

GREENWASH AND ASK FOR FORGIVENESS LATER: A CASE STUDY

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INSTRUCTORS' NOTES

CASE DESCRIPTION

On September 18, 2015, the U.S. Environmental Protection Agency (EPA) made a shocking announcement that some of Volkswagen's TDI diesel vehicles had a "defeat device" that allowed the nitrogen oxide (NOx) engine output to meet U.S. emissions standards during testing while the vehicle was emitting up to 40 times the permitted level in true driving conditions. The sophisticated scheme, also known as "Dieselgate," started with approximately 500,000 cars in the U.S., but the total of affected vehicles climbed sharply to nearly 11 million worldwide within days. The irony was that while Volkswagen was boasting about its eco-friendly, green image, its engineers were rigging millions of its theoretically clean diesel engines with software that tricked emissions tests.

This case is an excellent vehicle for demonstrating how greenwashing and deceptive advertising exist in today's world. The case highlights the significance of business ethics and corporate governance and could be used in an undergraduate green marketing or business ethics course. The case is designed to be taught in a 60–75-minute class and is expected to require 3 hours of outside preparation by students.

CASE SYNOPSIS

Volkswagen entered the U.S. market in 1955, but it wasn't until almost half a century later that the German automaker found its niche in the U.S. diesel engine (which uses diesel fuel) category. VW adored diesel. It accounted for half the new cars sold in Europe, triggered by lax EU regulations. Diesel vehicles were cheaper than hybrids and packed more power under the hood yet still garnered more than 40 miles to the gallon. The U.S. market was a different game with more strict environmental standards. Thus the trick came down to how to engineer a mechanism to strip soot exhaust of its pollutants to meet the tough U.S. regulations. Situations in which there is a significant gap between the expressed and genuine commitments to sustainability, like Volkswagen's, is known as greenwashing - The greenwashing was certainly elaborate as it involved fraud and deception on a wide scale. VW spared no effort to mislead millions of unsuspecting customers in an attempt to position itself as one of the world's greenest carmakers. But it backfired! The company found itself in a plethora of legal nightmares, and its impeccable reputation and brands were severely tarnished. The scandal plunged the German

auto giant into the deepest crisis of its history, costing \$30 billion in fines, recalls, buybacks, and class-action lawsuits. VW's revenues, profits, and market capitalization tanked for months. However, the new CEO, Matthias Müller, has managed to turn things around. Volkswagen bounced back and became the largest carmaker in the world with 9 million deliveries in 2021. The multi-brand company, which also produces 10 prominent brands like Audi, Lamborghini, and Porsche in addition to Volkswagen vehicles, has been more aggressively moving into electronic vehicle manufacturing lately, investing billions.

SUGGESTED TEACHING STRATEGY

The author typically starts the case discussion by asking students if they have heard this statement: “With great power comes great responsibility,” alternatively known as the “Peter Parker Principle.” Some students may recognize it is indeed a line from the Spider-Man 2002 movie. Playing the video clip usually triggers a conversation about the moral responsibility of MNCs to do the right thing and act in a way that is both legal and ethical. Depending on the scope and time of the class, the instructor can divide students into teams and assign each team icebreaker questions like: “How could such a scandal happen?” “How could so many laws be so blatantly violated?” “How could it have gone on for so long?” “Was greenwashing acceptable in VW’s corporate culture?” “How could a corporate culture evolve into one that crosses ethical lines?” Teams can also research other companies’ public relations fiascos to see how each crisis was handled. Sadly, there is no shortage of those: Boeing 737 MAX back-to-back plane crashes, BP Deepwater Horizon oil spill, CBS sexual harassment scandal, Chipotle food poisoning, Equifax data breach, Exxon Valdez ocean tanker, Facebook-Cambridge Analytica data scandal, Felicity Huffman and Lori Loughlin college admissions scandals, HP spying scandal, Johnson & Johnson baby powder recall, Lehman Brothers scandal, Luckin Coffee debacle, Martha Stewart’s insider trading affair, Monsanto’s GMO controversy, Nike sweatshops, Siemens bribery scandal, SpaceX rocket launch failure, Toyota accelerator scandal, and Wells Fargo accounts fraud. This case can be used in a class with a timeframe of 60 to 75 minutes (Table 1).

Table 1. Teaching Plan Based on a 75-Minute Session

Case Overview	10 minutes
Discussion of the greenwashing phenomenon	15 minutes
Evaluation of the effectiveness of government regulators	15 minutes
Discussion of the roots of VW “Dieselgate”	10 minutes
Debating how the scandal will transform VW in the next 10 years	20 minutes
Update on the case	5 minutes

SUGGESTED ANSWERS TO DISCUSSION QUESTIONS

1. What are some legal and ethical issues associated with the VW scandal?

In early 2014, researchers from the International Council on Clean Transportation (ICCT) conducted tests on diesel models of the Volkswagen Passat and Jetta to verify that the “clean

diesel” technology these cars were touting was in fact clean. ICCT also solicited help from researchers at the West Virginia University (WVU) Center for Alternative Fuels, Engines, and Emissions. Meanwhile, the California Air Resources Board (CARB) was conducting its own tests on VW diesel cars. The ICCT/WVU researchers road-tested their vehicles under real driving conditions, while CARB’s tests were performed in a lab. The results were baffling. VW vehicles tested in the lab conformed to the EPA standards, while the same models tested on the open road exceeded U.S. emissions standards by almost 40 times. Initially, Volkswagen adamantly denied any wrongdoing. In December 2014, Volkswagen issued a voluntary recall of about 500,000 vehicles in the United States, claiming a software glitch as the reason for the emissions discrepancy. ICCT and CARB continued testing the repaired vehicles but found no or little improvement when the cars were tested on the road. It wasn’t until September 2015 that Volkswagen, unable to explain the tests, implied that some diesel models might have been designed to provide inaccurate emissions test results that comply with the legal limit. On September 18, 2015, the EPA officially notified Volkswagen that its “clean diesel” vehicles were found to be in violation of the Clean Air Act. On September 23, 2015, CEO Martin Winterkorn released a statement maintaining that the diesel scheme was the brainchild of low-level engineers, not senior management. Nevertheless, he accepted responsibility for the crisis and resigned his position. Chairman of Porsche AG, Matthias Müller, succeeded him and vowed transparency in getting to the bottom of what really happened.

What followed was a Greek tragedy-level scandal. Volkswagen shocked the world and admitted that it had deliberately equipped its models of Turbocharged Direct Injection (TDI) diesel engines with a “defeat device” that was intended to trick elements of a vehicle’s emission control system during emissions testing. VW’s diesel cars were essentially programmed to sense when emissions were being tested and to turn on equipment that reduced the emissions. Then when driven on the road, the cars had better fuel economy and performance but produced as much as 40 times the legal amount of nitrogen oxide.

Initial reports suggested that approximately 500,000 Volkswagen diesel cars in the U.S. were equipped with the device. As the scandal continued to develop, the number of vehicles affected ballooned to almost 11 million vehicles across multiple VW brands worldwide. Table 1 breakdowns VW’s vehicles fitted with “defeat devices.” Some reporters have termed the scandal as “Dieselgate,” referring to the Watergate scandal that forced President Richard Nixon to resign in 1974. Even the German Chancellor, Angela Merkel, stepped in and described the VW predicament as “difficult,” and pressed the automaker to demonstrate “complete transparency” and to explain its actions fully.

Table 2: VW Vehicles with Deceptive Emissions Software (October 2015)

Brand	Number of Vehicles (Worldwide) in Millions
Audi	2.1
Seat	0.7
Skoda	1.2
Volkswagen	5.0
VW Commercial Vehicles	1.8

Source: [Statista](#) (2015)

On November 2, 2015, the EPA issued a second notice of violation to VW that included Audi diesel vehicles. As U.S. regulators accused the company of cheating on environmental standards, the Department of Justice filed a complaint on behalf of the EPA against VW for deliberate violations of the Clean Air Act, citing a sophisticated and orchestrated scheme to cheat diesel emissions tests. The 2016 complaint contended that Volkswagen had intentionally concealed the fact that the automaker was polluting 40 times above the legal limits. The affected vehicles included nearly 500,000 vehicles from model year 2009 through 2015 Volkswagen TDI diesel cars of Jettas, Passats, Golfs, and Beetles, as well as the TDI Audi A3.

2. Discuss why simply issuing an apology is not enough when handling a public relations crisis of the magnitude of “Dieselgate.”

The scandal hit the brand at its core—its authenticity—and negatively impacted the company’s image, sales, and bottom line. When VW admitted in September 2015 to cheating on U.S. air pollution tests for years, shares tanked, and the company lost 30% of its market value overnight. This led to Moody’s downgrading the automaker’s rating one notch. Obviously, the diesel scandal had a noticeable effect on Volkswagen AG’s customers’ loyalty and trust, leading to a crucial drop in sales and profits. In the United States, the company ceased selling the affected 2015 models, did not introduce its 2016 diesels, and extended its warranty to 6 years/72 miles bumper-to-bumper coverage on all other models. However, Volkswagen kept selling 2015 and 2016 diesels in Europe. The company also faced backlash from the millions of vehicle owners, and it was forced to recall or even buyback most of those vehicles. The fines in the U.S. alone were \$14.7 billion for violating emission standards for almost one-half million diesel cars. The fines, lawsuits, recalls, and buybacks for VW vehicles overall amounted to \$30 billion worldwide.

Diesel vehicles account for more than half of all vehicles sold in Europe mainly because of EU’s policies that have made diesel fuels cheaper than gasoline and because of less strict emissions standards for diesels than in the United States. Revelations that Volkswagen cars were not as environmentally friendly or green as its “clean diesel” advertising had pledged were more damaging to the company’s reputation in Europe than in any other part in the world. The United States, as the second-largest car market after China, is theoretically critical to Volkswagen’s prosperity. However, U.S. unit sales come in at just six percent, compared to 40 percent in Europe. Thus, mayhem in Europe is a far greater threat to Volkswagen’s future growth and profitability.

3. When faced with such an ethical crisis, how should companies like Volkswagen respond?

When Müller became the new CEO of Volkswagen AG in September 2015, he brought his unblemished reputation and proven track record that he had gained at Porsche. Suddenly he was in charge of re-establishing Volkswagen’s reputation for environmental friendliness and restoring the confidence of various stakeholder. On the first day of the job, he said, “My most urgent task is to win back trust for the Volkswagen Group—by leaving no stone unturned and with maximum transparency, as well as drawing the right conclusions from the current situation. Under my leadership, Volkswagen will do everything it can to develop and implement the most stringent compliance and governance standards in our industry. If we manage to achieve that, then the Volkswagen Group with its innovative strength, its strong brands, and above all its

competent and highly motivated team has the opportunity to emerge from this crisis stronger than before”.

Four years later, it is safe to say that Müller had delivered on his promise. Revenues, profits, stock price, and market capitalization had rebounded and surpassed the scandal plunge. In 2019, Volkswagen AG held a 9% market share in the \$3 trillion global auto industry. Meanwhile, Volkswagen has strived to put the fiasco behind it and restore its green reputation. In 2016, VW vowed to boost its electric vehicle production by 50% over the next decade, with electric engines in half of all Porsche sports cars by then too.

4. Can Volkswagen earn back customers' trust? How would you propose the company goes about it?

The German automaker is aiming to have VWs with fewer emissions (for real this time!) and sell 1 million electric cars annually by 2025. In 2018, Volkswagen announced a \$50 billion investment in electrification. The company is also planning to manufacture a fully electric SUV for the Chinese market starting in 2024, which is expected to compete directly with the Tesla Model X. And starting in 20225, Volkswagen will also build the ID.4 compact crossover in Tennessee, where it already assembles a number of VW conventional models. VW has invested \$800 million to expand its U.S. facility for the ID.4 electric vehicle production. The U.S. subsidiary has started taking orders for the concept car which has a price tag of approximately \$35,000 that is anticipated to satisfy value-conscious consumers with aspirations of owning an electric vehicle.

While there is still some amount of trust left with some consumers, VW will need to ensure that this trust is well deserved this time. Strong brands, like VW, can prove to be robust assets, and VW can capitalize on that to regain customer loyalty while being a green carmaker. The key is to continue to act in a legal, ethical, socially, and environmentally responsible, and sustainable manner. Only then will Volkswagen be able to sustain itself, benefiting the communities where it conducts business, the public, and the planet as a whole.

5. What strategies would you recommend to management for implementation to prevent these issues from reoccurring?

This is the \$30 billion question! Volkswagen (and other companies for that matter) must learn from this fiasco and put policies in place to prevent reoccurrence. The giant automaker should start with its corporate culture. A code of ethics must be published. For example, a written document stating ethical and unethical behavior must be part of a training program that ALL employees have to take. A zero-tolerance policy must be implemented against any employee who crosses the line. Transparency and open communication should be the norm. A hotline for anonymous whistle-blowers could be established. Ensuring anonymity and rewarding legitimate whistle-blowers will encourage various stakeholders to come forward and will deter unethical behavior. In other words, training, transparency, and not being tone-deaf to the writing on the wall is the way to go.