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Will the punishment fit VW's crime?

By Jonathan Michaels

By now, the world understands exactly how dastardly Volkswagen has been: It engineered a device whose sole purpose was to defeat emissions testing, and then outfitted 11 million diesel vehicles with the device, claiming that they had created the world's first "clean diesel."

In its quest to become the largest automotive manufacturer in the world, and without a competitive hybrid product in its lineup, Volkswagen unleashed its diesel vehicles on an unsuspecting public, accepting award after award for its revolutionary product. It is inconceivable that a company as large as Volkswagen would even try such a move — particularly given how regulated the industry is, and the likelihood of getting caught — but as a wise man once commented, the love of money is the root of all kinds of evil.

Now caught in a freefall of its own making, the question becomes how extensive will the carnage be, and whether regulators will finally administer a punishment that fits the crime?

The propensity to lie, cheat and steal is unfortunately nothing new to the automotive industry. General Motors proved this last year when it was revealed that it had been concealing a deadly ignition switch in millions of its vehicles for 13 years; and Chrysler eroded any remaining faith we had in the industry this past July when it admitted that it had been providing the National Highway Traffic Safety Administration with false and misleading information about defects in its vehicles for years.

The government's response to both scenarios was pitiful: GM was fined \$900 million and Chrysler was forced to hand over \$105 million, but not one managing officer was jailed or even charged with a crime, even though scores of consumers innocently — and unnecessarily — died. Instead, the companies purged their sins by writing checks from their massive stockpile of profits they derived from the very defective cars that were at issue.

Now the Department of Justice has an opportunity to restore the public's faith in our government's ability to control those it is charged with managing by handing down a real fine against the company that made \$97.1 billion in profits over the last six years, and jailing all U.S. nationals who were involved in the scam.



Workers leave after the morning shift at the Volkswagen factory in Wolfsburg, Germany, Oct. 4, 2015. VW is the Germany's largest company, employing some 600,000 people.

This, however, presents a dilemma of epic proportions that cannot be ignored: GM and Chrysler, two American born companies, were given extreme leniency for killing people, and now Volkswagen may get wholly shellacked for adding a little more pollution to the environment. No one should forget that Volkswagen has long stood as Germany's crown jewel.

While Germany is certainly upset about this episode — or at least embarrassed — recognize that Volkswagen is the country's largest company, employing some 600,000 people. Diplomatic relations with Germany have been good for years, but the country who served as our arch enemy a mere half-a-century ago may not view an uneven attack on its beloved manufacturer with complete acceptance. With Russian jets being shot down by terrorist missiles and bombs being detonated in Paris sporting arenas, the world's political environment isn't exactly stable, and unleashing a deserving attack on Volkswagen may cause our foreign relations to become a little more out of round.

Aside from the criminal and political implications, one has to wonder whether Volkswagen has the financial resources to survive the scandal. The Environmental Protection Agency has the ability to levy fines of up to \$37,500 per vehicle for Clean Air Act violations, exposing the company to as much as \$19 billion in fines. And that is in the U.S. alone, which only has 500,000 of the 11 million defective cars worldwide. If every country imposes the maximum fine, no company in the world could withstand such a front.

Then there is the matter of the cars themselves. It remains to be seen what the fix will be; whether it will be a mere software update, or whether it will be so invasive that buying back the cars is the only viable remedy. Whichever the case, it will either be expensive, or really expensive, and this assumes that the list of gamed cars does not continue to grow. Volkswagen has admitted to cheating on 11

million 2.0 liter diesel engines, but the EPA recently informed the automaker that it believes that the company's 3.0 liter diesel engines were part of the scam, too. Volkswagen has disputed this, but then again it disputed any wrongdoing with its 2.0 liter engines initially as well.

If it seems like that things could not get worse, consider that the European Investment Bank is deciding whether to recall \$5.2 billion in loans (of which \$2 billion is still outstanding) it made to Volkswagen for the development of lower emissions engines. The bank is reportedly seething, as it is required to fulfil certain climate targets with its loans, and now risks being out of compliance.

Volkswagen has substantial assets, but are they deep enough to cover all the implications of what is at hand? The company's 2014 annual report reflects a net equity position of \$95.6 billion, which includes cash of \$20.3 billion. Volkswagen has set aside \$7.3 billion to cover the scandal, but informed thinkers believe that this is not nearly enough. Credit Suisse, the Zurich-based financial service holding company, has predicted a best-case-scenario for Volkswagen of \$26 billion, and a worst-case-scenario of \$86 billion. It is no surprise then that earlier this month the company applied for short term loans of \$21.5 billion, and announced that it will be slashing \$12.8 billion in expenses next year.

If the company survives — and it is still an *if* — it may have to shed a part of its 12-brand empire that it spent the last two decades building. This means that iconic brands such as Lamborghini, Ducati, Bugatti and Bentley, brands which are nice to have, but do not add to overall company profit, may soon be put on the block.

Of course the real losers in the equation are the consuming public and the stockholders of Volkswagen, neither of whom did anything to deserve any of this. While consumers have seen their cars devalued, investors have seen fortunes evaporate as Volkswagen stock has plummeted since the news of the scandal broke. In May, Volkswagen stock was trading on the Frankfurt exchange at \$250 a share, yielding a market cap of \$126 billion. Those same shares have now seen a low price of \$102, and a market cap of \$56 billion — a market loss for investors of \$70 billion.

In many ways, the more things change, the more they stay the same. The scandal is new, but the element of greed is not. History is replete with bad actors who have impaled themselves with mortal, financially driven wounds, exposing themselves to all kind of grief. Volkswagen now joins the long list of social outcasts who have proven, time and time again, that greed is an element of human nature that we will never escape.



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