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PERSPECTIVE

# Time for some individual accountability

By Jonathan Michaels

In 2009, Volkswagen Group sat as the third-largest automaker in the world, trailing behind long-time leaders Toyota and General Motors in the heated race for automotive supremacy. The company had come a long way from its ominous beginning in 1937, when it created the "people's car" under the governmental control of the Third Reich.

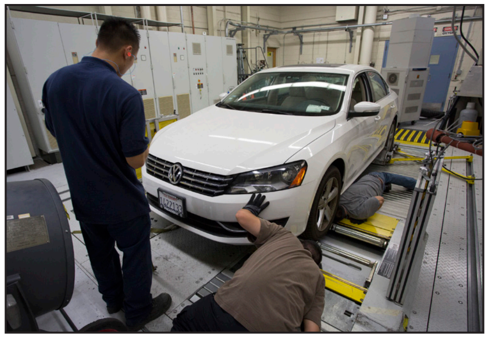
The fact that Volkswagen was even that large is a statement about the automotive industry itself. There once existed a time when the manufacturers themselves conceived and nurtured all of the automakers. General Motors, for instance, created Buick, Cadillac, Pontiac, GMC and Chevrolet in the early 1900s; and Ford likewise cultivated the Ford, Lincoln and Mercury brands over the ages.

But the 1990s saw a revolution of sorts, with automakers consolidating scores of smaller brands under larger controlling groups. Volkswagen officially became "Volkswagen Group," and since then has gone on to acquire Audi, Bentley, Bugatti, Lamborghini, Porsche and Ducati, as well as other non-US brands.

By 2009, Volkswagen was selling 6.3 million vehicles worldwide annually, and was on track to catch and eventually eclipse Toyota and GM. It was that year that Volkswagen made the decision to outfit its 2.0 liter TDI diesel cars with a complex software code that would enable vehicles to detect when they were being subjected to emissions testing.

Taking inputs from steering position and pedal movements, this "defeat device" detected when the car underwent emissions tests and manipulated the amount of nitrous oxide the vehicle emitted. In test mode, the vehicles were shown to be compliant; in real world driving conditions, however, the cars emitted as much as 40 times more pollutants.

The TDI diesel was Volkswagen's answer to the hybrid craze. Without significant inroads into the hybrid lineup, Volkswagen branded its diesel cars as "clean diesel" vehicles that were an attractive alterative to hybrid technology. From 2009 to 2015, Volkswagen sold some 500,000 Audi and Volkswagen branded vehicles in the U.S. that were pre-loaded with the emissions detecting software.



The New York Times

Technicians test a 2013 Volkswagen Passat for diesel emissions in El Monte last month.

This same software was embedded in another 10.5 million cars worldwide.

Volkswagen was successful in gaining substantial market share. By 2015, the company had succeeded in becoming the largest automaker in the world, boasting 600,000 employees, $270 billion in annual revenue, and sales of over 10 million new cars per year. The company that had given us common transportation and eternal free love was now the most powerful force in the automotive industry.

Volkswagen's decision to outfit its cars with test-defeating software has caused immeasurable harm to consumers and dealers alike. The automaker has issued a "stop order" to all U.S. dealers, precluding the sale of all new 2.0 TDI diesel vehicles, leaving dealers with the heavy burden of having to pay for the inventory finance charge on cars they cannot sell.

Consumers who now have cars that are not emissions compliant have it worse. Not only are the cars publicly seen as damaged goods, eliminating any legitimate resale value, but in the United Kingdom motorists are taxed on the amount of emissions their cars generate. So serious is the situation that the German Federal Motor Vehicle Office told Volkswagen that if it does not present the government with a "binding" plan of how the cars will be fixed by Wednesday, the government will bar the cars from operating on German highways.

Stateside, the scandal will cost the manufacturer greatly. Under the Clean Air Act, the U.S. government has the ability to fine Volkswagen $37,500 for each of the 500,000 noncompliant vehicles, or $18 billion. This is in addition to the actual costs of the repairs and a bevy of class actions alleging fraud. (Disclosure: My firm filed one such action.)

What is most disappointing about the situation is that Volkswagen officials felt comfortable enough to cheat in the first place. While our system does not necessarily encourage cheating, it does little to prevent it. In July, the Department of Transportation fined Chrysler $105 million for failing to inform the National Highway Traffic Safety Administration of safety defects and providing the agency with false information. In September, the DOT fined GM $900 million for concealing a deadly defect with its ignition switch for 13 years.

The fines against Chrysler and GM demonstrate everything that is wrong with the system. In both situations, vehicle defects led to tragic consumer deaths. And in both situations, the companies were allowed to rectify the situation by writing a check out of their massive profits, living free to cheat another day. No executives were jailed, and other than a few obligatory scapegoats, no careers were disrupted.

The situation with Volkswagen should be more of an expectation than a surprise. The expected fallout from the debacle will be a few billion dollars in fines and class action settlements, along with a few billion dollars to repair the vehicles. While these numbers are sizeable, they become less so when it is considered that the company recorded a profit of $12.3 billion over last year. Now consider that from 2009, when the scandal began, through the first half of 2015, Volkswagen generated $97.1 billion in profit. Even fines and recall costs of $10 billion are a mere 10 percent of the period's profit.

Until personal culpability becomes a part of the equation, we will never have a system free of deceit. The temptation to win at all costs is just too great, and the system gives the decision-makers all but complete immunity from severe forms of punishment — even though the harm they bring to others is life altering.

The Enron WorldCom financial scandals of the early 2000s resulted in the creation of the Sarbanes-Oxley Act of 2002. Under the act, senior executives take individual responsibility for the accuracy and completeness of corporate financial reports: Misstate a publicly reported financial statement, cause people to lose money, and you go to jail. Under the current automotive format, however, misstate the nature of your vehicle systems, cause people great harm including death, and face no personal responsibility.

To put a stop to the never-ending cycle of manufacturer abuse, we need to hold senior executives accountable for their stewardship over the massive companies they control. If prison terms, not percentages of profits, were a consequence of concealment and deceit, we would foster a culture where we would be surprised by the company that strayed into darkness. Right now, it is only a matter of time until we get the next public apology for having put the allure of profit above human life.

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