



CENTER FOR CATHOLIC STUDIES

TO: WBC AND MICAH PARTICIPANTS
FROM: MONSIGNOR RICHARD M. LIDDY
SUBJECT: *THE VOLKSWAGEN CASE*
DATE: NOVEMBER, 2015

- Welcome and Self-Introductions
- Woodstock Business Conference Mission Statement
 - The mission of the Woodstock Business Conference is to establish and lead a national and international network of business men and women to explore their respective religious traditions in order to assist the individual executives:
 - To integrate faith, family and professional life,
 - To develop a corporate culture that is reflective of their religious faith and values and
 - To exercise a beneficial influence upon society at large
 - The conference, grounded in the Roman Catholic tradition, welcomes believers who are open to and respectful of one another's religious tradition. It is committed to the conviction that ethics and values grow out of one's religious heritage.
- **SCRIPTURE: Matthew 13: 24-30 The Weeds**
- He proposed to them another parable: “The reign of God may be likened to a man who sowed good seed in his field. While everyone was asleep, his enemy came and sowed weeds through his wheat, and then made off. When the crop began to mature and yield grain, the weeds made their appearance as well. The owner's slaves came to him and said, ‘Sir, did you not sow good seed in your field? Where are the weeds coming from?’ He answered, ‘I

see an enemy's hand in this.' His slaves said to him, 'Do you want us to go out and pull them up?' 'No,' he replied, 'pull up the weeds and you might take the wheat along with them. Let them grow together until harvest. First collect the weeds and bundle them up to burn, then gather the wheat into my barn.'"

- Quiet Reflection 5 minutes followed by sharing insights.

TOPIC: Volkswagen Suspends More Employees: Law Firm Urges Action

By [WILLIAM BOSTON](#)

BERLIN— [Volkswagen](#) AG has suspended a larger number of engineers than previously acknowledged, following a recommendation from the law firm conducting an internal investigation into the auto maker's emissions cheating scandal, according to a person familiar with the matter. Volkswagen last month commissioned Jones Day, a U.S.-based law firm with offices in Germany, to conduct a probe into how illegal software used to dupe emissions tests [in the U.S.](#) and Europe could have been installed on nearly 11 million vehicles.

Jones Day urged the suspension of anyone who could have been involved in the scam—from high-level decision makers to ordinary engineers—to prevent possible perpetrators from tampering with the investigation, the person said. "We had to suspend everyone from this area to get them out of the way of the process," this person said. "This is necessary for the investigation, but it's really hard for us because we are now missing their professional experience and knowledge."

Many of the [Volkswagen employees](#) who have been suspended are likely to be found innocent of any wrongdoing and return to their jobs, the person said. The person added that this is why, in addition to rules of confidentiality, that the company is reluctant to publish the names of any suspects or suspended employees.

The suspended employees range from board-level executives at some Volkswagen units to low-level technicians, the person said.

Jones Day declined to comment.

U.S. environmental authorities disclosed the scam on Sept. 18, which led to the resignation the following week of Chief Executive [Martin Winterkorn](#). Winterkorn hasn't been charged with wrongdoing and has denied any knowledge of the affair.

Volkswagen admitted last month that some employees installed a so-called defeat device on the EA 189 diesel engine, which is used in cars and light trucks of several of its brands including VW, [Audi](#), Skoda and SEAT.

The device, described by experts as a few lines of computer code, allowed Volkswagen cars to emit less nitrogen oxide in laboratory tests than in normal road use. After the scandal's disclosure, Volkswagen confirmed that it commissioned Jones Day to conduct an investigation and that several senior executives had been temporarily suspended pending the probe's outcome. These included Ulrich Hackenberg, board member in charge of technical development at Audi AG; Wolfgang Hatz, a board member of Porsche AG and head of Volkswagen group

engine development; and Heinz-Jakob Neusser, a board member of the Volkswagen brand in charge of development.

Messrs. Hatz and Neusser declined to comment. Mr. Hackenberg hasn't responded to efforts to reach him. Other executives lower down the chain of command have also been suspended, according to people familiar with the matter.

Germany's weekly ***Bild am Sonntag*** newspaper reported Sunday that Volkswagen has suspended Hanno Jelden, head of Powertrain Electronics in connection with the emissions scandal. Mr. Jelden is quoted in *Bild* as refusing to comment. He didn't respond to Wall Street Journal requests for comment by email or voice messages.

A person familiar with the matter said Mr. Jelden had worked previously in exhaust treatment and wasn't involved in software applications. He said Mr. Jelden was suspended as part of the wide net cast in the wake of Jones Day's investigation.

In addition to Volkswagen's investigation, the U.S. Justice Department and German prosecutors are conducting separate criminal probes of still-unidentified people on suspicion of fraud in connection with the emissions cheating scam. Prosecutors in Braunschweig, Germany, have searched Volkswagen headquarters in Wolfsburg as well as private homes of unidentified employees.

No one has been charged with wrongdoing in connection with the emissions scandal and prosecutors say the investigation could take months before any charges are filed.

VW scandal another case of business as usual

Posted: Wednesday, September 30, 2015, 1:08 AM

By David Steingard

What does Volkswagen's emissions cheating scandal have in common with Enron's accounting fraud, the BP Deepwater Horizon oil spill catastrophe, the global financial meltdown of 2008, Barclay's Libor rate rigging, and General Motors' ignition recall? Why do these colossal breakdowns of public trust in corporations continue to repeat themselves?

At the heart of these scandals is an unchallenged attitude of "business as usual" that privileges financial metrics of success over all else and assumes that maximizing shareholder returns is the *raison d'être* of a corporation.

In the case of VW, the desire to surpass Toyota as the world's largest and most profitable automaker has put enormous demands on its management to deliver results: More profit. More growth. More market dominance.

The emissions test fraud clearly exposes the expectation to produce results at any cost: Customer brand loyalty evaporates. Public confidence erodes. Government agencies pursue damages. Employees challenge their loyalties. The natural environment experiences more toxic emissions. And, ultimately, the

venerated shareholders suffer an initial 20 percent decline in the value of their investments, with more losses arguably to come.

What would drive VW to commit fraud on such a grand scale that every one of its valued stakeholders is harmed and betrayed?

In VW's efforts to game the emissions test, this episode represents yet another manifestation of "If you're not cheating, then you're not trying." We now shift from deflated footballs to deflated integrity, let down by a great brand that once offered us *Fahrvergnügen* - "ultimate driving pleasure."

Consumers will have issues of confidence not only in VW but also in other carmakers whose vehicles have passed the tests. The spillover of VW's selfish act may have effects on its peers and rivals, BMW, Mercedes, and others. In fact, Caterpillar and Cummins settled similar accusations in October 1998 for \$1 billion. How did they pass the test?

As other corporate scandals have shown, the pursuit of profits without principles ultimately destroys profit itself - and sometimes the corporation as well. To avoid business ethics breakdowns of this magnitude, this misdirected mind-set of profits over principles must change. Companies need to reconnect with the true corporate purpose their legal charters demand - to serve society, sustain the natural environment, and foster well-being for all their stakeholders. Its time for "business as unusual."

David Steingard is an associate professor of leadership, ethics, and organizational sustainability and the acting director of the Pedro Arrupe Center for Business Ethics at St. Joseph's University in Philadelphia. steingard@sju.edu

Earnings Misstatements Come in Bunches, Study Says

OCT. 23, 2015

By GRETCHEN MORGENSON

One bad apple, they say, can spoil the bunch. That's the conclusion of a fascinating academic [study](#) that examined accounting restatements by thousands of corporations over a 12-year period. After one company was found to have misstated its earnings, the study determined, others in its industry often followed suit and began massaging their own numbers, ultimately resulting in their own restatements...

Equally intriguing were the exceptions. When companies playing accounting charades faced regulatory action, shareholder litigation or prominent news reports about their practices, the researchers found that their corporate peers declined to mimic their conduct. This shows the importance of highlighting and punishing bad behavior.

Three academics conducted the study, which will appear in the November issue of *The Accounting Review*, published by the American Accounting Association. They are [Simi Kedia](#) of Rutgers University Business School, [Kevin Koh](#) of Nanyang Business School in Singapore and [Shivaram Rajgopal](#) of Columbia University Business School.

The study, “Evidence on Contagion in Earnings Management,” looked at the restatements of 2,249 companies from 1997 through 2008. It found that earnings manipulation at companies was strongly related to the percentage of firms in the same industry or the same region that had announced restatements in the previous 12 months.

The study did not identify specific companies. But when bigger and more visible companies did the book-cooking, it found that the misconduct was more likely to be copied. The extent of a company’s initial restatement also had a bearing on whether it would be mimicked. Extreme restatements involving significant manipulation apparently were viewed as too risky to be imitated, the study found.

It turns out that copycats abound in corporate America. Companies emulated their peers with remarkable precision, the study found. Follow-on misstatements often occurred in the same corporate accounts that the initial case involved, like revenue manipulation, expense account fudging and massaging of inventory, assets or restructuring accounts.

“In a sense, restatements serve as handbooks of trickery,” Mr. Rajgopal said. Of course, companies in troubled industries might cook their books because of financial or operational challenges, not in response to peers’ earnings reporting practices. Recognizing this, the academics eliminated cases of what they called “contemporaneous adoption” from their study. That way, they could be confident their results pointed clearly to companies engaging in copycat earnings manipulation.

To some degree, Mr. Rajgopal said, the study confirms other behavioral research showing the contagious effects of leaving bad behavior unchecked. “I’m a big believer in this notion of contagion because I come from India, where littering is a huge example,” he said in an interview. “Everyone litters because everyone else litters. People don’t know what is acceptable, and they look to authorities for what would be reasonable social norms of what you can get away with.” On the issue of deterrence, the study showed a significant reduction in copycat earnings manipulations immediately after the passage of the Sarbanes-Oxley law in 2002. That [legislation](#), enacted after the accounting scandals at Enron,

Tyco and Worldcom, required top executives to take responsibility for the integrity of their financial statements. The law also gave the Securities and Exchange Commission the right to recover compensation improperly earned by executives as a result of misleading earnings statements and increased the criminal penalties associated with white-collar crime. For the three years after Sarbanes-Oxley went into effect, contagion in earnings misstatements disappeared, the academics found. But memories are short. The study provided evidence that the copycat behavior resumed in 2005 and continued through 2008, when the research concluded.

Class-action lawsuits and news reports critical of manipulative conduct reduce the likelihood that other companies will mimic the behavior, the study found. By contrast, restatements disclosed in a news release that receives little attention tend to encourage others to follow suit.

“One of the biggest problems in this research is that we can’t observe people who get away with this” and never disclose misconduct, Mr. Rajgopal said. “If Firm A is subject to an S.E.C. action or class action or if the press shows them in a bad light, this behavior goes down. You see less of this contagion if one of these things happens.”

The academics say their study is unusual in its documentation of the deterrent effects of policing by the S.E.C. and class-action lawsuits. Mr. Rajgopal said that he and his colleagues believed that their research could help the S.E.C. “By definition, deterrence is far more important than enforcement,” he said in the interview. “The S.E.C. has limited policing dollars: It can go after 60 or 90 criminals, but the more important issue is to stop the thousands of others.”

The same goes for the Justice Department, whose [pursuit](#) of criminal wrongdoers in the mortgage crisis was so undistinguished.

On Thursday, the [S.E.C.](#) said it brought a record 507 independent actions for violations of the federal securities laws in fiscal 2015, which ended in September. Of those, 134 were in the financial reporting and audit area, up from 96 such actions brought in 2014.

That is all to the good. But what this study hammers home is this: Accountability counts. Whether it comes from a regulator, a shareholder lawsuit or a journalistic enterprise, our capital markets and our investors need more of it, not less.

Questions for Reflection

Be Attentive: As you read all three articles what conditions exist to create these situations? Have you experienced similar conditions in your work life? Is anyone a VW owner? How have you reacted?

Be Intelligent: As we think about these situations they have both an individual impact and a systems or culture impact. They also have consequences. As the two cases unfold, it is easy to sit in judgment but there has been a process with multiple implications for stakeholders, describe the impact for various stakeholders, employees, management, boards, industry, consumers, government, etc.

Be Reasonable: How do you see values at play and in conflict in these situations. If you have encountered similar circumstances how have you reacted, acted or coped with the situation?

Be Responsible: How will the conversation this morning affect your work day? What will you carry with you? How do you exercise vigilance in your life? Are you able to have difficult conversations? What is the role of suffering and how does justice work?

John J. Fontana: Woodstock Business Conference
At Le Moyne College
847.703.5836