



Volkswagen, A Cautionary Tale

By now, you are most likely aware that Volkswagen ran afoul with the United States Environmental Protection Agency (“EPA”) but what you may not know are the details that serve as a cautionary tale for U.S. companies.

In 2007, Martin Winterkorn took over as head of Volkswagen. An engineer by trade, Winterkorn had worked his way up through the organization and was known for his Machiavellian leadership and intolerance for bad news. Winterkorn laid out a plan for Volkswagen to become the world’s largest automaker through “the power of German engineering” which was not just a motto, but rather the belief and drive behind the way Volkswagen ran its business.

The key to fulfilling the goal of becoming the world’s largest automaker was by capturing the U.S. market. Specifically, Volkswagen planned to leverage German engineering to optimize fuel efficiency and emissions and to compete with the hybrid-electric car market. Volkswagen’s answer to this challenge: clean diesel. Clean diesel was viewed as a more powerful and lower cost alternative to hybrid vehicles with the promise of better fuel efficiency. The only hurdle was meeting the EPA’s strict standards for nitrogen oxide emissions.

Volkswagen engineers worked tirelessly to meet the emission standards but failed to do so without sacrificing the performance standards that were the hallmark of Volkswagen’s products. Caving to the pressures of an aggressive goal to become the world’s largest automaker, a profit motive and a domineering leader, Volkswagen engineers installed software designed to recognize when the vehicle was being tested to reduce the performance of the engine and pass the emissions test. Once the vehicle was out of the testing environment, the software then instructed the engine to perform at its highest levels and disregard the levels of nitrogen oxide emissions.

The software, referred to as a defeat device, worked and Volkswagen launched its clean diesel engines throughout the U.S. and sales followed suit. Clean diesel sales grew by 20% in 2010, 26% in 2011 and 25% in 2012. By 2014 sales had more than doubled 2009 sales.

In 2013, a nonprofit group focused on clean transportation took notice of the clean diesel Volkswagen engine and commissioned a study to determine why diesel technology in the United States appeared cleaner than in Europe. While performing tests on diesel engines from various automakers, it was discovered that Volkswagen’s on-road test couldn’t replicate the in-lab testing environment results. In 2014, the testing results were turned over to the EPA, marking the beginning of the end for Volkswagen’s clean diesel and with it, the ambitious goal of becoming the world’s largest automaker.

After the findings came to light, Volkswagen reluctantly admitted to the use of the defeat device and was forced to pay various fines totaling over \$20 billion.

How Could This Happen?

During the time of Winterkorn’s reign, Volkswagen employed many of the compliance program elements used by nearly every company focused on maintaining an effective compliance program. There was a 20-

member supervisory board responsible for corporate governance. The company had stated core values and a 25-page code of conduct, and it regularly conducted compliance training. But despite these compliance efforts the company still participated in a blatant scandal that resulted in record fines.

What We Can Learn from Volkswagen

- Recognize that every organization has the capacity to lie. Organizationally speaking this comes in the form of rationalization and minimization of lapses in ethics and compliance. Internally, Volkswagen characterized the defeat device as a “technical problem” and over time it was handled like any other technical problem rather than what it really was – a scheme used to blatantly defraud U.S. regulators.
- Understand that compliance and culture are interconnected and interdependent. Culture is “the way we do things” combined with the systems and processes in place to get things done. Compliance is acting or behaving within established guidelines. As a result, culture and compliance are integrated. Culture drives profitability, productivity, efficiency, effectiveness and compliance. Volkswagen overrode its compliance program by creating a culture that prioritized results over ethics and compliance. Compliance is not a department, it is the responsibility of every employee and it is the responsibility of leadership to foster a culture of compliance.
- Recognize that culture doesn’t have a finish line. Every meeting, email, conflict, celebration, promotion or departure impacts culture, and as a result culture is constantly changing. Culture can both mature and digress. Volkswagen’s culture eroded over time and was not subject to periodic evaluation like other systems and processes, throughout the company.

What You Can Do

Recognition of these factors is important, but responding to them appropriately is paramount. One way to respond is to include a culture audit as part of a regular compliance program assessment. As part of the risk assessment process, identify the values and principles that address the identified risks. Then determine if or how the values and principles are practiced across the organization and the programs in place to teach and reinforce them on a consistent basis.

Performing a culture audit can reveal valuable information that can assist organizations in mitigating compliance risks. Talk to your organization about its goal setting process and corporate strategy and if they are realistic. Do employees trust and respect who they report to and who reports to them? Questions about risk tolerance and decision making as well as budget and spending decisions can give insight into how aggressive an organization is. Questions about rewards and recognition, performance management, communications, the promotion process, people and leadership development and compensation can all give insight into the priorities of the organization and if they are misaligned with the mission and values of the organization.

Compliance is integrated into your organization’s culture. Are your values aligned with compliance priorities and are your organizational goals and strategies aligned with your values? For more information contact Patrick Braley by calling 770.396.2200.

The American Bar Association Criminal Justice Section sponsored the Fourth Annual Southeastern White Collar Crime Institute on September 7-8, 2017. The program featured a variety of panel discussions covering relevant legal and compliance topics. Bennett Thrasher was a sponsor and panel participant on Lessons Learned from Volkswagen: Corporate Culture, Ethics, and Loss Prevention in a Performance Era.