 billion (\$0.50 per diluted share) for fiscal 2003, compared with net earnings of \$940 million (\$0.40 per diluted share) in the third quarter of fiscal 2002. Sales for the quarter increased 14.7 percent to \$16.6 billion

compared with the third quarter of fiscal 2002. Comparable store sales increased 7.8 percent, the company's best quarterly comp performance since the fourth quarter of 1999.

The Home Depot reiterated its annual sales growth guidance of 9-12 percent and raised its full year earnings per share growth guidance to 15-17 percent for the 2003 fiscal year.

186. As noted in an *Atlanta Journal-Constitution* news report addressing the Company's announcement:

Home Depot abounded in confidence Tuesday as the company reported a record third-quarter profit and its best sales performance at older stores in nearly four years.

The Atlanta-based home improvement retailer said it earned \$1.15 billion on \$16.6 billion in sales during the quarter. In the same period last year, Home Depot earned \$940 million on \$14.5 billion in sales.

The company's earnings per share increased to 50 cents in the third quarter, from 40 cents a year ago. Home Depot topped Wall Street analysts' per-share earnings expectations of 46 cents, according to Thomson First Call.

Home Depot's earnings provided an affirmative answer to analysts who wondered whether the company could match Lowe's, which reported record third-quarter earnings Monday. Home Depot and Lowe's have been battling for supremacy in the home improvement sector.

"They're turning the corner," Blaylock & Partners analyst Mark Mandel said of Home Depot. "There's nothing like having a strong competitor to light a fire under your feet."

\* \* \*

The company reported its best sales at stores open more than a year in nearly four years. Wall Street had expected Home Depot's same-store sales to increase 5.2 percent in the third quarter; the figure was 7.8 percent.

"It shows that No. 1, they are engineering their turnaround," said Alan Rifkin, a Lehman Brothers analyst in New York. "Obviously it's taking hold."

\* \* \*

With Home Depot's turnaround progressing, Blaylock & Partners raised its target share price for the company to \$41 from \$39.

"We believe the momentum the company has seen in (the third quarter) should carry through the remainder of the quarter and into (2004)," Mandel said. . . .

### **Form 10-Q for Third Quarter of Fiscal Year 2003**

187. On or about December 4, 2003, Home Depot filed with the SEC a Form 10-Q for the third quarter of Fiscal Year 2003 (ending November 2, 2003). Defendants Nardelli and Tomé signed Home Depot's Form 10-Q for the third quarter of Fiscal Year 2003. In addition, in

connection with this quarterly report, Defendants Nardelli and Tomé certified, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to their knowledge, the information contained in the report “fairly presents, in all material respects, the financial condition and results of operations of the Company.” Moreover, by certifying this report, Defendants Nardelli and Tomé represented, *inter alia*, that the quality and accuracy of the information contained therein concerning the Company's financial performance and condition was safeguarded by internal financial controls in place at the Company, which were designed to foster the development of reliable financial statements.

188. In that public filing, the Company reported that net sales for the third quarter of fiscal 2003 increased 14.7% to \$16.6 billion from \$14.5 billion in the third quarter of fiscal 2002 and that for the first nine months of fiscal 2003, sales increased 10.3% to \$49.7 billion from \$45.0 billion for the comparable period in fiscal 2002. The Company also reported that gross profit increased 13.4% to \$5.2 billion in the third quarter of fiscal 2003 from \$4.6 billion in the third quarter of fiscal 2002, and increased 12.5% to \$15.6

billion for the first nine months of fiscal 2003 from \$13.9 billion in the first nine months of fiscal 2002.

189. The Company also reported that diluted earnings per share were \$0.50 and \$1.46 in the third quarter and first nine months of fiscal 2003, respectively, compared to \$0.40 and \$1.26 in the third quarter and first nine months of fiscal 2002, respectively. The Company stated that diluted earnings per share were favorably impacted by approximately \$0.02 and \$0.05 per diluted share in the third quarter and first nine months of fiscal 2003, respectively, "as a result of the repurchase of shares of our common stock in fiscal 2002 and fiscal 2003."

190. With regard to the issue of internal controls, the Company stated that:

The Company maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed in the Company's reports under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and that such information is accumulated and communicated to the Company's management, including its Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

The Company's Chief Executive Officer and Chief Financial Officer have evaluated the effectiveness of the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of the end of the period covered by this report. Based on such evaluation, such officers have concluded that, as of the end of the period covered by this report, the Company's disclosure controls and procedures are effective in alerting them on a timely basis to material information relating to the Company (including its consolidated subsidiaries) required to be included in the Company's reports filed or submitted under the Exchange Act.

**February 24, 2004 Press Release**

191. On February 24, 2004, the Company issued a press release titled "The Home Depot Announces Record Fourth Quarter and Fiscal Year 2003 Results." In relevant part, that press release stated:

The Home Depot®, the world's largest home improvement retailer, today reported net earnings of \$951 million (\$0.42 per diluted share, up 40%) for the fourth quarter of fiscal 2003, compared with \$686 million (\$0.30 per diluted share) in the fourth quarter of fiscal 2002. Sales for the fourth quarter of fiscal 2003 totaled \$15.1 billion, a 14.5 percent increase from the fourth quarter of fiscal 2002. Comparable store sales for the fourth quarter of fiscal 2003 increased 7.6 percent.

For fiscal 2003, the company reported record net earnings of \$4.3 billion (\$1.88 per diluted share, up 21%), compared to net earnings of \$3.7 billion (\$1.56 per diluted share) in fiscal 2002. Sales for

fiscal 2003 increased 11.3 percent over fiscal 2002 to \$64.8 billion and comparable store sales grew by 3.8 percent.

\* \* \*

The company reiterated fiscal 2004 sales growth guidance of 9-12 percent and full-year earnings per diluted share growth guidance of 10-14 percent, excluding the change in accounting for certain vendor allowances due to EITF 02-16. Including the impact of EITF 02-16, earnings per diluted share growth guidance for fiscal 2004 is 7-11 percent.

192. Commenting upon the Company's announcement of its fourth quarter results, Nancy Aversa, an analyst with Victory Capital Management in Cleveland, said that "[i]f anything, this quarter indicated that the operating leverage that this company can generate regardless of top-line growth is pretty spectacular."

**Form 10-K for Fiscal Year 2003**

193. On or about April 12, 2004, Home Depot filed with the SEC a Form 10-K for Fiscal Year 2003 (ending February 1, 2004). Defendants Nardelli, Tomé, Langone, Cox, and Clendenin signed Home Depot's Form 10-K for Fiscal Year 2003.

194. In that public filing, Home Depot reported that net sales for fiscal 2003 increased 11.3% to \$64.8 billion from \$58.2 billion in fiscal

2002. The Company also reported that gross profit increased 13.7% to \$20.6 billion for fiscal 2003 from \$18.1 billion for fiscal 2002, and that gross profit as a percent of Net Sales was 31.8% for fiscal 2003 compared to 31.1% for fiscal 2002. The company claimed that its increase in the gross profit rate was in part attributable to “improved inventory management, which resulted in lower shrink levels....”

195. The Company also noted that diluted earnings per share were \$1.88 and \$1.56 in fiscal 2003 and fiscal 2002, respectively and that diluted earnings per share were favorably impacted in fiscal 2003 as a result of the repurchase of shares of the Company’s common stock in fiscal 2002 and fiscal 2003. The Company expected that in fiscal 2004, diluted earnings per share would grow by 7% to 11%, including the adoption of Emerging Issues Task Force 02-16, “Accounting by a Customer (Including a Reseller) for Certain Consideration Received from a Vendor” (“EITF 02-16”).

196. With respect to the issue of internal controls, the Company reported that:

The Company maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed in the Company's Securities Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the Securities

and Exchange Commission's rules and forms, and that such information is accumulated and communicated to the Company's management, including the Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

The Company's Chief Executive Officer and Chief Financial Officer have evaluated the effectiveness of the design and operation of the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act) as of the end of the period covered by this report. Based on such evaluation, such officers have concluded that, as of the end of the period covered by this report, the Company's disclosure controls and procedures are effective.

There have not been any changes in the Company's internal control over financial reporting (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act) during the fiscal quarter ended February 1, 2004 that have materially affected, or are reasonably likely to materially affect the Company's internal control over financial reporting.

197. Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, Home Depot's Form 10-K, filed on or about April 12, 2004, included certifications signed by Defendants Nardelli and Tomé to the effect that the information contained in the Form 10-K fairly presented, in all material respects, the financial condition and results of operations of the Company. Moreover, by certifying this report, Defendants Nardelli and Tomé

represented, *inter alia*, that the quality and accuracy of the information contained therein concerning the Company's financial performance and condition was safeguarded by internal financial controls in place at the Company, which were designed to foster the development of reliable financial statements.

198. Defendants' statements concerning Home Depot's financial performance and condition relating to fiscal year 2003 as set forth above were each false and misleading when made because they misrepresented or omitted the following material adverse facts that the Defendants knew at the time the statements were made:

- a. That during fiscal year 2003, Home Depot was engaged in a scheme to inflate the Company's earnings through fraudulent RTV practices;
- b. That during fiscal year 2003, Home Depot derived a material portion of its revenues and profits from fraudulent RTV practices;
- c. That the Company had failing and deficient internal controls and procedures and lacked any meaningful ability to accurately report its financial results;

- d. That the Company's improper RTV practices were in direct violation of its own code of conduct; and
- e. That the Company's illicit scheme *vis-à-vis* fraudulent RTV practices potentially subjected Home Depot to substantial regulatory fines, penalties and other legal action, thereby compromising the Company's overall financial condition and prospects.

**D. Fiscal Year 2004**

**May 18, 2004 Press Release**

199. On May 18, 2004, the Company issued a press release titled "The Home Depot Announces Record First Quarter 2004 Earnings." In relevant part, that press release stated:

The Home Depot, the world's largest home improvement retailer, today reported record first quarter net earnings of \$1.1 billion, \$0.49 per diluted share, up 26 percent, for the first quarter of fiscal 2004, compared with \$907 million, \$0.39 per diluted share, for first quarter fiscal 2003. Excluding the impact of the adoption of EITF 02-16, diluted earnings per share would have been \$0.52, or 33 percent higher than last year.

Sales for the period increased \$2.4 billion, 16 percent to \$17.6 billion. Comparable store sales rose 7.7 percent, the highest first quarter comparable store sales growth in five years.

\* \* \*

Based on its first quarter performance, the company announced that it has raised fiscal 2004 sales growth guidance to 10-12 percent. The company also raised its fiscal 2004 EPS growth guidance from 7-11 percent to 10-14 percent. Excluding the impact of EITF 02-16, the company expects EPS growth of 13-16 percent for fiscal 2004.

\* \* \*

“We also experienced the third quarter of sequential improvement in sales per square foot, which increased 3.9 percent to \$376.80,” added Carol Tome, executive vice president, chief financial officer. “This key productivity metric demonstrates solid progress in the transformation of our business.”

#### **Form 10-Q for First Quarter of Fiscal Year 2004**

200. On or about June 4, 2004, Home Depot filed with the SEC a Form 10-Q for the first quarter of Fiscal Year 2004 (ending May 2, 2004). Defendants Nardelli and Tomé signed Home Depot’s Form 10-Q for the first quarter of Fiscal Year 2004. In addition, in connection with this quarterly report, Defendants Nardelli and Tomé certified, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to their knowledge, the information contained in the report

“fairly presents, in all material respects, the financial condition and results of operations of the Company.” Moreover, by certifying this report, Defendants Nardelli and Tomé represented, *inter alia*, that the quality and accuracy of the information contained therein concerning the Company's financial performance and condition was safeguarded by internal financial controls in place at the Company, which were designed to foster the development of reliable financial statements.

201. In that public filing, the Company reported that net sales for the first quarter of fiscal 2004 increased 16.2% to \$17.6 billion from \$15.1 billion for the first quarter of fiscal 2003 and that net sales growth was driven by an increase in comparable store sales of 7.7% and sales from stores open for less than one year. The Company further indicated that it expected sales growth of 10% to 12% driven by comparable store sales, new store openings and stores opened during fiscal 2003. The Company also reported that gross profit increased 19.4% to \$5.8 billion for the first quarter of fiscal 2004 from \$4.8 billion for the first quarter of fiscal 2003, and that gross profit as a percentage of net sales was 32.9% for the first quarter of fiscal 2004 compared to 32.0% for the first quarter of fiscal 2003.

202. The Company further indicated that (a) diluted earnings per share was \$0.49 for the first quarter of fiscal 2004 compared to \$0.39 for the first quarter of fiscal 2003; (b) excluding the impact of the adoption of EITF 02-16, diluted earnings per share would have been \$0.52, or 33.3% higher than the prior year; and (c) diluted earnings per share was favorably impacted in the first quarter of fiscal 2004 as a result of the repurchase of shares of the Company's common stock in fiscal 2003 and 2004.

203. With regard to the issue of internal controls, the Company stated:

The Company maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed in the Company's Securities Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and that such information is accumulated and communicated to the Company's management, including its Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

The Company's Chief Executive Officer and Chief Financial Officer have evaluated the effectiveness of the design and operation of the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act) as of the end of the period covered by this report. Based upon that evaluation, the

Chief Executive Officer and the Chief Financial Officer concluded that, as of the end of the period covered by this report, the Company's disclosure controls and procedures were effective.

**August 17, 2004 Press Release**

204. On August 17, 2004, the Company issued a press release titled "The Home Depot Continues Strong Performance and Announces Record Second Quarter Results." In relevant part, that press release stated:

The Home Depot®, the world's largest home improvement retailer, today reported record second quarter net earnings of \$1.5 billion, \$0.70 per diluted share, up 25 percent, for second quarter fiscal 2004, compared to \$0.56 per diluted share, for second quarter fiscal 2003. Excluding the impact of the adoption of EITF 02-16, diluted earnings per share would have been \$0.71, or 27 percent higher than last year.

Sales for the period increased \$2.0 billion, or 11 percent, to \$20.0 billion. Comparable store sales rose 4.8 percent, with strength across all geographic regions. "Our business strategy of enhancing the core, extending the business and expanding our markets is clearly driving consistent, profitable sales growth. For the first time in our company's 25-year history, we achieved \$20 billion in sales in a single quarter. This achievement demonstrates that our knowledgeable associates are delivering on our company's core purpose: to improve everything we touch," said Bob Nardelli, chairman, president & CEO.

\* \* \*

“In addition to our record sales during the second quarter, the company had record operating margin of 12.3 percent, one of the highest in retail, reflecting strong gross margin expansion and good expense control,” said Carol Tome, executive vice president, CFO.

\* \* \*

The company reiterated its fiscal 2004 sales growth guidance of 10-12 percent and increased its fiscal 2004 EPS growth guidance from 10-14 percent to 14-17 percent.

205. Analysts reacted favorably to the Company’s announcement. For example, Eric Bosshard, an analyst with FTN Midwest Research in Cleveland, noted that “[i]t was a very impressive performance in an environment where interest rates are rising and gas prices are rising.”

**Form 10-Q for the Second Quarter of Fiscal Year 2004**

206. On or about September 2, 2004, Home Depot filed with the SEC a Form 10-Q for the second quarter of Fiscal Year 2004 (ending August 1, 2004). Defendants Nardelli and Tomé signed Home Depot’s Form 10-Q for the second quarter of Fiscal Year 2004. In addition, in connection with this quarterly report, Defendants Nardelli and Tomé certified, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-

Oxley Act of 2002, that, to their knowledge, the information contained in the report “fairly presents, in all material respects, the financial condition and results of operations of the Company.” Moreover, by certifying this report, Defendants Nardelli and Tomé represented, *inter alia*, that the quality and accuracy of the information contained therein concerning the Company's financial performance and condition was safeguarded by internal financial controls in place at the Company, which were designed to foster the development of reliable financial statements.

207. In that public filing, the Company reported that net sales for the second quarter of fiscal 2004 increased 11.0% to \$20.0 billion from \$18.0 billion for the second quarter of fiscal 2003 and further stated that for the first six months of fiscal 2004, sales increased 13.3% to \$37.5 billion from \$33.1 billion for the comparable period in fiscal 2003.

208. The Company reported that gross profit increased 18.8% to \$6.7 billion for the second quarter of fiscal 2004 from \$5.6 billion for the second quarter of fiscal 2003, and increased 19.1% to \$12.4 billion for the first six months of fiscal 2004 from \$10.4 billion for the first six months of fiscal 2003. The Company claimed that gross profit as a percentage of net sales was 33.4% for the second quarter of fiscal 2004 compared to 31.2% for

the second quarter of fiscal 2003, and was 33.1% for the first six months of fiscal 2004 compared with 31.5% for the comparable period of fiscal 2003. The Company claimed that the gross profit rate increase for both periods “was primarily attributable to lower shrink than we experienced in the comparable periods of fiscal 2003....”

209. According to the Company, diluted earnings per share was \$0.70 and \$1.18 for the second quarter and first six months of fiscal 2004, respectively, compared to \$0.56 and \$0.96 for the second quarter and first six months of fiscal 2003, respectively.

210. With respect to the issue of internal controls, the Company stated that:

The Company maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed in the Company's Securities Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and that such information is accumulated and communicated to the Company's management, including its Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

The Company's Chief Executive Officer and Chief Financial Officer have evaluated the effectiveness of the design and operation of the Company's

disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act) as of the end of the period covered by this report. Based upon that evaluation, the Chief Executive Officer and the Chief Financial Officer have concluded that, as of the end of the period covered by this report, the Company's disclosure controls and procedures were effective.

### **November 16, 2004 Press Release**

211. On November 16, 2004, the Company issued a press release titled "The Home Depot Reports Record Third Quarter Results, Increases Fiscal 2004 EPS Growth Guidance to 19-20 Percent." In relevant part, that press release stated:

The Home Depot(R), the world's largest home improvement retailer, today reported record third quarter fiscal 2004 net earnings of \$1.3 billion, or \$0.60 per diluted share, up 20 percent compared to \$0.50 per diluted share for the third quarter fiscal 2003.

Sales for the period increased \$2.2 billion, or 13.1 percent, to \$18.8 billion. Comparable store sales rose 4.5 percent.

Based on the strong third quarter performance, the company announced that it is raising its fiscal 2004 earnings per share growth guidance from 14-17 percent to 19-20 percent.

\* \* \*

The company ended the quarter with \$39.6 billion in total assets, including \$3.4 billion in cash and stockholders' equity of \$23.7 billion.

“Our solid financial results drove our return on invested capital to 21.4 percent, up 260 basis points from the third quarter last year,” said Carol Tome, executive vice president, CFO, The Home Depot. “Our financial condition remains unparalleled in retail.”

212. Analysts reacted favorably to the foregoing announcement. For example, Eric Bosshard, an analyst with FTN Midwest Research in Cleveland, stated that “[t]his is still very much a turnaround story. . . . We think the Home Depot story is very powerful based on the magnitude of internal improvements taking place.”

#### **Form 10-Q for Third Quarter of Fiscal Year 2004**

213. On or about December 2, 2004, Home Depot filed with the SEC a Form 10-Q for the third quarter of Fiscal Year 2004 (ending October 31, 2004). Defendants Nardelli and Tomé signed Home Depot’s Form 10-Q for the third quarter of Fiscal Year 2004. In addition, in connection with this quarterly report, Defendants Nardelli and Tomé certified, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to their knowledge that the information contained in the report “fairly presents, in all material respects, the financial condition

and results of operations of the Company.” Moreover, by certifying this report, Defendants Nardelli and Tomé represented, *inter alia*, that the quality and accuracy of the information contained therein concerning the Company's financial performance and condition was safeguarded by internal financial controls in place at the Company, which were designed to foster the development of reliable financial statements.

214. In that public filing, Home Depot reported that net sales for the third quarter of fiscal 2004 increased 13.1% to \$18.8 billion from \$16.6 billion for the third quarter of fiscal 2003. For the first nine months of fiscal 2004, the Company reported that sales increased 13.3% to \$56.3 billion from \$49.7 billion for the comparable period in fiscal 2003. According to the Company, net sales growth for the third quarter and the first nine months of fiscal 2004 was driven by, *inter alia*, an increase in comparable store sales of 4.5% and 5.6%, respectively.

215. The Company also reported that gross profit increased 20.4% to \$6.3 billion for the third quarter of fiscal 2004 from \$5.2 billion for the third quarter of fiscal 2003 and 19.5% to \$18.7 billion for the first nine months of fiscal 2004 from \$15.6 billion for the first nine months of fiscal 2003.

216. The Company further indicated that gross profit as a percentage of net sales was 33.3% for the third quarter of fiscal 2004 compared to 31.3% for the third quarter of fiscal 2003, and that for the first nine months of fiscal 2004, gross profit as a percentage of net sales was 33.2% compared with 31.4% for the comparable period of fiscal 2003. The company claimed that its gross profit rate increased in part because of “lower shrink than it experienced in the comparable periods of fiscal 2003....”

217. With regard to the issue of diluted earnings per share, the Company reported that:

Diluted earnings per share was \$0.60 and \$1.78 for the third quarter and first nine months of fiscal 2004, respectively, compared to \$0.50 and \$1.46 for the third quarter and first nine months of fiscal 2003, respectively. . For fiscal year 2004, we estimate our diluted earnings per share growth will be 19% to 20%.

218. With regard to the issue of internal controls, the Company stated that:

The Company maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed in the Company's Securities Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the Securities

and Exchange Commission's rules and forms, and that such information is accumulated and communicated to the Company's management, including its Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

The Company's Chief Executive Officer and Chief Financial Officer have evaluated the effectiveness of the design and operation of the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act) as of the end of the period covered by this report. Based upon that evaluation, the Chief Executive Officer and the Chief Financial Officer have concluded that, as of the end of the period covered by this report, the Company's disclosure controls and procedures were effective.

219. Defendants' statements concerning Home Depot's financial performance and condition relating to fiscal year 2004 as set forth above were each false and misleading when made because they misrepresented or omitted the following material adverse facts that the Defendants knew at the time the statements were made:

- a. That during fiscal year 2004, Home Depot was engaged in a scheme to inflate the Company's earnings through fraudulent RTV practices;

- b. That during fiscal year 2004, Home Depot derived a material portion of its revenues and profits from fraudulent RTV practices;
- c. That the Company had failing and deficient internal controls and procedures and lacked any meaningful ability to accurately report its financial results;
- d. That the Company's improper RTV practices were in direct violation of its own code of conduct; and
- e. That the Company's illicit scheme *vis-à-vis* fraudulent RTV practices potentially subjected Home Depot to substantial regulatory fines, penalties and other legal action, thereby compromising the Company's overall financial condition and prospects.

### **GAAP VIOLATIONS**

220. The Company's fraudulent vendor chargebacks violated GAAP and the SEC's regulations governing financial statement reporting.

221. GAAP are those principles recognized by the accounting profession as the conventions, rules, and procedures necessary to define accepted accounting practices at a particular time. Those principles are the

official standards accepted by the SEC and promulgated in part by the American Institute of Certified Public Accountants (“AICPA”), a private professional association, through three successor groups it established: the Committee on Accounting Procedure; the Accounting Principles Board (the “Board”), and the Financial Accounting Standards Board (the “FASB”) with the permission of the SEC (Accounting Series Release 150).

222. The SEC requires that public companies prepare their financial statements in accordance with GAAP. As set forth in SEC Rule 4-01(a) of SEC Regulation S-X, “[f]inancial statements filed with the [SEC] which are not prepared in accordance with [GAAP] will be presumed to be misleading or inaccurate.” 17 C.F.R. § 210.4-01(a)(1).

223. Management is responsible for preparing financial statements that conform with GAAP. As noted by AICPA auditing standards (“AU”), § 110.02:

Financial statements are management's responsibility . . . management is responsible for adopting sound accounting policies and for establishing and maintaining internal controls that will, among other things, record, process, summarize, and report transactions (as well as events and conditions) consistent with management's assertions embodied in the financial statements. The entity's transactions and the related assets, liabilities and equity are within the direct knowledge and control of management... Thus, the fair presentation of financial

statements in conformity with Generally Accepted Accounting Principles is an implicit and integral part of management's responsibility.

224. The Company's financial statements filed with the SEC during the Class Period violated the following provisions of GAAP, among others:

a. The principle that financial reporting should provide information that is useful to present and potential investors and other users in making rational investment, credit and similar decisions. (FASB Statement of Financial Accounting Concepts – "SFAC" No. 1);

b. The principle that financial reporting should provide information about how management of an enterprise has discharged its stewardship responsibility to owners (stockholders) for the use of enterprise resources entrusted to it. (SFAC No. 1);

c. The principle that financial reporting should be reliable in that it represents what it purports to represent. That information should be reliable as well as relevant is a notion that is central to accounting. (SFAC No. 2);

d. The principle of completeness, which means that nothing is left out of the information that may be necessary to insure that it validly represents underlying events and conditions. (SFAC No. 2);

e. The principle that conservatism be used as a prudent reaction to uncertainty to try to ensure that uncertainties and risks inherent in business situations are adequately considered. The best way to avoid injury to investors is to try to ensure that what is reported represents what it purports to represent. (SFAC No. 2);

225. The foregoing provisions of GAAP were violated, *inter alia*, to the extent that (1) Home Depot failed to disclose the fraudulent RTV chargebacks in its financial statements; (2) Home Depot overstated its earnings through fraudulent RTV chargebacks, (3) Home Depot's undisclosed practices of processing fraudulent vendor chargebacks potentially exposed the Company to significant regulatory fines and penalties; and (4) Home Depot failed to disclose the uncertainty surrounding its ability to continue to recognize revenue and earnings from fraudulent RTV chargebacks in the event that the true nature of the revenue and earnings was publicly disclosed.

226. The SEC regulates statements by companies “that can reasonably be expected to reach investors and the trading markets, whoever the intended primary audience.” SEC Release No. 33-6504, 3 Fed. Sec. L. Rep. (CCH) 23,120, at 17,095-3, 17 C.F.R. § 241.20560 (Jan. 13, 1984). Under SEC regulations, the management of a public company has a duty promptly “to make full and prompt announcements of material facts regarding the company’s financial condition.” SEC Release No. 34-8995, 3 Fed. Sec. L. Rep. (CCH) 23,120A, at 17,095, 17 C.F.R. § 241.8995 (Oct. 15, 1970). The SEC has emphasized that “[i]nvestors have legitimate expectations that public companies are making, and will continue to make, prompt disclosure of significant corporate developments.” SEC Release No. 18271, [1981-1982 Transfer Binder] Fed. Sec. L. Rep. (CCH) 83,049, at 84,618 (Nov. 19, 1981).

227. In Securities Act Release No. 6349 (Sept. 8, 1981), the SEC stated that:

[I]t is the responsibility of management to identify and address those key variables and other qualitative and quantitative factors which are peculiar to and necessary for an understanding and evaluation of the individual company.

228. In Accounting Series Release 173, the SEC reiterated the duty of management to present a true representation of a company's operations:

[I]t is important that the overall impression created by the financial statements be consistent with the business realities of the company's financial position and operations.

229. Item 7 of Form 10-K and Item 2 of Form 10-Q, Management's Discussion and Analysis of Financial Condition and Results of Operations, require the issuer to furnish information required by Item 303 of Regulation S-K [17 C.F.R. § 229.303].

230. On May 18, 1989, the SEC issued an interpretive release (Securities Act Release No. 6835 - May 18, 1989) which stated, in relevant part:

The MD&A requirements are intended to provide, in one section of a filing, material historical and prospective textual disclosure enabling investors and other users to assess the financial condition and results of operations of the registrant, with particular emphasis on the registrant's prospects for the future. As the Concept Release states:

The Commission has long recognized the need for a narrative explanation of the financial statements, because a numerical presentation and brief accompanying footnotes alone may be insufficient for an investor to judge the quality of earnings and

the likelihood that past performance is indicative of future performance. MD&A is intended to give the investor an opportunity to look at the company through the eyes of management by providing both a short and long term analysis of the business of the company. The Item asks management to discuss the dynamics of the business and to analyze the financials.

231. SEC Staff Accounting Bulletin No. 101 (“SAB 101”), Revenue Recognition in Financial Statements, drawing from Regulation S-K, Article 303, and Financial Reporting Release No. 36, also reiterated the importance of the MD&A in financial statements:

Management’s Discussion & Analysis (MD&A) requires a discussion of liquidity, capital resources, results of operations and other information necessary of a registrant’s financial condition, changes in financial condition and results of operations. This includes unusual or infrequent transactions, known trends, or uncertainties that have had, or might reasonably be expected to have, a favorable or unfavorable material effect on revenue, operating income or net income and the relationship between revenue and the costs of the revenue. Changes in revenue should not be evaluated solely in terms of volume and price changes, but should also include an analysis of the reasons and factors contributing to the increase or decrease. The Commission stated in Financial Reporting Release (FRR) 36 that MD&A should “give investors an opportunity to look at the registrant through the eyes of management by providing a historical and prospective analysis of the registrant’s financial condition and results of

operations, with a particular emphasis on the registrant's prospects for the future.”

(Footnotes omitted.)

232. In discussing results of operations, Item 303 of Regulation S-K requires the registrant to “[d]escribe any known trends or uncertainties that have had or that the registrant reasonably expects will have a material favorable or unfavorable impact on net sales or revenues or income from continuing operations.” The Instructions to Paragraph 303(a) further state, “[t]he discussion and analysis shall focus specifically on material events and uncertainties known to management that would cause reported financial information not to be necessarily indicative of future operating results.” 17 C.F.R. § 229.303(a)(1)-(3) and Instruction 3.

233. In addition, the SEC, in its May 18, 1989 Interpretive Release No. 34-26831, has indicated that registrants should employ the following two-step analysis in determining when a known trend or uncertainty is required to be included in the MD&A disclosure pursuant to Item 303 of Regulation S-K: (a) a disclosure duty exists where a trend, demand, commitment, event or uncertainty is both presently known to management; and (b) is reasonably likely to have a material effect on the registrant's financial condition or results of operations.

234. However, the MD&A section of Home Depot's filings with the SEC during the Class Period failed to comply with the foregoing SEC regulations because, among other things, (1) Home Depot failed to disclose the fraudulent RTV chargebacks in its financial statements despite their materiality; (2) Home Depot overstated its earnings through fraudulent RTV chargebacks, (3) Home Depot's undisclosed practices *vis-à-vis* fraudulent vendor chargebacks potentially exposed the Company to significant regulatory fines and penalties; and (4) Home Depot failed to disclose the uncertainty surrounding its ability to continue to recognize earnings from fraudulent RTV chargebacks in the event that the true nature of the earnings was publicly disclosed.

### **SCIENTER ALLEGATIONS**

235. In addition to the allegations set forth above, the following allegations also give rise to a strong inference that the Individual Defendants acted with scienter with respect to the false and misleading statements in that they had actual knowledge of their falsity or acted with reckless disregard for the truth. Specifically, they knew, or but for their deliberate recklessness would have known of the fraudulent RTV practices and the extent to which

those illicit practices had artificially inflated the Company's financial results during the Class Period.

**The Pervasiveness, Magnitude and Duration of the Fraud  
Support a Strong Inference of Scienter**

236. The fact that the Company processed fraudulent RTV chargebacks in stores throughout the country constitutes strong circumstantial evidence that the Individual Defendants knew or, at a minimum, recklessly disregarded the extent to which the illicit misconduct has artificially inflated the Company's financial results.

237. As detailed above, former employees detailed how the illicit misconduct was "common place" in, *inter alia*, the Northwest Division, at least four stores in the New York region, three stores in the Connecticut region, numerous stores in California (California is not part of the Northwest Division) and at least one store in Massachusetts. Additionally, current and former Home Depot employees in stores spanning at least four states, including the Company's corporate headquarters in Atlanta, detailed the fraud to the media.

238. The pervasiveness of the fraud is further evidenced by a supposed internal investigation in which Company auditors descended on stores in Washington, D.C., Virginia, Maryland, Pennsylvania and New

York and interrogated store employees, sometimes for up to five hours at a stretch, and carried away documents, as alleged above.

239. Indeed, the fraudulent misconduct did not occur by happenstance. Rather, it occurred pervasively within Home Depot stores across the country, evidencing a companywide scheme orchestrated at corporate headquarters that could have only occurred with the knowledge or deliberate recklessness of the Individual Defendants.

240. In addition to its pervasiveness, the fraud's astonishing magnitude gives rise to a strong inference of scienter. According to CW2, the impact of the fraud at just two stores amounted to approximately \$1 million annually. Extrapolated on a company wide basis, the magnitude of the fraud was roughly \$1 billion per year, in pure profit, or 10% of Home Depot's \$10.6 billion operating income in 2003.

241. Davis, in connection with the Whistleblower Complaint, corroborated the amount when he reported to the media that the fraud at the Aspen, Maryland store amounted to \$25,000 per week, or approximately \$1.3 million per year. As CNBC reported, extending that amount out to the more than 2,000 stores in the Home Depot Empire and the fraud amounted to more than \$1 billion annually in earnings.

242. It is simply inconceivable that the Company fraudulently misrepresented its financial results at such an enormous magnitude unless the Individual Defendants knew or, at a minimum, were severely reckless in not knowing that the use of fraudulent RTVs had artificially inflated the Company's financial results.

243. In addition to the pervasiveness and magnitude, the duration of the fraud gives rise to a strong inference that the Individual Defendants knew or, at a minimum, were severely reckless in not knowing, that the Company's financial results were materially misstated during the Class Period. According to numerous former employees, the fraud began well before the Class Period. Indeed, according to CW4, the fraud dates back to perhaps as far as 1993.

**The Mercer Memo  
Gives Rise to a Strong Inference of Scienter**

244. The fact that in April 2002 Mercer circulated a memo to all store managers that discussed "missed RTV dollars" and pinpointed specific departments that had the greatest opportunity to "boost chargebacks" creates a strong inference of scienter.

245. As detailed above, CW5 reported that following the Mercer Memo every department manager was required to spend an hour each week

processing RTV chargebacks, which increased the fraudulent chargebacks by approximately 25%.

246. That the locus of the fraud was fraudulent RTVs and that Mercer authored a companywide memo (in the heart of the Class Period) that resulted in increased processing of fraudulent RTVs gives rise to a strong inference that Mercer knew or, at a minimum, was severely reckless in not knowing of the misconduct alleged herein.

247. Further, according to CW5, the Company had a centralized system of distributing memos to the more than 2000 stores in the Home Depot Empire, and over 95% of memos came in the form of a voicemail. CW5 explained that the Mercer Memo was a “red flagged” memo because it came in writing, was backed up by voice-mailed instructions, and resulted in extensive changes in-store, including mandatory manager hours with the RTV clerks and vendor lists with RTV allowances printed out and handed out to management.

248. That the Mercer Memo was widely distributed throughout the Company, in writing and backed up by voicemail, gives rise to a strong inference that each of the Individual Defendants knew or, at a minimum, recklessly disregarded the fraud.

**The February 12, 2004 Memo  
Gives Rise to a Strong Inference of Scienter**

249. That a “senior Home Depot official” told *The New York Post* that the Company had issued a memo on February 12, 2004 to “quell the concerns of several employees who complained that superiors were pressuring them to participate in the scheme,” gives rise to a strong inference of scienter.

250. According to *The New York Post* in an article dated August 11, 2005, “a senior Home Depot official had acknowledged that management has been aware of the problem for at least 19 months, when a memo dated February 12, 2004, was circulated by the corporate office that outlined procedures for collecting chargebacks from suppliers.”

251. Indeed, the fact that Home Depot issued the memo to “quell the concerns of several employees who complained that superiors were pressuring them to participate in the scheme” is tantamount to an admission that the Individual Defendants knew, or but for their severe recklessness should have known, that the Company was engaging in fraudulent RTV practices to artificially inflate earnings.

**The RTV Overhaul  
Gives Rise to a Strong Inference of Scienter**

252. That the Company Home Depot identified the need to overhaul the RTV system in the summer of 2003, and identified the overhaul as a “critical focus area in 2004” gives rise to a strong inference of scienter.

253. As stated in the July 1, 2004 Memo, and reiterated in the November 11, 2004 Memo, the goal of the RTV overhaul was to “*reinforce desired behaviors*” and provide “more consistent and accurate RTV execution in stores.” To accomplish this goal, the overhauled system would prohibit “*store override[s] of negotiated RTV policies,*” and would provide “improved metrics and reporting to be generated upon rollout” that would “*track supplier product performance (i.e. true defective rate).*” (Emphasis added.)

254. That in the summer of 2003 the Company’s senior most management identified the need to reinforce desired RTV behaviors and identify the “true defective rate” of defective merchandise gives rise to a strong inference that the Individual Defendants knew or with deliberate recklessness disregarded the fact that fraudulent RTVs were being processed to artificially inflate the Company’s financial results.

**Budgeting for the Fraud  
Gives Rise to a Strong Inference of Scienter**

255. That the Company's written Plan included budgeting for the fraud gives rise to a strong inference of scienter. As alleged above, CW1 explained that the Plan included "Vendor Income (Rebates)" which accounted for 4.5% of gross margins in 2001, and were targeted to increase to 4.7% in 2002, 4.9% in 2003, and 5.2% by 2004. Initially the Plan referred to the line item as "Vendor Income." According to CW1, the Plan changed the language to read, "Vendor Income (Rebates)" to disguise the fact that the Company accounted for RTVs in gross margins in blatant violation of GAAP.

**INAPPLICABILITY OF SAFE HARBOR**

256. The statutory safe harbor provided for forward-looking statements under certain circumstances does not apply to the false and misleading statements alleged herein. Many of the statements pleaded herein were not specifically identified as "forward-looking statements" when made, and many were representations about the Company's present status and thus were not "forward-looking."

257. To the extent there were any forward-looking statements: (a) there were no meaningful cautionary statements identifying the important

then-present factors that could cause actual results to differ materially from those in the purportedly forward-looking statements; and (b) the particular speakers of such forward-looking statements knew that the particular statements were false or misleading, and/or the forward-looking statements were authorized and/or approved by an executive officer of Home Depot who knew that those statements were false and misleading when made.

258. Any purported warnings contained in the press releases and statements quoted herein were generic and unparticularized boilerplate statements of risks, and thus lacked meaningful cautionary language necessary to insulate the purportedly forward-looking statements.

### **FRAUD-ON-THE-MARKET**

259. In bringing these claims, Lead Plaintiff and all members of the Class are entitled to the presumption of reliance established by the fraud-on-the-market doctrine. At all times relevant to this Complaint, the markets for Home Depot's ordinary shares were highly efficient for the following reasons, among others:

- a. The Company's shares met the requirements for listing, and were listed and actively traded on the NYSE;

- b. As a regulated issuer, Home Depot filed periodic public reports with the SEC;
- c. Home Depot regularly communicated with public investors via established market communication mechanisms, including through regular disseminations of press releases on the national circuits of major newswire services and through other wide-ranging public disclosures, such as communications with the financial press and other similar reporting services;
- d. The market reacted to public information disseminated by Home Depot;
- e. Numerous securities analysts employed by major brokerage firms covered Home Depot and wrote reports which were distributed to the sales force and certain customers of their respective brokerage firms. Each of these reports was publicly available and entered the public marketplace;

- f. The material misrepresentations and omissions alleged herein would tend to induce a reasonable investor to misjudge the value of Home Depot securities; and
- g. Without knowledge of the misrepresented or omitted material facts, Lead Plaintiff and the other Class members purchased or otherwise acquired Home Depot securities between the time Defendants made the material misrepresentations and omissions and the time the fraudulent RTV scheme was being wound down, during which time the price of Home Depot securities was inflated by Defendants' misrepresentations and omissions.

260. As a result of the foregoing, the market for Home Depot's securities promptly digested current information regarding Home Depot from all publicly available sources and reflected such information in Home Depot's securities prices. Under these circumstances, all purchasers and acquirers of Home Depot's securities during the Class Period suffered similar injury through their purchase or acquisition of Home Depot's

securities at artificially inflated prices and therefore a presumption of reliance applies.

### **LOSS CAUSATION**

261. Throughout the Class Period, the price of the Company's stock was artificially inflated as a direct result of the fraudulent scheme alleged herein.

262. The Company's financial condition and results, including Home Depot's reliance upon improper RTVs to inflate the Company's income and operating margins, were material information to Lead Plaintiff and the other members of the Class. Had the truth been disclosed to the market during the Class Period, Lead Plaintiff and the other Class members would not have purchased Home Depot stock at all, or would have done so only at substantially lower prices than the artificially inflated prices which they actually paid.

263. The Company's failure to exceed analysts' expectations with regard to diluted earnings per share during the fourth quarter of fiscal 2004 (and the fact that revenue and EBIT growth fell short of historical levels) was not due to results from Home Depot's ordinary business operations. Rather, these facts were directly attributable to the Company's decision,

during that time period, to curtail the amount of improper RTV chargeback revenue.

264. Following the issuance of the Company's February 22, 2005 press release announcing Home Depot's financial results for the fourth quarter of fiscal 2004, the inflation that had been caused by Defendants' misrepresentations and omissions regarding vendor chargeback money and the RTV scheme was eliminated from the price of the Company's common stock, causing significant losses to Lead Plaintiff and the other Class members. Indeed, after the issuance of the above-referenced press release, the Company's share price declined precipitously. At the close of trading on February 18, 2005 (the last trading day prior to the issuance of the above-referenced press release), Home Depot's shares stood at \$42.02 per share. By the close of trading on April 28, 2005, Home Depot's shares were trading at \$35.09 per share, representing a decline of over 16% since February 18, 2005 and a loss of market capitalization of \$16.5 billion.

265. The decline in the Company's share price following the issuance of the February 22, 2005 press release, and the resulting losses suffered by Lead Plaintiff and the other members of the Class are directly attributable to the market's reaction to Home Depot's disclosure that it had

failed to exceed analysts' expectations with regard to diluted earnings per share during the fourth quarter of fiscal 2004 (and the fact that revenue and EBIT growth fell short of historical levels), and to the market's adjustment of the Company's stock price to reflect the foregoing facts.

266. Defendants' fraudulent conduct, as alleged herein, proximately caused foreseeable losses to Lead Plaintiff and the other members of the Class.

## **CAUSES OF ACTION**

### **COUNT I**

#### **Violations of Section 10(b) of the Exchange Act and Rule 10b-5 Promulgated Thereunder (Against all Defendants)**

267. Lead Plaintiff repeats and realleges each and every allegation above, as if fully set forth herein. This Count is brought pursuant to 10(b) of the Exchange Act, 15 U.S.C. § 78j(b), and Rule 10b-5 promulgated thereunder, 17 C.F.R. § 240.10b-5, on behalf of Lead Plaintiff and all members of the Class against all Defendants.

268. During the Class Period, Defendants carried out a plan, scheme and course of conduct which was intended to and, throughout the Class Period, did: (a) deceive the investing public, including Lead Plaintiff and other Class members, as alleged herein; (b) artificially inflate and

maintain the market price of Home Depot's securities; and (c) cause Lead Plaintiff and other members of the Class to purchase or otherwise acquire Home Depot's securities at artificially inflated prices. In furtherance of this unlawful scheme, plan and course of conduct, each of the Defendants took the actions set forth herein.

269. Defendants: (a) employed devices, schemes, and artifices to defraud; (b) made untrue statements of material fact and/or omitted to state material facts necessary to make the statements not misleading by use of means or instrumentalities of interstate commerce; and (c) engaged in acts, practices, and a course of business which operated as a fraud and deceit upon the purchasers and acquirers of the Company's securities in an effort to maintain artificially high market prices for Home Depot's securities in violation of Section 10(b) of the Exchange Act and Rule 10b-5.

270. As a result of their making and/or their substantial participation in the creation of affirmative statements and reports to the investing public, the Defendants had a duty to promptly disseminate truthful information that would be material to investors in compliance with the integrated disclosure provisions of the SEC as embodied in SEC Regulation S-K (17 C.F.R. § 229.10, *et seq.*) and other SEC regulations, including

accurate and truthful information with respect to the Company's operations and performance so that the market prices of the Company's publicly traded securities would be based on truthful, complete and accurate information. Defendants' material misrepresentations and omissions as set forth herein violated that duty.

271. Defendants engaged in the fraudulent activity described above knowingly and intentionally or in such a reckless manner as to constitute willful deceit and fraud upon Lead Plaintiff and the Class. Defendants knowingly caused their reports and statements to contain misstatements and omissions of material fact as alleged herein.

272. As a result of the Defendants' fraudulent activity, the market price of Home Depot's securities was artificially inflated during the Class Period.

273. In ignorance of the true financial condition of Home Depot, Lead Plaintiff and other members of the Class, relying on the integrity of the market and/or on the statements and reports of Home Depot containing the misleading information, purchased or otherwise acquired Home Depot securities at artificially inflated prices during the Class Period.

274. The market price of Home Depot's common stock declined materially upon the Defendants' decision to curtail and/or wind down the scheme, plan, and course of business which operated as a fraud and deceit upon the purchasers and acquirers of the Company's securities.

275. Lead Plaintiff and the Class members' losses were proximately caused by Defendants' active and primary participation in Home Depot's scheme to defraud the investing public by, among other things, falsifying the Company's financial results through fraudulent RTV practices. Lead Plaintiff and the members of the Class purchased Home Depot securities in reliance on the integrity of the market price of those securities, and Defendants manipulated the price of Home Depot securities through their misconduct as described above.

276. Furthermore, Defendants' misconduct proximately caused Plaintiff's and the Class' losses. Lead Plaintiff's and the Class' losses were a direct and foreseeable consequence of Defendants' failure to disclose and their concealment of, *inter alia*, the true state of the business operations and financial condition of Home Depot.

277. Throughout the Class Period, Defendants were aware of material non-public information concerning Home Depot's fraudulent

conduct, and willfully and knowingly concealed this adverse information regarding Home Depot's falsified income and operating margins. Lead Plaintiff's and the Class' losses were the foreseeable consequence of Defendants' concealment of this information.

278. As a direct and proximate cause of the Defendants' wrongful conduct, Lead Plaintiff and other members of the Class suffered damages in connection with their respective purchases and sales of Home Depot securities during the Class Period.

**COUNT II**  
**Violation of Section 20(a) of the Exchange Act**  
**(Against the Individual Defendants)**

279. Lead Plaintiff repeats and realleges each and every allegation contained above, as if fully set forth herein. This Count is brought on behalf of all members of the Class against the Individual Defendants pursuant to Section 20(a) of the Exchange Act, 15 U.S.C. § 78t(a).

280. For all the reasons set forth in Count One above, the Company is liable to Lead Plaintiff and the Class members who purchased Home Depot securities based on the materially false and misleading statements and omissions set forth above, pursuant to § 10(b) of the

Exchange Act, 15 U.S.C. § 78(j)(b), and Rule 10b-5, 17 C.F.R. § 240.10b-5, promulgated thereunder.

281. As alleged herein, the Individual Defendants acted as controlling persons of the Company within the meaning of Section 20(a) of the Exchange Act.

282. By virtue of their executive positions or Board membership positions, as alleged above, the Individual Defendants had the power to influence and control and did influence and control, directly or indirectly, the decision-making of the Company, including the content and dissemination of the various statements that Lead Plaintiff contends are false and misleading. The Individual Defendants were provided with or had unlimited access to copies of the Company's internal reports, press releases, public filings and other statements alleged by Lead Plaintiff to be misleading prior to and/or shortly after these statements were issued and had the ability to prevent the issuance of the statements or cause the statements to be corrected.

283. The Individual Defendants had direct involvement in the day-to-day operations of the Company and, therefore, are presumed to have

had the power to control or influence the particular transactions giving rise to the securities violations as alleged herein.

284. Defendants Nardelli and Tomé were the Company's senior executive officers who were responsible for reviewing the Company's annual, quarterly and periodic reports filed with the SEC and certifying that they fairly presented, in all material respects, the Company's financial conditions and operating results.

285. According to an article by Patricia Sellers titled "Home Depot Something to Prove," that appeared in *Fortune*, Bill Conaty, General Electric's human resources chief, said that, "With Bob, it's very, very difficult to have a surprise, because he's into the details down to the level of the shop floor." According to this article, Nardelli

is intensely hands-on [and] meets with his 21 direct reports every Monday at noon, zeroing in on KPIs (key performance indicators, such as customer counts and average tickets) and action plans. "I love data," he effuses. "I love to know what's going on in the company totally." Former executives say that the new environment is "command and control" and "all business all the time."

286. That Mercer is a controlling person within the meaning of Section 20(a) of the Exchange Act is evidenced by his position as Home

Depot's Executive Vice President of Store Operations, responsible for the day-to-day oversight of the Company's store operations. That Mercer authored the Mercer Memo that related directly to the RTV chargebacks is further evidence that he is a controlling person within the meaning of Section 20(a) of the Exchange Act.

287. That Langone is a controlling person within the meaning of Section 20(a) of the Exchange Act is demonstrated by virtue of his having co-founded Home Depot and his roll as "Lead Director" of the Company's Board of Directors and membership on the Board's "Audit Committee," "Executive Committee" and "Nominating and Corporate Governance Committee" during the Class Period.

288. Langone is also a controlling person by virtue of his substantial ownership of more than 17 million shares of Home Depot stock. Indeed, a June 2002 article in *Fortune* referred to Defendant Langone as "arguably the most powerful person at Home Depot."

289. That Defendants Cox and Clendenin are controlling persons within the meaning of Section 20(a) of the Exchange Act is evidenced by their having served as Chairman of Home Depot's Audit Committee at various times during the Class Period. As chairpersons of the Audit

Committee during part of the Class Period, Cox and Clendenin had the responsibility to, among other things, monitor the Company's financial reporting processes and internal control systems and review the Company's financial statements prior to their public dissemination.

290. As a direct and proximate result of the Individual Defendants' wrongful conduct, Lead Plaintiff and the other members of the Class suffered damages in connection with their purchase or acquisition of Home Depot securities during the Class Period.

#### **PRAYER FOR RELIEF**

WHEREFORE, Lead Plaintiff prays for relief and judgment, as follows:

- (a) Determining that this action is a proper class action;
- (b) Awarding compensatory damages in favor of Lead Plaintiff and the other class members against all Defendants, jointly and severally, for all damages sustained as a result of the Defendants' wrongdoing, in an amount to be proven at trial, including interest thereon;
- (c) Awarding Lead Plaintiff and the Class their reasonable costs and expenses incurred in this action, including counsel fees and expert fees; and

(d) Awarding such other and further relief as the Court may deem just and proper.

**JURY TRIAL DEMANDED**

Lead Plaintiff hereby demands a trial by jury on all claims set forth herein.

Dated: November 13, 2006

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**CERTIFICATE OF SERVICE**

I hereby certify that on November 13, 2006, I electronically filed the foregoing "Amended Class Action Complaint" with the Clerk of the Court using the CM/ECF system which will automatically send email notification of such filing to the following attorneys of record:

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I hereby certify that I have mailed by United States Postal Service the document to the following non-CM/ECF participants:

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This 13th day of November, 2006.

s/ Martin D. Chitwood  
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