

# Volkswagen Emissions Scandal: A Global Case Study of Legal, Ethical, and Practical Consequences and Recommendations for Sustainable Management

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## Abstract:

In today's global workplace, all executives and corporations must ensure that their managers and employees make ethical and sustainable decisions for their own long-term interest as well as those of the environment and consumers. Volkswagen (VW) has traditionally been known as a quality brand of automotive organization; but now they will also continue to be recognized as a global company that willfully and consciously manipulated their car's software to falsify data. They will be known as a company that deceived the U.S. government and the public regarding compliance with emission standards; however, they got caught and will pay a heavy price in managing this crisis. This willful scandal makes one think if government deception was considered normal and acceptable in VW's corporate culture and how such manipulation can be prevented in the future.

In this article, we provide the facts about the VW emissions crisis along with a discussion of the harmful consequences resulting from the scandal. Based on the lessons learned, the article offers recommendations for managers and employees of all local and global corporations in making ethical, transparent and sustainable decisions. Finally, a list of discussion questions are offered so managers and business students can reflect upon them for the creation of an organizational culture where effective and sustainable decisions become the norm.

**Key words:** Volkswagen, VW emissions scandal, VW automaker, car pollution, software and technology manipulation, Environmental Protection Agency, EPA and sustainability.

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## I. INTRODUCTION

Volkswagen (VW) until recently always has been regarded as a hardworking, efficient, effective, as well as honest and trustworthy company that made excellent products for the consumer. Yet in September of 2015 a scandal of major and dramatic proportions engulfed the German automaker based on the company fraudulently deceiving government regulators regarding compliance with pollution emission standards. How could so many laws be so blatantly violated? How could such a scandal happen? How could it have gone on for so long? Was deception considered acceptable in VW's corporate culture? How could a corporate culture devolve into one of tolerance for fraud, deception, and rule-breaking? Were there not moral leaders at the "top" who "stood their ground" and objected? Were there not any "whistleblowers" anywhere inside the company? Did a corporate culture based on wrongdoing emanate from the "top" or the "bottom"? Did the company take a narrow, short-term, perhaps jaundiced view of its own self-interest? Did the company abjure its moral responsibility to its stakeholders as well as to society and the environment as a whole? How could this happen? And what should be done about it? This article attempts to provide some balanced perspective to the VW emissions crisis; and then the article tries to examine the legal, ethical, and practical consequences resulting from the scandal, and finally offers some suggestions – specifically to VW on how to address the ramifications of this scandal – and generally to business managers on how to avoid such debilitating and harmful occurrences. Finally, since this article is formulated as a "case study" the authors have provided discussion questions at the end to stimulate analysis and discussion of the legal, ethical, socially responsible, and practical consequences of the scandal.

## II. BACKGROUND

In September of 2015 a scandal of major and dramatic proportions engulfed the German automaker, Volkswagen (Environmental Protection Agency, News Releases from Headquarters, 2016). On September 18, 2015, the U.S. Environmental Protection Agency (EPA) issued a Notice of Violation of the Clean Air Act alleging that the company in its model year 2009-2015 Volkswagen and Audi diesel cars had software designed to circumvent EPA emissions standards

for nitrogen oxides (Environmental Protection Agency, Volkswagen Violations, 2016). The software is defined in the Clean Air Act as a “defeat device” (Environmental Protection Agency, Volkswagen Violations, 2016). Then on November 2, 2015, the EPA issued a second notice of violation to VW including Porsche diesel vehicles as well as vehicles with larger engines than in the first notice (Environmental Protection Agency, Volkswagen Violations, 2016). And on January 4, 2016, the Department of Justice filed a complaint on behalf of the EPA against VW for alleged violations of the Clean Air Act (Environmental Protection Agency, Volkswagen Violations, 2016). The complaint, it must be noted, is a civil one; and as such the agency is asking for civil penalties and an injunction (Environmental Protection Agency, News Releases from Headquarters, 2016).

The essence of the scandal was that U.S. regulators accused the company of programming perhaps 11 million vehicles worldwide to falsely show on official tests that the vehicles were emitting lower levels of harmful emissions than they actually were when being driven on the roads (Environmental Protection Agency, News Releases from Headquarters, 2016). Regulators in the U.S. accused the company of cheating on environmental standards by programming engine management software in some diesel cars to detect when the vehicles were being tested by regulators and then to turn on emission controls only when being tested on treadmills by government authorities (Environmental Protection Agency, News Releases from Headquarters, 2016). Apparently, the cheat device is not actually a device but rather several lines of software code in the computer that controls the engine’s exhaust system (Lawrence, Elgin, and Silver, 2015). *Bloomberg Business Week* explains that “when the car detects a test – certain steering patterns; speed barometric pressure; only two wheels spinning instead of four – it switches to a cleaner mode called ‘dyno calibration,’ after the testing machines. The cars can run cleaner, but they can’t run cleaner without sacrificing fuel efficiency or some of the engine’s power” (Lawrence, Elgin, and Silver, 2015, pp. 52-53).

Consequently, the vehicles seemingly operated within emission control parameters; yet cars equipped with these devices would emit more than 40 times the emissions when back in normal driving conditions and actually running on the road (Bomey, 2015; Mouawa, 2015; Thompson and Kottasova, 2015). The software switches the engines to a more clean emissions mode while testing, but then after testing switches off again, thereby enabling the vehicle to drive more powerfully on the road, but by emitting as much as 40 times the legal pollution limits, particularly emitting nitrous oxide, a pollutant connected to lung ailments (Foxnews, 2015; Mouawad, 2015). U.S. government regulators called the programming software “defeat devices” (Environmental Protection Agency, News Releases from Headquarters, 2016; NBC News, 2015).

In essence, VW could not meet government emissions standards; and consequently someone, somewhere, and somehow in the company decided to cheat. Yet, as *Bloomberg Business Week* emphasizes: “Who exactly is responsible for devising and allowing the VW cheat remains a mystery” (Lawrence, Elgin, and Silver, 2015, p. 54). VW has always been known as a “company where engineers are in charge,” and the company initially blamed lower-level engineers for the cheat, yet, according to *Bloomberg Business Week*: “It’s not credible that top managers were unaware corners had been cut” (Lawrence, Elgin, and Silver, 2015, p. 53). Apparently, at some level or levels in VW “failure was not an option” and thus cheating and deception became the operational norm since the company could not scrap or delay its diesel plans. And regardless of pinpointing blame, the scandal and concomitant harm and loss of reputation to the company were, and still are, severe, and acutely so, since these cheating actions amounted to intentional deception and wrongdoing.

The company’s CEO at the time, Martin Winterkorn, who has since resigned, immediately apologized to VW’s customers, the public, and government authorities (Thompson and Kottasova, 2015). He said that the company had “broken the trust of our customers and the public” (Foxnews, 2015). A company spokesperson also said the company “does not tolerate any kind of violation of laws whatsoever” (FoxNews 2015). Winterkorn also said that “this type of manipulation must never happen again” at VW, but that “it would be wrong to place the hard and honest work of 600,000 people under general suspicion because of the grave mistakes of the few” (Moulson and Pylas (2), 2015, p. 2D). A company spokesperson said that the company was working “intensely” to eliminate the problem (Foxnews, 2015).

Michael Horn, the head of the Volkswagen brand in the U.S. also profusely apologized, and vowed that the company would win back the trust of the U.S. consumer (Bomey, 2015). He said that the scandal was not the result of any action or inaction by the company’s management, but rather was the scheme of “a couple of software engineers who put this together for whatever reasons” (Spector and Harder, 2015, p. B1; Lawrence, Elgin, and Silver, 2015, p.53). Mr. Horn also said that the company will withdraw applications for U.S. emissions certifications for its 2016 vehicles of Jetta, Golf, Passat, and Beetle. Now, thousands of these cars are stuck at U.S. ports until the matter is cleared up. Moreover, Horn said that the company will be recalling vehicles to adjust them so they comply with U.S. emissions standards, but the recall would not be completed until the end of 2016 at the earliest (Editorial, 2015). Michael Horn was always regarded as a good, honest, and frank leader who had the trust, confidence, and respect of the U.S. dealers (Stoll and Spector, 2016); but nevertheless on March 10, 2016 Horn resigned on mutually agreed upon terms (Stoll and Spector, 2016), “effective immediately,” to “pursue other opportunities” (Associated Press, 2016, p. 10A). A company spokesperson said his leadership in difficult times was appreciated (Stoll and Spector, 2016).

Soon after the scandal emerged, Mr. Winterkorn resigned, taking responsibility for what he initially termed “irregularities” in the company’s diesel engines, but he insisted he had done nothing wrong (Moulson and Pylas, 2015, p. 2D). Nonetheless, he said that the company needed a “fresh start” and that he was “clearing the way” for new management (Moulson and Pylas (3), 2015, p. 9A). Very soon after the resignation, VW’s board of directors appointed the head of its Porsche unit, Matthias Muller, who is a long-time company insider, as CEO (Moulson and Pylas (1), 2015, p. 3D). He promptly assured everyone that “it is decisive that nothing like this will ever happen again at Volkswagen” and that the “company will introduce even tougher compliance and governance standards” (Moulson and Pylas, 2015, p. 9A). Mr.

Mueller also accepted the resignation of VW's head of quality assurance (Boston, February 9, 2016). Furthermore, Mr. Muller "has attacked symbols of executive privilege," such as eliminating the corporate Airbus jet; and he also has an "open door" policy as opposed to his predecessor who forbid unannounced visits by company personnel, including his own staff, at the executive suite; and Mr. Muller is also hiring "outsiders" in order to "jump-start change," including new chiefs of strategy and digitization (Boston, 2016, p. B7). Thus, it appears that Mr. Muller is taking some steps to change the corporate culture.

Nonetheless, the company also set aside 6.5 billion euros, approximately \$7.4 billion, to cover the costs of expected recalls, fines, and lawsuits. The company has also stopped selling certain vehicles in the U.S. The result was a material drop in the company's profit for the year (Bomey, 2015; Thompson and Kottasova, 2015). The fines in the U.S. alone could be as high as \$18 billion, at \$37,500 per vehicle, as the Environmental Protection Agency (EPA) has the authority to fine up to that huge dollar amount based on the company violating emission standards for almost one-half million diesel cars in the U.S. (Bomey, 2015; Thompson and Kottasova, 2015). Moreover, in the U.S., the EPA and California regulators are now investigating diesel-powered vehicles from other auto manufacturers to see if they also used devices to cheat on emission tests (Boston, 2015).

The VW models affected so far are: the Jetta, Beetle, and Golf from 2009-2015, the Passat from 2014-2015, and the Audi A3 from 2009-2015 (Thompson and Kottasova, 2015). The *New York Times* (Mouawad, 2015) also reported that the Porsche model line might be affected. Purchasing an environmentally-friendly "clean diesel" car was a big part of the company's advertising campaign for the aforementioned vehicles (Bomey, 2015). The scandal thus may hurt the manufacturers and sellers of other diesel vehicles too. When the dishonesty came to light, VW's share price dropped a precipitous 34% in a matter of days, resulting in a loss of 25 billion euros (Foxnews, 2015). In addition to the negative publicity and financial losses, the scandal has engendered serious legal consequences in varying jurisdictions and pursuant to several types of laws.

### III. LEGAL CONSEQUENCES

The key statute applicable in the VW emissions scandal is, as noted, the U.S. Clean Air Act. Section 203 of the statute prohibits the manufacture, sale, or installation of any device that "intentionally circumvents EPA emission standards by bypassing, defeating, or rendering inoperative a required element of the vehicle's emissions control system" (Environmental Protection Agency, Volkswagen Violations, *Laws and Regulations related to Volkswagen Violations*, 2016). In addition to seeking civil fines as sanctions, the Clean Air Act also empowers the EPA to require a manufacturer to conduct a recall when a "substantial number" of vehicles do not conform to the agency's regulations (Environmental Protection Agency, Volkswagen Violations, *Laws and Regulations related to Volkswagen Violations*, 2016).

The U.S. government and some state governments, notably, California, apparently prompted by fears of "climate change," have established very strict emission standards for vehicles. Moreover, federal and California regulators began to adopt timelines to comply with the new regulations, which would, according to *Bloomberg Business Week*, "demand ingenious feats of engineering" (Lawrence, Elgin, and Silver, 2015, p. 53). *Bloomberg Business Week* also attempted to explain VW's possible rationale for the "defeat devices" going back to 2007:

VW liked diesel. A niche market in the U.S., diesels accounted for more than half the new-car registrations in the European Union that year. They were cheaper than hybrids and packed more muscle under the hood yet still got more than 40 miles to the gallon. VW, which aspired to surpass Toyota as the largest carmaker in the world, saw the U.S. as a growth market for a new diesel engine, one that could be branded as green. The trick would be to engineer a way to strip soot exhaust of its pollutants to meet the new U.S. rules (Lawrence, Elgin, and Silver, 2015, p. 53).

The "trick," however, was truly, and sadly, a devious one as it involved fraud and deception on a massive scale. As a result of the deception, as noted, in January of 2016, the U.S. government on behalf of the Environmental Protection Agency filed the civil suit against Volkswagen in U.S. District Court in Detroit, Michigan. The suit, emerging from the recent diesel emissions scandal, one of the biggest scandals in corporate auto history, or even generally for business, alleges that VW illegally installed software, called "defeat-devices," to make its diesel engines pass U.S. emissions standards, particularly strict ones in California set by the California Air Resources Board, during laboratory testing (Environmental Protection Agency, News Releases from Headquarters, 2016). The essence of the civil complaint is that the company obstructed efforts by the government to learn the truth about the excess emissions as well as making material omissions and providing misleading information (Environmental Protection Agency, News Releases from Headquarters, 2016; Viswanatha and Spector, 2016). The effect of the deceptive software was to boost the vehicles' performance, but also resulting in the emission of green-house gasses up to 40 times more than current U.S. environmental standards. The cheating software had been installed in VW diesel vehicles – cars and SUVs – sold since the 2009 model year, thereby potentially affecting 11 million vehicles (Environmental Protection Agency, News Releases from Headquarters, 2016).

The dollar figure for the civil penalties will be decided in federal court. However, pursuant to the Clean Air Act, as per the lawsuit, the company could be fined up to \$32,500 for each of the about 499,000 2-liter diesel vehicles in which it installed the software, and up to \$37,000 for each of the 85,000 3-liter vehicles in which VW installed the software. The result is a potential maximum penalty of more than \$19 billion (Davenport and Hakim, 2016). In the past, VW executives "pleaded ignorance" of the fraud and have blamed only a small number of lower level software developers and engineers for the creation and use of the computer software used to trick emission tests and regulators. The decision to defraud regulators was made about a decade ago when VW began a major effort to sell diesels in the United States. However, at the time, the company's technology was apparently inadequate for the vehicles to comply with the increasingly more stringent emissions standards, particularly in the U.S., to prevent smog-forming pollutants (Davenport and Hakim, 2016).

The *Wall Street Journal* quoted a products liability law school professor who said that the U.S. lawsuit was meant by the government to “send a signal to the auto industry generally, but to VW specifically, that this kind of behavior will not be tolerated” (Viswanatha and Spector, 2016, pp. B1-2).

Regarding criminal liability, there is also an ongoing criminal investigation in the U.S. by the Justice Department (NBC News, 2015). However, the *Wall Street Journal* (Harder and Viswanatha, 2015, p. B1) pointed out that prosecuting the company for environmental crimes could be problematic due to a loop-hole in the Clean Air Act of 1970 which eliminated criminal penalties; but prosecutors could still institute prosecutions for perjury, lying to government regulators, fraudulent concealment, and obstruction of justice, assuming evidence of such wrongdoing could be obtained. So far, as of the writing of this article, the U.S. government has not filed any criminal charges – either against the company or its executives. The current lawsuit is “merely” civil. However, there is the ongoing criminal probe by federal prosecutors in the United States (Viswanatha and Spector, 2016). Moreover, in Germany, there is a criminal investigation, but the *Wall Street Journal* (Harder and Viswanatha, 2015, p. B1) noted that “Germany’s criminal code does not provide much corporate liability.”

In the U.S., in addition to the federal regulatory actions, the owners of the supposedly “Clean Diesel” automobiles are filing lawsuits based on violations of federal and state consumer protection and anti-deception laws. Moreover, civil suits could be filed based on the common law torts of fraud and strict liability for defective products (Mujtaba, 2014; Cavico and Mujtaba, 2014). Individual consumers, the owners of the diesel vehicles, have paid up to \$6000 more for what they thought was a “green” diesel compared to a gasoline-fueled model. They thus are seeking compensation for their vehicles’ declining resale value (Viswanatha and Spector, 2016). Individual consumers were harmed by being deceived into buying what they thought were environmentally-friendly, socially responsible, and sustainable vehicles; and now consumers will confront declining resale values for their vehicles as well as a potential lessening of performance once the vehicles are fixed and thus are in true compliance with pollution limit standards. Moreover, VW dealers could sue the company for the fraud alleging lost sales and reduced market values of VW vehicles.

The U.S. has strict diesel emission standards; and, it is important to note, that California has even more strict pollution-control standards than the U.S. federal standards (NBC News, 2015). The California Air Resources Board, a division of the California Environmental Protection Agency, in September of 2015, notified VW that the company was in violation of state emission rules (California Environmental Protection Agency, 2016). As a result, VW was ordered to conduct a recall program and to correct a range of non-compliance issues, including, of course, the illegal defeat-devices. Penalties are still to be determined for the violations of California’s air quality regulations (California Environmental Protection Agency, 2016).

The *Wall Street Journal* (Boston, 2015, p. B7) also reported that a class action suit has been filed in federal court in California against VW accusing the company of fraudulent concealment, false advertising, and violating consumer rights laws. In particular, the lawsuit alleges that customers paid premium prices for VW and Audi cars powered by purportedly clean diesel engines on false promises of more horsepower and greater fuel efficiency, and, as a result of the company’s wrongful actions, the customers will suffer harm as a result of the investigations, legal proceedings against the company, and the recall of their cars (Boston, 2015, p. B7). The *Wall Street Journal* (Spector, 2015, p. B1, B4) also reported that the plaintiffs in the lawsuits are seeking compensation to off-set the higher prices they paid, at times exceeding \$60,000, for vehicles advertised as “clean diesel cars” with “impressive horsepower” as well as fuel economy (Spector, 2015, p. B4). In Kentucky, in March of 2016, the state’s attorney general sued VW contending that the company violated that state’s consumer protection law. The lawsuit seeks civil damages, which potentially could total millions of dollars, as well as restitution to the approximately 3800 vehicles registered in the state (Business Briefing, 2016). Moreover, in Florida, a woman in Palm Beach County filed a class-action lawsuit against VW and her car dealer, Auto Nation, which is the largest car dealership in the U.S., accusing the companies of fraud and deception pursuant to state law by deceiving her into buying what she thought was an environmentally-friendly “clean-diesel” vehicle. She is also suing for violations of RICO (Racketeer Influenced and Corrupt Organizations Act). The Chief Operating Office for Auto Nation denied all liability saying they had no knowledge of the fraud (Nehamas, 2015).

Several other civil suits have been filed by states in state courts in the U.S. alleging violations of environmental and consumer protection statutes. For example, civil actions seeking fines have been filed so far by state attorneys general in Texas, New Mexico, and West Virginia (Spector, February 8, 2016). In New Jersey, in February of 2016, the Acting Attorney General, John Hoffman, sued VW over the emissions scandal, contending the automaker violated state environmental and consumer protection statutes by selling more than 17,000 diesel-powered vehicles with software designed to deceive government pollution tests. The lawsuit was filed in state court and seeks financial penalties for the company’s violation of state pollution control limits (Spector, February 8, 2016). The government and consumer lawsuits – with potentially millions of dollars in fines, damages, and costs – are bad enough for VW; but the company’s damage to its reputation as an ethical, socially responsible, and environmentally sustainable company could be much worse.

Moreover, in March of 2016 the U.S. Federal Trade Commission (FTC) instituted a civil complaint against VW contending that the company engaged in false advertising for claiming that its vehicles were “environmentally friendly.” Some of the advertisements cited by the FTC included the statements: “Diesel: It’s no longer a dirty word,” “Green has never felt so right,” and “Clean as a whistle.” The FTC is seeking court orders to impose fines against the company as well as to require VW to compensate U.S. consumers who purchased or leased diesel vehicles between 2008 and 2015 (Randazzo, Sarah, 2016).



#### IV. ETHICAL CONSEQUENCES

The full impact of the scandal has yet to be seen as of the writing of this article; but it is safe to predict that the scandal will have a huge negative effect on the company's brand, image, sales, and "bottom-line." The German Economic Minister is concerned that the scandal could damage the "justifiably excellent reputation" of the German car industry (Boston, 2015, p. B7). The German Chancellor, Angela Merkel, said that the VW situation was "difficult," and she urged the automaker to show "complete transparency" and to explain its actions fully (Thompson and Kottasova, 2015). The German Environmental Minister called the case one of "blatant consumer deception and environmental damage" (Boston, 2015, p. B7). Moreover, it will be most interesting as well as "educational," to say the least, to see how the company tries to get back its good reputation and regain the trust of its customers, the public, and governments, as well as other stakeholders. Regaining one's reputation after it is lost is a difficult undertaking indeed. And one industry analyst and commentator, quoted in the *Wall Street Journal*, declared that this case is "really serious" and there is "no way to put an optimistic spin on this" (Boston, 2015, p. B7). The company's reputation for trust, as well as for making quality vehicles, was seriously damaged of course. And consequently the issue arises as to how the company can regain the trust of its customers as well as government regulators and how it can restore its damaged reputation (Cavico, Mujtaba, Nonet, Rimanoczy, and Samuel, 2015). Key questions to be answered during the investigations and lawsuits are who decided to install the deceptive software, what was their motivation, and did VW executives know, approve, or should they have known, of the fraud (Review & Outlook, 2015). How, who, and why could a corporate culture with a tolerance for rule-breaking have been created? And what are the company and its leadership going to do about changing the corporate culture to a more sustainable, legal and ethical one?

The ethical challenge for any business leader today is to make decisions and engage in actions that advance self-interest of the organization (Ethical Egoism), are culturally competent (Ethical Relativism), and achieve greater good (Utilitarianism) (that is, to strive for "win-win" scenarios for all stakeholders), but not to demean or disrespect any stakeholders (Kantian Ethics) in achieving personal or societal good (Cavico and Mujtaba, 2016; Mujtaba, 2014). The rationale for acting morally, the authors submit, is Ethical Egoism; that is it is in the long-term advancement of self-interest for the leader and his or her company to be rightfully perceived as not only a legal firm but also a moral one. Principled leaders who possess integrity and fulfill their moral responsibilities establish and lead firms that have good moral character and as a result their firms will do better financially in the long-term (Cavico, 2014). Yet VW, according to Drew Kodjak, the executive director of the International Council on Clean Transportation, plainly did not correctly calculate its own long-term self-interest. Mr. Kodjak stated, as reported in the *New York Times* (Mouawad, 2015, p.8), that "Volkswagen made a tremendous mistake in its corporate risk assessment, believing it could get away with this type of cheating and believing that the repercussions would be modest."

The role of a leader is to educate people as to their own true, long-term, self-interest; that is, the role of a leader is to "show the way" (to top management, board of directors, shareholders) that acting morally will benefit the organization and its stakeholders (Cavico and Mujtaba, 2016; Cavico, 2014). The role of a leader also encompasses objecting to, and inculcating his or her employees to object an action if it is illegal and immoral. That is, leaders must live and act by the "stand your ground" rule; disagree (strenuously if necessary yet trying not to be disagreeable); and have the strength of character, courage, and moral conviction to do the "right thing" and not do the "wrong thing" (Cavico and Mujtaba, 2016).

The role of the new leadership at Volkswagen, therefore, is to now create at an ethical organizational culture that fosters and supports moral behavior; to establish a personal and corporate/organizational reputation for integrity and trust, because, as VW is experiencing, once a reputation for trust is lost, it is very difficult to get it back. So, in the case of the VW emissions scandal, trust perhaps regained by total honesty, transparency, acceptance of responsibility, empathy for victims (that is, sympathy plus a true understanding of another's state or condition), identification of the harms caused, speedy adoption of remedial measures, promises of follow-through, and, most importantly, a heart-felt apology (Investing, 2015). Accordingly, the challenge and role for Matthias Muller, the new CEO for VW, is to change the past corporate culture of deceit, immorality, and a tolerance for rule-breaking to a culture of integrity, trust, honesty, and adherence to law and ethics. However, although several high-ranking company officials have been suspended and others have resigned, including the former CEO, the *New York Times* (Mouawad, 2015, p. 8) had a cautionary note about the new CEO, Mr. Mueller, saying there is skepticism about his ability to change the corporate culture because he was "Volkswagen head of product planning from 2007 to 2010, a period when many of the cars that caused the scandal were being developed." Nevertheless, Mr. Muller said that his "most urgent task" was to "win back the trust" for VW as an ethical company (Hotten, 2015, p. 3/14).

#### V. PRACTICAL CONSEQUENCES

By deceiving government regulators and consumers Volkswagen has caused a scandal of epic proportions encompassing detrimental environmental health consequences as well as the deception of government regulators and potentially millions of consumers. Volkswagen initially set aside approximately \$7.4 billion to cover the anticipated expenses of recalling the affected vehicles and fixing the illegal software, but according to the *New York Times* (Mouawad, 2015, p. 8) "the scandal could cost Volkswagen considerably more than that." Volkswagen is attempting to develop recall plans in conjunction with federal regulators in the U.S. for all the vehicles in order to remove the deceptive software and to make them compliant with federal pollution standards. Vehicle recalls commenced in Europe in January of 2016 (Spector, February 8, 2016). In Germany, the federal motor vehicle agency, known as the KBA, must approve any fix for each VW model affected; and once the KBA gives approval, the fix applies to vehicles across the European Union (Boston, January 29, 2016).

The company also has stopped the sale of the affected vehicles in the United States. So far, government regulators have not found similar defeat-devices on diesel models made by other automakers. As of the writing of this article the company was still trying to determine how to fix the affected vehicles in cooperation with U.S. government regulators. There has been a proposal to install a new catalytic converter in some U.S. diesel models, but U.S. regulators as of the writing of this article have not yet approved the plan (Boston, January 29, 2016).

The VW emissions scandal likely will have a lasting deleterious effect on other companies in the auto industry. Due to the suspicions and mistrust engendered by VW, other vehicle manufacturers will certainly be called into account for environmental compliance and thus additional testing. The whole auto industry will be examined much more closely now. The scandal will also have an especially harmful effect in Germany, where VW is a major manufacturer and exporter. VW, which also owns Audi and Porsche, is the world's largest automaker by vehicle sales (Thompson and Kottasova, 2015). The European Union is also now investigating VW vehicles sold in Europe; and there are separate country investigations in England, France, and Italy (Thompson and Kottasova, 2015); moreover, South Korea is investigating the company too (FoxNews, 2015). The scandal could also have a negative effect on other carmakers, especially Daimler, maker of Mercedes-Benz cars, which stock was down 6% after the scandal was revealed, and BMW, which stock fell 5.3% (FoxNews, 2015). Daimler immediately stated that it did not use any software to manipulate emissions tests (Boston, 2015).

VW is now assuring everyone that it is working hard with government regulators to ensure that its vehicles are fixed and properly meet U.S. emissions standards (Viswanatha and Spector, 2016). The company, in addition to telling its U.S. customers "to be patient," is also offering them a Goodwill Program including a "goodwill package" worth about \$1000 in the form of a gift card and free road-side assistance for three years (Boston, January 29, 2016, p. B5; Perez, 2016). Nevertheless, the damage to the company's finances and reputation could be enormous. The *New York Times* (Mouawad, 2015) reported on growing Congressional pressure in the U.S. on the company and cited a joint statement from "senior leaders" of the House Energy and Commerce Committee which statement asked: "Where does VW's road of deceit end?" And which also stated: "It's time for Volkswagen to fully come clean."

## VI. RECOMMENDATIONS

There is no simple and straightforward solution to this very, very bad emissions scandal. Nonetheless, the authors would recommend that Volkswagen managers do the following:

1. "Come clean," be fully transparent, accept responsibility as a company (and not merely blame lower-level engineers), apologize profusely, be humble, be sympathetic and empathetic; and provide sufficient redress to the injured parties.
2. Set forth in cooperation with government regulators a credible plan to fix the affected vehicles, truly reduce emissions, and verify compliance with pollution standards.
3. Offer a "buy-back" program wherein the company will buy back affected vehicles at a suitable price to get them out of circulation (this cost might actually be cheaper than the potential fines per vehicle and this would help to rebuild customer trust and loyalty).
4. Combine business profits with social responsibility and sustainability by making fuel-efficient and environmentally "friendly" vehicles.
5. Make a substantial and long-term commitment to research and development in the area of pollution emissions technology.
6. Develop technology that will reduce emissions yet still produce enhanced performance.
7. Advertise the company's commitment to and involvement in "sustainability" efforts, especially regarding "climate change"; and specify what the company's "best practices" will be to refurbish and enhance the company's environmental responsibility reputation and "green" image, particularly pertaining to reducing emissions while maintaining enhanced performance.
8. Establish a corporate culture of adherence to the law, ethics and integrity, social responsibility, and sustainability.
9. Establish stronger accountability structures, practices, and standards.
10. Establish a positive corporate culture by means of a commitment of the top leadership to integrity, the promulgation of Corporate Governance Policies, Codes of Ethics, Codes of Conduct, and communication thereof, as well as the relevant education and training of employees.
11. Communicate this new ethical value system and corporate culture to all its stakeholders as well as the communities and societies where the company does business.
12. Institute structures, practices, and channels to ensure legal and ethical compliance and the disclosure of any wrongdoing, as well as responsibility for redress and accountability for corporate actions, for example, in the form of Ethics Officers, ethics "hot-lines," ombudsmen, and other avenues and personnel for "whistleblowing" by employees.
13. Strongly tell and communicate in writing to employees that they have a legal and moral duty to report any wrongdoing on the part of the company or co-workers; assure employees that absolutely no reprisals will be

taken for “whistleblowing”; and state that requests for anonymity during the reporting process will be respected to the fullest extent possible (Cavico and Mujtaba, 2013).

14. Allow and encourage the employees to take a prudent amount of paid time-off to work in the community on social and environmental projects.
15. Ensure that the company itself is a “green” one; that is, engage in environmental conservation and protection; and thus show that the company is “reducing its carbon footprint.”
16. Also, the authors would suggest that the U.S. Congress should amend environmental laws to encompass criminal sanctions of companies and their personnel for intentional violation of environmental regulations.

The aforementioned recommendations for VW are good for society as a whole but they are also in the company's long-term self-interest; they will counter negative publicity and criticism; they will go a long-way to reestablish trust and confidence. These suggestions are designed to show that the company is doing everything possible to deal with the scandal and to do justice, to restore Volkswagen's reputation as a legal and ethical company, to regain the confidence of government regulators, customers, and other stakeholders, and to create positive momentum toward achieving a reputation as a company of integrity.

## SUMMARY

Volkswagen was a company that flagrantly disregarded the law by cheating government regulators and ultimately their own customers and dealers. In essence, the company by means of its deceptive practices stripped its customers and dealers of the freedom to make rational choices and decisions. These stakeholders and others felt betrayed as a result of the dishonest and fraudulent practices. VW, apparently, took the short-sighted, short-term, “easy-way out.” The company could not readily meet emissions standards so it devised ways to lie and to cheat. Consequently, the company's disrespect for the law and its own stakeholders engendered a scandal of epic proportions. The company is engulfed in a plethora of legal problems; its stellar reputation and brand have been severely tarnished.

Volkswagen obviously needs to work extremely hard to build the company's reputation back up to its former glory as an outstanding vehicle manufacturer that provides very good value to the consumer as well as a company that acts in a legal, moral and socially and environmentally responsible manner. Consumers who have purchased their products have lost trust in the company's brand. The company's reputation has been severely damaged. Volkswagen, therefore, should act strategically so the company can win back its customers; it must take a long-term perspective of achieving the organization's goals and its stakeholders' interest. Volkswagen made a start by the company taking responsibility for the wrongdoing when its leadership confessed to what they did and apologized profusely. Volkswagen has begun to make redress to consumers. The company will be punished civilly by government regulators and consumer lawsuits and perhaps criminally too. As such, now, Volkswagen needs to work hard to fix what they did wrong – practically and legally – and demonstrate that such deceptive conduct will never happen again. Specifically, the company must assure government regulators and consumers as well as its own dealers that its vehicles will now be equipped with emission exhaust systems that not only meet legal requirements but exceed the standards by using the best, state-of-the-art environmental technology. The company, therefore, must act in a legal, ethical, socially and environmentally responsible, and sustainable manner. Only then will Volkswagen be able to sustain itself, the communities where it does business, society as a whole, and the planet.

## DISCUSSION QUESTIONS

1. Discuss the legal issues involved in the Volkswagen (VW) emissions scandal, for example, under federal and state consumer protection and deceptive advertising statutes, the common law torts of fraud and strict liability for defective products, and the government's power to recall vehicles.
2. Did VW act morally pursuant to the ethical theories of Utilitarianism and Kantian ethics? Why or why not?
3. How should VW as an Ethically Egoistic company respond to this scandal?
4. What should VW as a socially responsible and sustainable company now be doing in the aftermath of this crisis?
5. How could VW's corporate culture devolve into a culture of tolerance for rule-breaking?
6. What can the company do to change the corporate culture to one of respect for the law and ethics?
7. How does a company go about “policing” its own corporate culture?
8. How does a company get its reputation back after such a major scandal and breach of trust?
9. Can Auto Nation or any other car dealership be held legally liable for the intentional fraud committed by VW? Why or why not?
10. Assuming that Auto Nation or any other car dealership can be held liable, is it moral to do so? Why or why not?
11. Discuss the legal issues involved in the U.S. v. Volkswagen lawsuit and how they should be resolved. What challenges would confront the government in bringing criminal charges against the company and its personnel? Also discuss the consumers' lawsuits against VW pursuant to the tort of fraud as well as products liability law.
12. How does a corporation such as VW reestablish a reputation for integrity after such a scandal and its concomitant lawsuits?

13. As a socially responsible and sustainable company, how should VW respond to this scandal? Provide examples of actions that will help the company restore its reputation.
14. What should other companies learn from VW's "mistakes"? What should managers and employees take away from the VW's scandal?
15. Is it ever possible to get one's "good reputation" back after a scandal of such major proportions? Why or why not?

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