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# **Stakeholder Relationships in International Crisis:**

## **Focus on Volkswagen Emissions Scandal**

A thesis submitted to Zurich University of Applied Sciences  
School of Management and Law, Department of International Business  
in partial fulfilment of the requirements for the Degree of

**Master of Science in International Business**

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**For the Year:**

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## Abstract

This study aims to uncover, in-depth, the stakeholder relationship in the international crisis of a well-publicized case involving a multinational corporation. For the purpose of the subject matter, relevancy, research objective, research question, and to limit the domain of research the Volkswagen emissions scandal that began in September 2015 and ended in May 2018, when its former CEO was indicted on federal charges of fraud in Michigan, USA, is the primary focus of this paper. The company suffered over \$30 billion in financial damages, as well unknown added cost due to value loss of automaker's brand equity, specifically to its reputation.

The paper examines in-depth the background information of the international scandal, identifies the multiple stakeholders involved, defines their roles, expectations, and strategies applied in the Volkswagen crisis. Furthermore, the research spurs deeper understanding, and creates new knowledge by providing corporate strategic management theories, as well as highlights alternative theory as a guideline to follow for international company vis-à-vis its stockholders, that might lead to corporate crisis avoidance, and build sustainable value maximization for the firm, while maintaining and maximizing superior stakeholder relationships.

**Keywords:** *stakeholder relationship, corporate crisis, Volkswagen emissions scandal, Dieselgate, international business*

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## List of Abbreviations

**VW** – Volkswagen

**CARB** - California Air Resources Board

**DAF** – Deutsche Arbeitsfront or German Labour Front

**EPA** – Environmental Protection Agency of United States

**DM** – Deutsche Mark or Germany's mark

€ – Euro

\$ – American Dollar

**AG** – Aktiengesellschaft or Group

**ICCT** – International Council on Clean Transportation

**CEO** – Chief Executive Officer

**CFO** – Chief financial Officer

**NGO** – Non-governmental organization

**NO<sub>x</sub>** – nitrogen oxides

**NO<sub>2</sub>** – nitrogen dioxide

**DAX** – Deutscher Aktienindex or Germany's Stock Exchange Index

**DSW** – Deutsche Stiftung Weltbevölkerung or German Investor Advocacy Group

**MSCI** – Morgan Stanley Capital International

**CSR** – Corporate Social Responsibility

**EVM** – Enlightened Value Maximization

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## 1. Research Background

### 1.1 Research Topic Significance

It is no industry secret that the stakeholder relationships in any organization has often represent the bulk of company's net value. Humans are social animals, by nature, meaning trustworthiness and goodwill play a huge role how we interact with each other. This truism extends into the marketplace. When it comes to international corporations, it is then imperative to study not only how those human relationships benefit the company, but also how to expand the pool of valuable stakeholders, maintain reputable relationships, and perfect those mutually beneficial ties with them over an extended period of time.

Inversely, it is just as important to study specific cases, and the underpinnings, where those stakeholder relationships were significantly diminished, hence tarnishing company's reputation in the collective eyes of great number of its stakeholders. Finally, the case study attempts to do just that, but also provide more theoretical underpinnings to corporate structure and strategies that potentially could lead to unsustainable practices that lead to decision-making that prove to be detrimental to company's long term financial well-being and loss of its market standing.

The study, then, steeped in relevance for international businesses, operating globally that might face challenges when trying to properly identify their pool of stakeholders, and how to assess on which subgroups of stakeholders the global firms must focus their attention and resources, in general, as well as the ranking of importance to the company's goals of sustainable growth and betterment of the stakeholder relationships. The case study is also timely, as many firms are now looking for internationalization strategies of expanding into other markets and cross-cultural boundaries. Although, the research concentrates on German corporate culture, corporate governance, and one company's specific and rather unique corporate structure, its findings have relevance to other industries and corporate structure and practices that are located elsewhere, since due to globalization there is been a greater push for global standards of doing business, as well as systemic, and empirically backed, stakeholder relationship approach.

The research found in this paper creates value for academics, as well. Since the science is not (nor ever) settled, when it comes to theoretical underpinnings behind corporate strategy towards maintaining and improving relationships between internationals and their vested stakeholders, as

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well as the data-backed approaches to corporate sustainability. The paper will provide some of the numerous competing theories and practices existing on the market of ideas, thereby requiring more discussion and research done towards creating a body of academic knowledge for currently operating, as well as future entrepreneurs and managers studying international or local business to guide them towards proper toolset and understanding of what to expect, and perhaps avoid, in the real world of commerce or working in any modern and complex organizational setting.

## **1.2 Significance of Focusing on Volkswagen's Scandal**

Henceforth, Volkswagen's emission crisis provides a real world example for closer examination. As it stands in 2018, Germany-based, Volkswagen Group is second biggest automaker in the world. It's a truly multinational organization with operations all over the globe. Comparatively to most other firms, it has higher level and scope of stakeholder interest, with both social and cultural aspects attached to it. When the still ongoing Volkswagen emissions scandal was made public in September 2015, and dominated the headlines years after that, many corporate management experts, industry insiders, and laymen alike, continue to be flabbergasted as to why an organization like VW went so far as to downright deceive their core stakeholders, such as customers and shareholders.

Prior to the scandal, they went out of their way to prove their "green" credentials, and explicitly announcing that they developed an environmentally friendly engine that is capable of reducing nitrogen oxide emissions to comply with strict U.S. pollution standards. The deception that was involved had not only put Volkswagen reputation at a stake, worldwide, as well as reputation of "made in Germany" brand, altogether. The reasons behind such decision and subsequent actions streaming from those decisions, therefore, worth careful exploration.

## **1.3 Formulation of Key Definitions**

Foremost, the key concepts further analyzed in the Volkswagen emissions scandal crisis stakeholder relationships case study must be properly defined. Stakeholder analysis is a technique widely used to identify and assess the importance of key people, groups of people, or institutions that may significantly influence the success of an activity, project, or business. In the context of what you are learning here, individuals or organizations will have an interest in international

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business if it affects them in some way - positively or negatively. (Management Sciences for Health , 1998)

Before venturing into further stakeholder analysis and specifics to Volkswagen emission crisis, some basic terminology must be defined. Though the term *crisis* might have many different meanings, in its origins the word is rooted in ancient Greek word 'krisis' referred to separation, a power of distinction, or placing judgement. (English Wiktionary, 2018) Today, generic crisis referred to decisive or crucial point, with negative connotations in terms of consequences. (English Wiktionary, 2018) According to Alben Björck, the term oftentimes used in exaggeratory manner to refer to any negative change in a daily routine with little consideration for that change's scope, severity, and its outcomes. (Björck, 2016)

Therefore, for this thesis and subject matter involved, and as per Björck's recommendation, the crisis, which will be described in depth, is broadly defined as "a major occurrence with a potentially negative outcome affecting an organization, company, or industry, as well as publics, services or good name. It interrupts normal business transactions and can sometimes threaten the existence of the organization." (Fearn-Banks, 1995)

Furthermore, Ian Mitroff and Murat Alpaslan team conducted in-depth study of typical corporate crises and broken them down to three types of crisis: natural accidents, normal accidents; abnormal crises. The latter is distinct from the other two due to the incident's deliberate nature, and usually denoted by perpetrator's intention to commit a crime (Mitroff & Alpaslan., 2003) Building on this work, the research team led by Peter Snyder suggested a more complex typology to best describe an organizational crisis using two dimensions: the first has to do with organizational distance to the crisis origin (internal/external); the second is based on frequency factor (normal/abnormal). (Snyder & al., 2006)

In the Volkswagen emissions crisis study, further in-depth analysis will bring attention to what Snyder's team deemed as "internal abnormal" crises. (Snyder & al., 2006) The journal article points out that these type of corporate crises originate from within the organization - internal crises present the biggest problem for any large scale organization due to fall in organizational

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reputation – and are relatively rare. Snyder’s working definition of internal/abnormal crisis specifically applicable in the case of Volkswagen’s emission crisis, also known as Dieselgate in popular culture, as “an extraordinary condition that is disruptive and damaging to the existing operational state of an organization.” (Snyder & al., 2006)

Furthermore, what does the term *stakeholders* entail? The stakeholder is an individual or organization who has a *stake* in an organization, and its interests might be affected as the consequence of what that company does. (Carpenter & al., 2010) From the company’s perspective, these stakeholders generally can be divided between internal and external stakeholders. Whereas the internal stakeholders typically include company owners or shareholders, management, employees, suppliers, retailers, and so on, so long as they work within the organization to some capacity (Savage & al., 1991), the external stakeholders are governments, NGOs, customers, and media outlets, and general public. This two-tier breakdown is rather unnuanced representation of stakeholders, and the paper further examines more detailed picture of stakeholder mapping, and how those two seemingly separate groups diverge and intertwine.

At first glance, there are two competing widely accepted theories to what the firm’s primary, if not sole, objective should be. In contrast to pursuit of value maximization for the company’s owners, the stakeholder theory to strategic management approach takes into account the interests of consumers, trade unions, government agencies, non-governmental organizations and activist groups, local communities, society as whole, media outlets, etc., all of which belong to the group of external stakeholders (Freeman R. E., 1984)

Moreover, according to authors of Corporate Valuation for Portfolio Investment, close to 80 percent of the total market value of Standards and Poor’s 500 companies comes from intangible assets, including reputation and relationship ties the company obtained with its stakeholders. (Lajoux & Monks, 2010) This points to irrefutable fact that there is some legitimacy to the popular of stakeholder theory. However, it falls short of telling the whole story. Therefore, the paper analyzes both theories closer, while also looks for alternative objective for the firms to pursue in order to achieve sustainable long-term growth, while possibly building and maintaining excellent stockholder relationships in the process.

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The fact remains, that in 21<sup>st</sup> century, highly competitive, and increasingly globalized business environment, each stakeholder relationship is then either an intangible asset for the businesses that must not only be cultivated, but maintained, so not to tarnish the firm's reputation that might negatively affect its bottom line and long term sustainability. Still, how is this related to automotive leader Volkswagen, and its recent scandalous emissions crisis?

Back in 2014, VW's carefully crafted published financial statements and public relations efforts, Volkswagens management seemed to acknowledge this truism about sustained long term success strategy, even prior to the emissions scandal unfolding: "Being aware of our stakeholders' needs and expectations is an important precondition for business success. Our aim is to understand and respond to stakeholders' expectations and promote appreciation of our positions and actions. In order to achieve this, we strive to continuously intensify the process of dialogue with our stakeholders" (Volkswagen AG Strategy , 2014)

The rest of the case study will focus on taking an in-depth look whether Volkswagen AG top management's actions towards its numerous stakeholders, worldwide, actually matched the its publicly stated vision and approach to stakeholder management. It will do so by presenting a condensed overview of the company's history prior to the scandal, as well as detailed description of the emissions crisis. The research objective and research questions put forth are then followed by findings derived through analysis of the literature review on the subject matter of the case.

### **1.4 Volkswagen's Background Before the Emissions Crisis**

Controversies and scandals around Volkswagen company go back to its original founding days in 1937 the company called *Gesellschaft zur Vorbereitung des Deutschen Volkswagens mbH*, which was put together by the German Labor Front (DAF), a national trade union, solely for Nazi party leader Adolf Hitler's idea of mass produced personal vehicle that's affordable for the average German folks (Volkswagen's literal English translation is *people's car*) (Rosenfeld & Jaskot, 2008 ). The first Volkswagen factory opened its doors in the small town of Lower Saxony, Wolfsburg in 1938, starting with production of now infamous Volkswagen *Beetle* model. (Allen-Mills, 2018)

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Beetle's production was heavily subsidized by DFA, it was also partially paid for via payroll deductions of the 340,000 car manufacturing workers, themselves for the promise to receive a car down the road. (Tooze, 2007 ) However, due to industry's war effort for envision of Poland, none of workers who participated in the scheme actually end up receiving the Beetle. (Tooze, 2007 )



*Figure 1: The Tatra 97 (left) and the VW Beetle (photo courtesy of thesamba.com)*

Reportedly, Adolf Hitler saw futuristic Czechoslovakian designs of Tatra models at produced in mid to late 1930's, especially T97 model, and said "This is the car for my roads" (Mantle, 1995). Though the official story behind the initiative involves Ferdinand Porsche receiving sketches of the Beetle design from Hitler himself, Tatra sued Porsche for infringement due to Beetle's close resemblance to Hans Ledwinka's work on Tatra engineering (rear mounted air cooled engine, backbone chassis and four-wheel independent suspension), which would've been settled, if it wasn't for Sudetenland occupation. (Ewing, 2017) The lawsuit was reinstated after the end of WWII, and only in 1967 Tatra finally received settlement from VW AG of 3 Million DM for proven infringements on its patents. (Ewing, 2017)

As the war was engulfing much of the world, just as in U.S., the Detroit's assembly lines were revamped for war effort, so too did Volkswagen's Wolfsburg factory. Shelving the mass production of Beetle plans for manufacturing of military use "Jeeps" (Kubelwagens), Fi103

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“flying bombs”, bazookas and other paraphernalia used in war time. (Kane, 2012) The controversial difference is that Volkswagen factory relied heavily involuntary laborers, and some 80% of its workforce came from concentration camps and/ or were prisoners of war. (Volkswagen AG, 2018) A stain on VW’s history and reputation that still haunts the company image to this day.

Still, after the WWII was finally over in 1945, Hitler’s dream became somewhat of reality, the VW Beetle became the most-manufactured car ever made, propelling Volkswagen’s brand to a symbol of mass produced affordable vehicle for working and middle-class Germans, as well as overseas. The manufacturer experienced fast paced internationalization in Europe and debuted in the U.S. market in 1949. (Lupa, 2008) The expansion into United States market strategy eventually led to establishing of Volkswagen of America in 1955 in New Jersey. (Lupa, 2008)

1960 was another crucial threshold year for Volkswagen, as it was previously jointly owned by West German federal government and Lower Saxony state government. That year marked the passing of Volkswagen Act by the federal government as the company was making concrete step towards full privatization. (Müller-Stewens & Stonig, 2015) The enacted law was a legislatively dubious resulting in corporate structure anomaly, but ultimately it was meant to act as a compromise between competing stakeholder interests - ensuring 60 percent partial privatization of ownership, while maintaining some public control over the company, by a way of legislating that the federal government and state of Lower Saxony, where the corporation still has its headquarters, each would retain some 20 percent of VW’s ownership with voting rights and four seats on its board of shareholders as people’s representatives. (Association of Corporate Counsel, 2014)

Since transition to a semi-private enterprise, VW had incredible growth and gained a reputation throughout the world as being a respectable brand that provides reliable “German engineering” quality product. In the United States, it was largely successful in spite of domestic Detroit’s booming car manufacturing empire, and was the third largest importer among foreign competitors. (Lupa, 2008) In part this was due to clever advertisers’ tactics to promote Beetle to a larger audience that had preference for big muscle cars, specifically “Think Small” campaign launched by American ad agency in 1959 (see figure 2). (Johnson, 2017)

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*Figure 2: 1959 Volkswagen Beetle Think Small Ad. Image courtesy of York Volkswagen*

It was also other external factors that further spurred its popularity. The unintended new subset of consumer base in U.S. as well as Europe that VW did not up to that point considered as viable target group was taking shape. The counterculture revolution and anti-war movement of the 1960s spurred off a subculture of hippies, who forgone the previous generation preference for white fence lifestyle in the suburbs and Cold War angst for communal and vagabond lifestyle of traveling the country, supposedly, practicing and spreading “peace and love” and social - environmental awareness. (Burnett, 2002)

They were searching for was a vehicle that would provide them with mobility in that search for themselves. The Volkswagen T2 model minibus proved to have the winning formula – it had easy on the eyes design, it lacked the extravagance of traditional American cars of the time, it was economically priced, durable, it had ample space, fuel efficient vehicle for new hippie generation and young people, in general, to experience the world. (Ebbert, 2017) As the director of the documentary on the subject called “The Bus”, called that multi-generational appeal of VW’s ‘hippie van’ model is that it “represents freedom”. (Lehman & Brooks, 2013)

### **1.5 Volkswagen’s Past Notable Scandals**

Throughout 80 plus years of Volkswagen’s corporate history, it accumulated many accomplishment, international expansion, and by yearly 1970’s certainly became a household name. However, as the saying goes, with great power comes great responsibility. While VW top management were basking in their recent market power position, it was constantly falling short on their responsibilities to many stakeholders the German automaker had to have reputable

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relationships with. Though the list of scandals and allegations are virtually bottomless, for the sake of paper's subject matter, it is valuable to the research to look at two particular company crisis, as they are related, and are prelude to the Dieselpgate.

Possibly, most notable of which, also unraveled the United State, involving one of its federal agencies with a mandate for protection of the national environment - EPA, a legislative power that resulted in enactment and various updates to Clean Air Act, which also covered the acceptable legal standards for emissions levels of new cars being sold in United States, EPA's press release and the report to Congress detailed its concerns of egregious violation, and investigation into VW's 1973 models. (Geuss, 2017) To dismay of EPA officials and many VW stakeholders, the agency's investigative efforts uncovered "failure to report the existence of and the use of possible defeat devices" by Volkswagen. (EPA , 1974)

Specifically, what the agency initially alleged, and then definitively proved through internal investigation, is that VW produced and sold 25,000 Type 3 models, pre-installed with temperature sensory switch technology that would send a deactivation signal to the emissions control system. Additionally, the infamous VW "hippie van" were found to have similar cheating technology. (Geuss, 2017)

That year of 1973, was the first encounter of such analog "defeat device" in automobile industry, which EPA described as mechanism that "reduces the effectiveness of the emission control system under conditions which may reasonably be expected to be encountered in normal vehicle operation and use", that the environmental agency's regulators, other lawmakers, and the general population in the United States have seen. (ICCT , 2016) Though VW was by far not the only automaker who used the illegal technique of skirting Clean Air rules, they were one of the first ones to get caught. Hit with a lawsuit, Volkswagen AG did not admit any wrongdoing on their part, but agreed to 120,000 dollar settlement, while their fleet of 1974 affected vehicles received a rejection to sell, as is, by the federal authorities. (Geuss, 2017)

More recently, in 2005 the car manufacturer found itself embroiled in one of Germany's biggest corruption scandals. The list of wrongdoings by VW included corruption, bribery, backdoor dealings, fraudulent use of shareholders' funds, and conflict of interests collision - a scandal that

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read like a thriller script rather than corporate government “how to” manual. The most notable part of the scandal involved high ranking HR managers, the head of VW’s works counsel (equivalent to a labor union), local politicians, with possible involvement of VW top executives on the board.

The top management were interested for major worker restructuring plans, while then acting head of VW’s labor union and the local politicians were almost sure to reject such a proposal if were to put forth during the board meeting. One particular scheme involved establishing company slush fund £500,000 to entertain Lower Saxony politicians and the union bosses in a compromising way, as a way to both incentivize and possibly blackmail the two parties into rubberstamping to the reforms the top management wanted to see enacted.

In the aftermath, the head of human resources resigned, confessed to the charges and even went to jail for it, along with other two managers. The head of the union received swift justice for his involvement. The disgraced politicians resigned from his position. KPMG’s issued an estimate that the scandal would cost Volkswagen’s shareholders five million euros, presumably this figure didn’t include the cost of diminished reputation in the eyes the stakeholders. Neither CEO nor the chairman of the supervisory board of VW AG, admitted to any knowledge of such backdoor dealings or wrongdoing, of any kind. The case did, however, shone some light on both cozy and toxic relationships between the company’s top management, labor representatives, and local legislators, as well as on the state of VW AG corporate culture, and how they operate in crisis mode.

## **1.6 Volkswagen Dieselgate Scandal In Depth**

Fast forward 50 years since its founding, the Volkswagen Group of America was embroiled in corporate-wide scandal and crisis resulting in largest settlement by any auto maker in United States history, and in parent company’s history since its highly controversial beginnings (Peltz & Masunaga, 2016). In 2015, Environmental Protection Agency (EPA) made allegations that VW violated its Clean Air Act of 1963 - enacted to control the air pollution - by developing and installing emission control system, also known as ‘defeat device’ in 2009–2015 models with 2.0 liter diesel engines (Majláth, 2016).

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Such devices are equipped with software that designed to both (1) detect when emissions tests are being run, as well as (2) activate pollution controls for sole purpose that the vehicle can meet desired air quality standards (see figure 3). While on the road the car's pollution controls are disabled to improve engine performance, as well as fuel economy (Majláth, 2016). However, the new changes result in higher emissions, such as nitrogen dioxides, which are toxic in high levels. EPA enacted test runs of VW vehicles in use being investigated by the agency, and found their emissions were anywhere from 10 to 40 times above its legal acceptable standards. (Mohan & Welsh, 2015)

Before turning into major international scandal, it was the environmental regulator in California - California Air Resources Board (CARB) - began to take note of a persistent problem in EU, where they saw discrepancies in the diesel emissions in the laboratory setting and on the road. Shortly, in 2013, International Council on Clean Transportation (ICCT, who provide scientific analysis to regulators) made a suggestion to put emissions of popular diesel vehicles sold in U.S. under the test with the assumption that they will emit relatively less emissions on the road due to Clean Air Act's tough regulations in place.

Out of three models chosen randomly, BMW's X5 indeed passed the test, however, Volkswagen's Jetta and Passat were found to have significant discrepancies. California environmental agencies were rightly concerned about, leading to regulators alerting federal EPA agency of the findings.

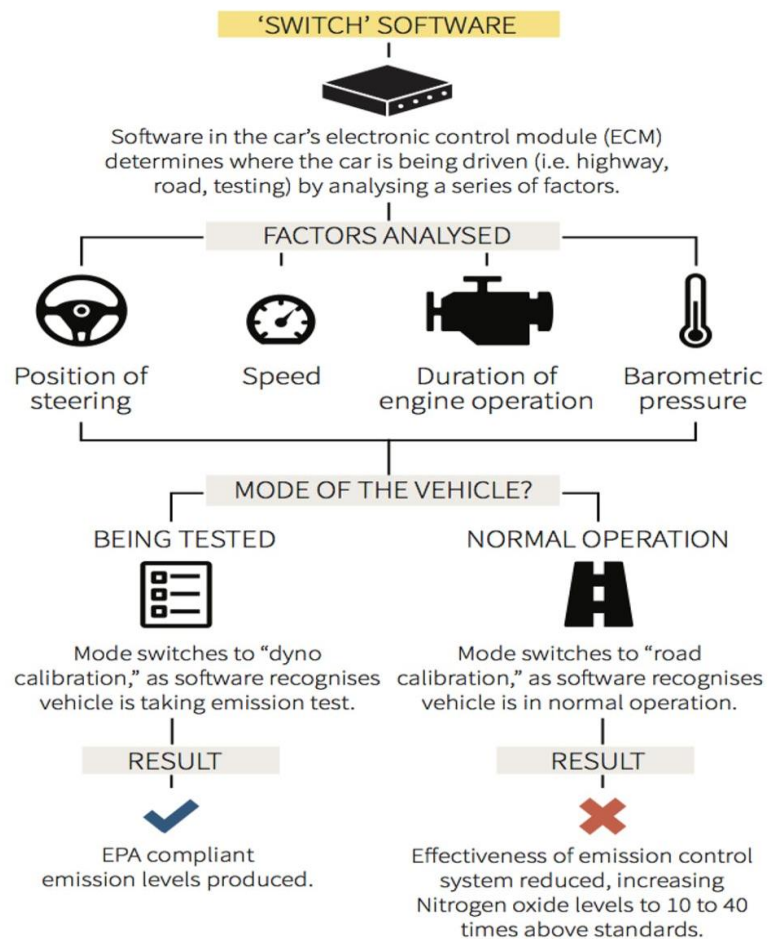
Consequently, EPA proceeded with their own internal investigation of all VW diesel passenger cars, and confirmed the fraudulent practice of using 'defeat-device' (see Figure 3), also called cheat software, that made possible for shutting down emissions mechanism specifically when those vehicles were in operation on the road, allowing the car to emit environmentally harmful gases beyond the regulatory agency's legal limits.

It took VW management whole seven months to respond to concerns and allegations made by CARB, for example. The company's top management failed to adequately address the state regulators' initial concerns and ICCT study findings, since they regarded the issues described in internal memos as "technical problem that did not differ from other everyday technical problems" (Reuters Staff, 2017)

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As a consequence to the criminal investigation and findings of the highly publicized scandal, the VW management had eventually admitted that a cheat software was in fact installed in 11 million cars, worldwide with type EA189 engines vehicles. (Ewing, 2015) After a meeting with prominent shareholders at the executive committee, on September 23rd 2015, Martin Winterkorn, who has been CEO of VW group since 2007, made an official statement of resignation - "As CEO, I accept responsibility for the irregularities that have been found in diesel engines". Mr. Winterkorn added to the statement that "I am not aware of any wrongdoing on my part". (Ewing, 2015)

## How Volkswagen's defeat device works



Source: U.S. Environmental Protection Agency  
J. Wang, 22/09/2015

REUTERS

Figure 3: Volkswagen's defeat device process. Illustration courtesy of Reuters

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Whether he was being truthful in that position is impossible for general public to know for sure, but there were many industry analysts, and opinion makers, who either disagreed or were, at least, skeptical of such presumption of innocence to wrongdoing due to ignorance of the issue. That statement did raise legitimate question as to why VW CEO had to resign if he had was not personally aware of the emission software manipulation, as he claimed.

The biggest shock in the wake of Winterkorn's admissions and resignation was just how widespread the deception was. For example, by the late September, in Germany, the minister of transportation made a statement indicating that practice of defeat device installed cars extended to Europe and beyond, and that all together 11 million VW diesel vehicles contained "cheat" software, worldwide. (Tidwell, 2017) Public's attention then refocused from VW legal troubles and ramifications in the United States and former CEO, to VW Group corporate governance, it's hierarchy, corporate structure and culture under which such brazen cheating can occur. Concretely, the public wanted clear answers to who had the knowledge of deceptive practices, and when they knew it, and what they plan to do about it. (Tidwell, 2017)

Some critics rightfully argued that VW was infamous for its top-down corporate organization, where even not very significant decisions require approval from the top executives from its headquarters in Germany. Hence, even minus direct culpability by Mr. Winterkorn, its 'command and control' structuring made it difficult for the top management to forgo personal responsibility. (Ewing, 2015) Various experts and critics of the company have long pointed out to what they saw as highly hierarchical corporate culture that did damage to company-wide internal communication and may acted as discouragement to midlevel managers, and lower level employees, from delivering the news the executive office didn't necessarily wanted to hear, but would have been of value to its other numerous stakeholders. (Ewing, 2015)

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## **2. Research Questions**

The research objective is to examine one of the most famous cases of international corporate crisis, that's both immediate and exemplary due to its scale of damage, and carefully identify the stakeholders involved and the effects of the crisis on each groups of stakeholders. Furthermore, the paper attempts to create new knowledge for corporations and international business academics by examining theoretical guidelines on how to avoid potential similar international crisis scenarios vis-à-vis creating and maintaining excellent relationships with stakeholders through pursuing shareholder value maximization.

The research paper puts forward a two research questions to meet the stated research object. (1) Who were the most relevant stakeholders in the real-life international corporate crisis - e.g. Volkswagen emission scandal? What were their expectations, motivations, roles, and strategies in such a crisis? (2) From theoretical and practical approaches, and from a perspective of an international corporation what is the corporate objective to follow in order to ensure sustainable value maximization? How such an objective could've either prevented Volkswagen's emissions scandal, or could help the repair of the reputation of the firm in the future?

## **3. Research Methodology**

This research uses an inductive approach (i.e. theory building) to reach its overarching objective of understanding how stakeholders deal with an international crisis. This inductive approach (compared to a theory-testing, deductive approach) has the advantage of showing in-depth information on the topic, and revealing concrete directions for future research.

### **3.1 Research design**

First, an in-depth case study will be carried out of what can be understood one of the largest, and highly complex international crises to date. This case was selected because of the high availability of information that is available online. This will enable extensive secondary qualitative data analysis. In a second step, the stakeholder relationship management will also be reviewed to derive some findings specifically applicable to a real-life example of international

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corporation crisis, followed by theories and specific recommendations on how that and other companies should approach stakeholder relationships management to achieve sustainable growth, whilst improving their stakeholder relationships, at the same time, since without the latter the firms oftentimes won't be able to achieve the former.

### **3.2 Data collection**

Since the research focuses on real life, as opposed to hypothetical, international crisis, as well as cause and effects of such crisis, the research methodology will rely heavily on literature review, secondary data, as well as qualitative research. The methodology further attempts to use most recent findings and guidelines of proper crisis management and prevention to account for rapidly changing business environment and more intercultural and globalized set of stakeholders.

The research turns to previously published research papers, articles, case studies, reports, governmental documents etc. to uncover all stakeholders of Volkswagen, and who were primary stakeholders who were most affected by Volkswagen emission scandal, and therefore require further research and analysis. It also examines strategic management theories, and backs up some of those theories with empirical data from literature review.

### **3.3 Verification and generalization of empirical data**

To provide high-quality scientific answers to the research questions, the issue of validity, reliability and generalization has to be addressed. Validity in case studies means to what extent the drawn conclusions correspond to the data, whereas reliability means the extent to which the results are replicable. Validity for the case study is drawn from sourcing scholarly papers, articles, reports, and publications related to the case within. Whilst replicability, though typically applies to primary research, is nevertheless recommended in this case as a matter of further research pertaining to subject matter. Finally, the issue of generalization will be addressed in the discussion section of the thesis, i.e. to what extent the results from the studied case can be extended to other cases, such as other international companies, and / or alternative industries, altogether.

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### **3.4 Research Limitations**

For the purpose of the study of stakeholder relationships in international corporate crisis, the paper limits to one specific corporate crisis in history, involving single multinational conglomerate. The case study's research is also limited to specific four types of stakeholders affected by company's actions, due to limited space and time of such research, but also due to the scope and impact such scandal had on those stakeholders. The rationale behind concentration is that the most affected parties require more and detailed attention.

## **4. Literature Review**

### **4.1 Stockholder Relationship Mapping And Management**

Anyone venturing towards even minimal understanding the stakeholder relationships management, be it for academic reasons or, especially, for the purposes of applying that knowledge in the real world situation of practical considerations, will quickly come to realization that most organizations will have numerous groups and subgroups of individuals and other organizations that in one form or another will have a direct or indirect stake in that organization, and therefore must be considered during decision-making process or when unperceived events are faced by the firm. When we discuss international organizations, especially on grand scale, such as Volkswagen AG, it should come to no surprise that we are referring to virtually limitless number of stakeholders involved that in one way or another might be affected by both company's operations and outcomes stemming from top managers' decision making – including those decisions involving fraudulent activities when it comes to emissions of the diesel vehicles that were sold all over the globe.

It's undeniable that from the generic firm's perspective, when they look at scope of all those stakeholders, especially more obvious, set of stakeholders have clear legitimate stake or interest in that corporate organization, such as investors, its customers, and competing firms. (Harris & Fleisher, 2005) However, from the perspective of highly complex, marked by cross-culture and cross-border trade and operations, which underlines the reality of contemporary business environment and modern day corporations, the not-so-obvious stakeholders also include, but

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certainly not limited to, different jurisdictions, government bodies, print, online and social media providers, activist groups with various agendas, future generations, local communities and societies at large. Lately, it's been even argued that firms increasingly should include and focus their efforts on "the environment" as an integral stakeholder, finding new business models or new approaches and technologies to operate and grow in environmentally sustainable fashion, and defying long terms practice of stakeholder management where only individuals, or groups of individuals were of sole consideration. (Harris & Fleisher, 2005)

Provided such complexity to stakeholder relationship vis-à-vis the international corporation, all this means that it is essential to firm's long term sustainability for its managers to develop a systematic approach to identifying those stakeholders, categorize them in more manageable blocks, analyze those stakeholders in terms of their interest in the form as well as their power vis-à-vis the corporation, and lastly, prioritize those stakeholders. (Harris & Fleisher, 2005) In academic and industry literature, this three-step process often referred to as *stakeholder mapping*, whereby the prioritization step is especially vital, since it will enable clear foresight where the company's limited resources and energies should be directed by management that will derive maximum benefit towards its long term strategy and overreaching goal, by engaging, via communication efforts and company actions, and efficiently investing in the sorts of stakeholders that yield mutually beneficial relationship standing for both. (Kloosterman, 2014)

Following the steps outlined in the stakeholder mapping and management, firstly the corporation, be it international or otherwise, must go through identification of stakeholders who directly or indirectly might have a vested interest or are simply affected in the outcome of decision-making of the top management of such firm. (Professional Academy, 2018) It is imperative in the mapping of stakeholder relationships to also properly categorize the groups of distinct stakeholders by commonly shared attributes. One way to do that is to broadly categorize the types of stakeholders already identified as those that contribute to achieving the firm's overreaching goal and short term goalposts, and, conversely, those that are affected by firm's operations. In practical terms, it is easy to see that in the case of stakeholders such as i.e. investors, the board, top managers, employees, and business partners, all contribute to company's long term success. (Professional Academy, 2018) In the mean time, the company

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must also considered the local communities, local and national governments, the competing firms, environment, and societies at large, where they do business as some of many stakeholders who are affected by corporate business practices. (Harris & Fleisher, 2005) In the context of complexity of modern day corporate activities, as well to reflect the reality of stakeholder relationships, the managers must also keep in mind that in some cases, the stakeholders belong to both affected and contributing camps, as for example, employees who might have a stake in company's stock, therefore both contributing to its ongoing operation, as well as affected by the value of that company, when it comes to fluctuation of their stock portfolio at any given time. (Professional Academy, 2018)

Similar inter-connectivity applies to top echelon managers who without a doubt contribute to the firm's day-to-day operations, but also share the same natural environment and are members of the same community, which are affected by the firm's i.e. environmental impact on that society. Governments on behalf of taxpayers often contribute to various nationally or locally vital industries in order to spur up the economy and job growth, while also be affected if one of those companies begins outsourcing staff and operations to other jurisdictions to cut on costs or boost profit margins. (Professional Academy, 2018) To put it concretely, even broad categorizations recommended by contribute/affect model require complexity in those stakeholder analysis and some degree of connection between two juxtaposed camps.

Another way to categorize the stakeholders identified is by the distance they have to the core day-to-day operations of the company's activities. For example, senior and mid-level managers, as well as the board would clearly wall into internal stakeholders camps. While government, local communities, customers, media, and society are members of the external stakeholders category that are, whether rightly or not, considered outside of realm of the company , requiring distinct approach to stakeholder relationship management. Even this approach to categorization poses nuanced thinking about these internal and external stakeholders, as many, such as shareholders are not entirely outside of corporation's activities realm, since large portfolio shareholders of company's stock do have a say on its corporate governance and by association general direction of the firm. (Harris & Fleisher, 2005)

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Precisely, due to intrinsic complexity and interconnectedness of some of the stakeholders and stakeholder relationships, be it incorporations in crisis mode or during the time of stability, it is imperative for, especially, large organizations to follow through with stakeholder analysis. A type of analysis which would encompass clear and systematic approach to defining those affected and contributing entities' roles, as well as expectations.

Unlike many governmental institutions in representative liberal and constitutional societies, for corporate governance not all stakeholders are to be treated equally. To act otherwise would be detrimental to sustainability of any profit or even non-profit corporations. Some stakeholders do contribute or pose higher impact on company's operations or decision-making than others. An organization in pursuit of sustainable growth and corporate governance with clear vision what it aims to achieve must not lose focus of who its key stakeholder players are and what makes them the utmost priority for stakeholder management. This truism is further underlined during the crisis a corporation might experience, as it provides a guiding principle of where to direct their contingency and trust rebuilding efforts.

According to the literature, one systematic way is to assess the degree of where the stakeholder group stands on the hierarchy of importance, is to map the stakeholders identified in previous step according to their level of power, in terms of their influence on the corporate decision-making and company's continued operations, and level of interest or the stake. Mindelow Matrix, (Figure 4) allows for systematic and big-picture analysis of what kind of a relationship the company should thrive for with diverse stakeholders, often with conflicting interests. The Mindelow Matrix provides a helpful tool for firms to see more clearly how to do a balancing act between different and conflicting stakeholder motives and priorities, as well as adjust the level of engagement with them, according to their power/interest standing in the grid.

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## MENDELOW MATRIX

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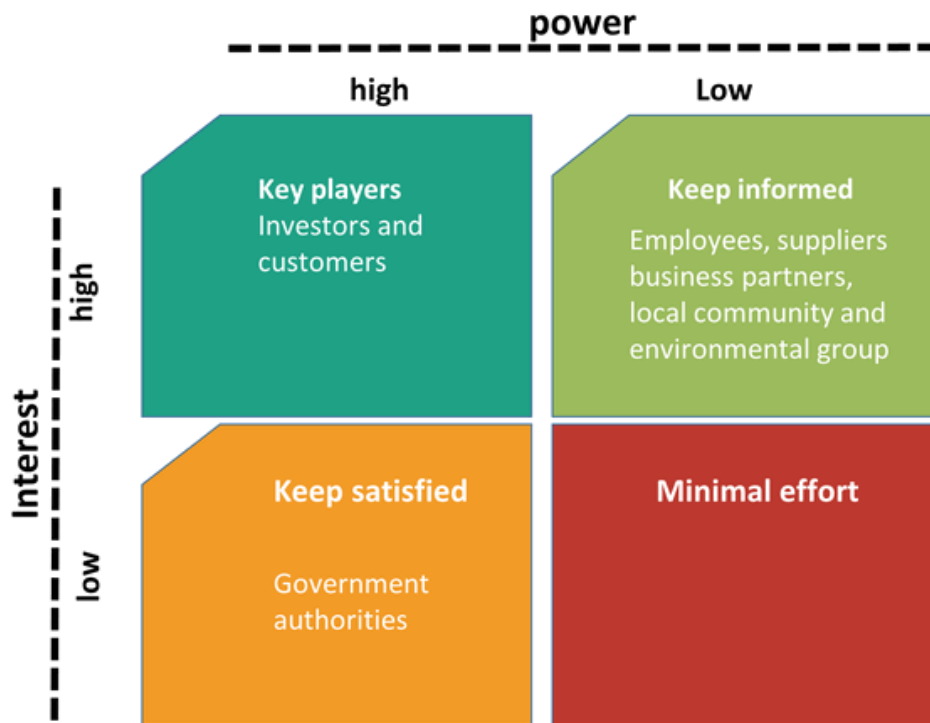


Figure 4: Mendelow Matrix, Image courtesy Zolot Jubar, 2018

The final step, then, in stakeholder mapping is the prioritization their level of needs in terms of resources and engagement proportionate to their interest and stake in the corporation. Stakeholder analysis and stakeholder positioning on Mendelow Matrix grid, then, poses series of questions as well as more likely to present with solutions to stakeholder relationships management. Which stakeholders require management's utmost attention for engagement?

According to the findings in the literature, key players like shareholders and customers attributed with combination of high interest and high power. These particular stakeholders relationships require the most effort in terms of engagement, as well as satisfaction and keeping them well informed on what the corporation is doing as well as future plans. This particular grouping of key stakeholders are typically prone to wilding a significant degree of influence on the organisation's direction, and are often the drivers when it comes to compote strategy. If

unsatisfied with company's performance or deterioration in mutual relationship status, the key players poses the high level of power and stake in the corporation's current standing and its long term outlook, they are often the ones that will create pressure for strategic changes, and overhauls in corporate structure.

The stakeholder group or groups marked by low interest / low power though indeed require much less resources, energy and overall effort than some other stakeholders identified, still require active monitoring. Oftentimes, this group represents competitors, who are identified as stakeholders, if simply ignored would be to company's detriment, especially in highly competitive fields and industries. These stakeholders are to be watched closely, as those competitors are also likely to monitor your organization for strengths these competing firms might emulate to their advantage, as well as weaknesses, which various corporate crisis present, that they might exploit to gain competitive edge.

## 4.2 Corporate Strategy Theories

According to renowned American economics professor, Michael C. Jensen:

"Every organization attempting to accomplish something has to ask and answer the following question. What are we trying to accomplish? ... How do we measure better versus worse? .. How do we keep score?" (Jensen, 2000)

Jensen acknowledges that the widely accepted competing theory to shareholder value maximization is stakeholder theory. The former's priority is defined by Glen Arnold, a former corporate finance academic and avid investor guru "Maximizing shareholder wealth means maximizing the flow of dividends to shareholders through time" (Arnold, 2005) What was often dubbed as *Friedman doctrine*, in laymen terms, this means that the so-called social responsibility of a corporation is to increase its profits, therefore if an executives were to actual pursue responsibility of reaching some arbitrary social goals that would conflict with the responsibilities of the corporations' shareholders, a.k.a. the employers who in essence hired him or her to make them richer, so long as such business plays by the rules of the game – "engages in open and free competition without deception or fraud". (Friedman, 1970)

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Counter to the argument Milton Friedman put forth, in R. Edward Freeman's *Strategic Management: A Stakeholder Approach* publication, the Stakeholder Theory made a proposition that executives should exercise their power within the organizational structure and managerial skills to balance, oftentimes divergent, interests of all stakeholders in the corporation. (Freeman R. E., 1984) This includes not just financial backers such as shareholding owners of the company, but also customers, workers and their union representatives, various business partners, governmental municipalities, and the general public in local and global communities. In short, the goals and aspirations of all the stakeholders ought to be a large chunk of the corporation's processes of decision-making. (Pablo, 2017) At least on the surface, the stakeholder theory appears to be more all together ethical than pursuit of profit-making for its own sake, but not without flaws.

Case in point, since Freeman's stakeholder approach either omitted, or failed to acknowledge the importance of specifications on how exactly a generic team of executives can arrive at necessary tradeoffs among these competing interests. The motion that top executives should practice the art of pragmatism to achieve the balancing act necessary to keep all stakeholders satisfied is simply implied in the stakeholder theocratization. Jensen dually noted, that such theory's many proponents end up leaving corporate governments with an objective that makes it highly unlikely for those managers to make decisions that lead to sustainable success of the organization they oversee. (Jensen, 2005)

What, then, explains the stakeholder theory being popular amongst the top managerial class, and not solely by academics and the theory's advocates, is that the absence of systematic score-keeping, the Freeman's doctrine effectively results in management that's left largely devoid of any accountability for their decisions. (Jensen, 2005) In other words, if you are CEO of a multinational conglomerate with a mandate to be responsible to virtually everyone on the planet, you are responsible to no one, other than your own self-interest.

Professor Jensen goes further to point out both drawbacks, and positive attributes of both theories. For example, shareholder value maximization as a firm's core objective value, is an assessment of how well relative to other firms the corporation's performance stacking up. (Jensen, 2000) However, this is not enough to be source for motivating the top management, as

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well as creating high levels of enthusiasm among low level workers. Therefore, though it would be a prudent corporate practice to set up value maximization score-keeping, the corporate government of the firm must also painstakingly craft, and update when necessary, a clear vision for the enterprise, paired with strategy to achieve that vision, that has the high potentially of uniting the corporation's various many stakeholders for a common goal. (Jensen, 2000)

Jensen calls this compromise between two competing camps of firm objective as Enlightened value maximization. The theory he puts forth represented a shift in one-dimensional thinking, and a genuine effort to reach a balancing act between primacy of the shares-owners and interests of corporation's multiple stakeholders whose interests might be diverse from those of the owners. When these stakeholders are properly incentivized by company's long term strategy, tactics and overall vision, this allows them to stay motivated and focused on long-term value maximization. Since, EVM theory takes the long-run, as opposed to short-term gains and run approach, to value maximization as its primary objective, this translates into "enlarging the corporate pie" by making investments or corporation's resources and energy into identified set of stakeholder groups, just so long as in doing so the long-term value for the firm will be greater than the cost of such investment. This is especially the case with firm's blind-spot stakeholders, where the corporation failed to address their interest in the past. (Jensen, 2005)

In such scenario, i.e. the investment efforts in corporate social responsibility (CSR) management, which proponents of Stakeholder Theory would suggest as a tactical measure to meet the firm's objective, is not only compatible with firm's long-term financial success, it might accelerate it. The corporations, international or otherwise, which are willing to change their corporate culture in order to have a long-term vision and the strategy to match it, will reap the rewards of sustainable growth.

The data collected and analyzed by James Wallace, though might need further research, suggests that value creation for the shareholders - not to be confused with value optimization – acts as a precondition to making the rest of stakeholder beneficiary of value creation. It is a prerequisite state for the latter to occur, and Wallace's findings, looking at data analyzed, points to strong correlation between corporations that failed to provide additional value for their owners and failure in added value creation for the rest of stockholders. (Wallace, 2004) What's more, for the

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corporate boards that have neglected to invest or haven't sufficiently invested in strengthening stakeholder relationships, and finally make the necessary effort to do so, the research suggests that this in a longer run will lead to additional value for the shareholders. (Wallace, 2004)

## **5. Findings to First Research Question**

By the 21<sup>st</sup> century, it was widely expected and accepted by businesses themselves, that corporations need to recognize and map out (as illustrated by Figure 4) the scope and power of their stakeholders and be closely in-tuned to their needs and concerns and consider them during business decision making. At that point, the executives are then faced with a hard, but not impossible, task of maximum value creation for stakeholders whilst forgoing making major trade-offs. Ultimately, the stakeholder theory holds that more competitive organizations will endure in the long-run, precisely because they found a way to manage, aligned towards overall same direction, multiple stakeholder interests. (Freeman E. , 2014)

### **5.1. Mapping Volkswagen Stakeholders**

Considering that Volkswagen Group has presence world-over, and what's more, a large number of diverse stakeholders (as illustrated in Figure 4), it was of no shock value that plenty of other stakeholders such as fleet managers, governmental agencies, dealers, competing firms, environmental NGOs, and all kinds of other interest groups followed up the scandal with dismay, disapproval, and disbelief. This paper then will take a closer look at who were the most relevant stakeholders in VW emission scandal, and what were their expectations, motivations, roles, and counter strategies.

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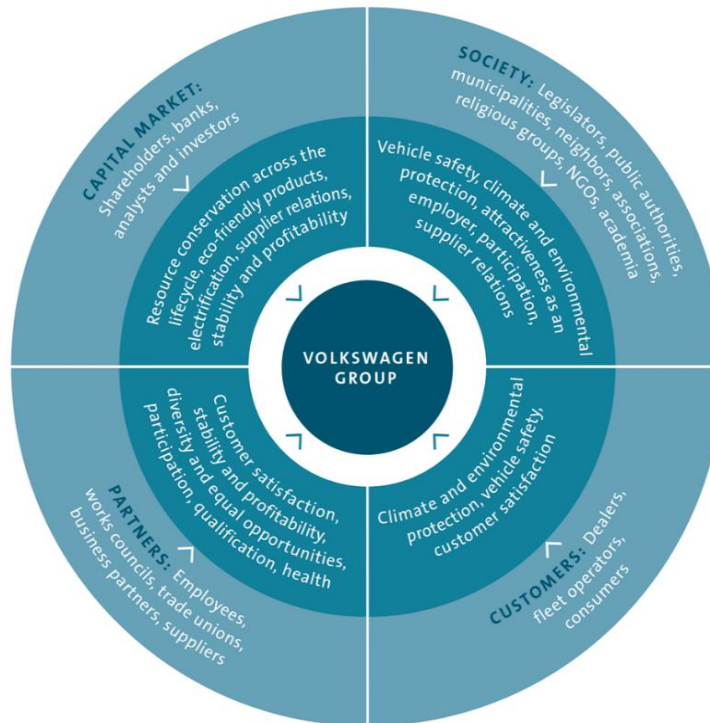


Figure 5: Volkswagen's Stakeholder Management Map. Image courtesy of Volkswagen Sustainability Report 2014

In contrast, VW stakeholder groups mapping, as seen in Figure 5, has a two-tiered structure, where primary and secondary social connection within Volkswagen's stakeholder grouped like so:

- (1) Internal stakeholders – is really a composite of two divisions
  - (a) Automotive services
  - (b) Financial services
- (2) External stakeholders - consisting of capital markets, customers, partners, and society.
  - (a) Capital markets - shareholders, banking institutions, financial analysts, investors
  - (b) Customers – comprise of consumers, dealers, fleet operators
  - (c) Partners – are employees, work counsel, trade unions, trade partners, suppliers

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(d) Society – are legislators, public authorities, local municipalities, NGOs, “neighbors”, associations, religious groups, academia

## **5.2 Significance of Focus on Specific VW Stakeholders**

For the sake of clarity and consistency, the most affected stakeholders in the VW’s Dieselgate are broken down, and further analyzed in details with a subsequent Stakeholder Mapping technique done according Volkswagen Stakeholder Management Map (see figure 5), prior to emissions scandal unfolded. This approach also has a secondary purpose to point some of Volkswagen’s management’s blind spot/s, prior to getting embroiled in the emissions scandal. By evaluating the stakeholder relationships between the key players, with utmost interest and power, according to Mendelow’s Matrix, allows for uncovering of the group of stakeholder’s motivations, roles, strategies, and counter-strategies to the unfolding major international corporate crisis.

From the research paper background, it was thoroughly established that Volkswagen top management failed to satisfy the legislations in place, concerning environmental impact, of fraudulent emissions standards skirting, in multiple jurisdictions. It’s been also covered in great detail the impact, strategies, and likely motivations of top management of the company just prior to Dieselgate and throughout the crisis as well. What, then, requires careful consideration is closer look at what Volkswagen Group deemed as “external stakeholders”, who were also most affected by their internal and abnormal deceptive practices.

Specifically, in addition to key players, such as shareholders, customers, and dealers, the paper also makes explicit attempt to analyze “the society” as an important, but low in power stakeholder vis-à-vis Volkswagen. The significance on looking at society in international crisis context, is briefly already covered in literature review, and has to do with complexity of inter-connectivity of other stakeholders to a larger society, which they are also members of. Furthermore, same could be said for the natural environment. However, the environment’s motivations, and strategies cannot be assessed, while the society’s role, motivation, and strategies can be established via relevant research and scientific data published, with environmental impact of the Dieselgate scandal covered as an affect to society, at large.

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### 5.3 Society

Margaret Thatcher, who served as Conservative prime minister in United Kingdom between 1979 and 1990, one famously quipped that there is “no such thing as a society”, referring to the fact that as an entity, *the society* is a social construct that we use to refer to many distinct and diverse individuals who belong to other small subgroups, such as families and local communities, typically within a nation state. (Brittan, 2013) Whether one agrees with former prime minister’s analysis, the corporations’ misconduct or crimes, as in VW case of emissions regulations cheating, against the environment, it’s rather difficult to make precise calculations whether any or substantial damage is being done, which particular individuals are affected the most, what those damages might be, and what is the monetary effect on those affected. However, based on our scientific knowledge of how atmosphere works, and of how various pollutants in the atmosphere lead to effects on human health, it is possible, with some degree of both error and certainty, to come up with estimate of those damages to a society, as a stockholder.

There were numerous studies done on VW Dieselgate’s effects on society, mostly looking concretely at environmental damages and public health risks associated with those damages. Just when putting health risk of Americans at a focus, according to a study led by MIT and Harvard University researchers, VW deceptive worldwide company practice of installing its light duty diesel vehicles with “cheat” software in order to evade enacted regulations regarding emissions standards in some 480,000 diesel VW vehicles sold in U.S. has a high likelihood of directly contributing to premature deaths in around 60 Americans, nationwide. (Chu, 2015)

According to the study, published in the *Environmental Research Letters* journal, the methodology behind its findings involved looking at the amount of excess emissions. This extra pollution was then multiplied by the total number of vehicles that were affected by the defeat software already sold in the U.S., and further extended over population distribution and factors of health-risk around the country, ultimately finding significant negative effects to public health, as a direct result of VW’s Dieselgate practices. (Chu, 2015) The group of researchers built on calculations already made by their colleagues at the University of West Virginia. They uncovered that VW diesel models tested on road mode emitted from 30 up to even 40 times the toxic emissions that was allowed by federal law. A team of aeronauts and astronauts at MIT led

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by Steven Barrett made calculations of emissions under the following scenarios: (1) The status-quo scenario under the assumption that 482,000 VW cars were already emitting above permissible levels into the atmosphere; (2) a recall scenario, where VW recalls all vehicles with defeat software by the end of 2016; (3) and no recall scenario, where affected vehicles are let to continue drive on the roads, emitting the excess pollutants over a course of those vehicles' lifetime. (Chu, 2015)

The study further concluded in real terms that 60 individuals will die, on average 10 to 20 years, prematurely. The MIT and Harvard team made a case that if the automaker follows with policy of recalling all affected vehicles in U.S. by the end of 2016, more than 130 premature deaths may be avoided, and may lead to 840 million USD in savings in further healthcare and public funding costs for the society, at large. (Chu, 2015) In addition to premature deaths estimates, published research paper also pointed out that VW's over-the-legal limit extra emissions would *contribute* - making important distinction between causation and contribution – to 31 chronic bronchitis cases, as well as 34 hospital admissions of patients suffering with respiratory and cardiac conditions. (Chu, 2015)

Those findings are just concerning U.S. society as VW's stakeholders who were affected by their deceptive practices and subsequent scandal that followed as a result of those practices. The MIT researchers put a premature death toll, much higher than American counterpart, concluding that European nations, including Germany, France, Poland, and Czechs were hardest impacted by excess emissions between 2008 and 2015. Of the total 1,2000 premature deaths, 500 will likely occur in Germany, the home of Volkswagen Group, while the rest premature mortalities stemming from faulty cars will hit many neighboring countries as well. (Chu, 2017 ) It's not only that far more number of VW vehicles were sold in Germany, 2.6 million compared to 482 thousand in United States. Other differences must be taken consideration to properly assess the damage made to public health across European continent, such as different driving behaviors, population density, and local atmosphere. (Chu, 2017 )

The team of researchers behind *Environmental Research Letters* closely examined VW, Skoda, SEAT and Audi models with excess emission levels beyond the EU's permissible limits, and

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concluded that negative effects stemming from those emissions significantly affected the public health of not just Germans, but European societies, in general. Steven Barrett, Associate Professor of Aeronautics and Astronautics at MIT, as well as a co-author of the study pointed out that “Air pollution is very much transboundary... Thus, a car in Germany can easily have significant impacts in neighboring countries, especially in densely populated areas such as the European continent.” (Chu, 2017 )

Volkswagen’s main disservice to society stakeholders, world-over, was not just that they’ve broken a long-standing environmental protection legislation of those nations, but knowingly and actively failing those society members at properly controlling VW vehicle for dangerous air pollutants at certain levels: nitric oxide and nitrogen dioxide. Collectively abbreviated as NO<sub>x</sub>. NO<sub>2</sub>, are well known to cause respiratory damages. NO<sub>x</sub> is found to be contributing factor in the formation of ozone. (Selin, 2015) Moreover, it especially when combined with other pollutants in the atmosphere, that NO<sub>x</sub> becomes a serious threat - when ozone mixes with particulates in the atmosphere – such as ammonia. The ozone and fine - smaller than 2.5 micrometres in size - particles present in the atmosphere were known to scientists and medical community to lead to series of health problems for those that are in its close vicinity, such as people who live near highways and busy roads. (Selin, 2015) What’s more, since NO<sub>x</sub> leaves the engine as a gas, it is likely to be then taken up by winds, while on its travel, the pollutant will interact with ammonia already present in the air – a reaction that results in production of fine particles. (Chu, 2017 )

This was found to be a bigger public health hazard in Europe than it was in United States, where the emissions scandal initially broke out, precisely due to the fact that European region’s atmosphere contains more ammonia than in the latter. The public’s exposure to such fine particles mixture has also been scientifically proven to lead to respiratory and cardiopulmonary diseases. (Chu, 2017 ) Negative health symptoms include shortness of breath, coughing, and inflammatory issues, that can onset such ailments as asthma, harming of lungs function, and other respiratory illnesses, such as emphysema. (Selin, 2015)

The way researchers arrived at the estimates of premature mortality was by using similar methods that were adopted for VW impacts on health in the U.S., as illustrated early in the

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chapter. To assess the actual numbers of premature deaths likely to have been caused or contributed to as a result of VW deceptive practices, and by each European country, the team of researchers resorted to basing their analysis on the affected VW vehicles emissions data generated German Federal Motor Transport Authority.

Under one scenario, between the years of 2008 and 2015, the research found that 1,200 premature deaths of Europeans will likely take place due to excessive emissions by VW vehicle that have already been emitted into the atmosphere, with most damage done to Germany's society stakeholders, with estimate of 500 deaths. (Chu, 2017 ) Whereas, under second scenario, the Barrett's team estimated that if VW would make an effort to fix all the affected vehicles to get them to comply with European environmental standards by the end of 2017, the VW Group would prevent 2,600 lives lost due to premature deaths. (Chu, 2017 )

Though when Dieselgate began in 2015 VW did immediately followed through with recalling 8.5 million vehicles across European region, their repair was rather slow, reaching 80 percent of all affected diesel vehicle by middle of 2018, with de facto guarantee to resolve all recall-related issues by the end of 2020. This was also related to the fact that many customers made performance and fuel efficiency related complaints of the vehicles post fixed emission levels. One class action suit against the company claimed that 10 percent of VW diesel owners made claims of "limp mode" episodes - loss of power at relatively high speed, while 40% reported suffering reduced power and acceleration. (Brignall, 2017)

While, when it comes to fuel efficiency trade-off, the Australian Automobile Association released stark findings that "fixed" VW diesel by the company, now use up to 14% more fuel after the recall, without any compensation from the company (outside of U.S. customers) (Ayre, 2018). These allegations and findings confirmed similar complaints against the company's reactive practices made by owners, worldwide, as well as the general theory that the reason why VW skirted the regulations on emissions standards, in the first place, was to have cars that are superior in performance and fuel consumption when compared to competing brands that met the regulatory standards, at the expense of higher than acceptable emissions, thereby putting societies at higher health issues and premature deaths risk.

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The value proposition and sales pitch of Volkswagen's luxury brands, including Bentley and Porsche up to recently have been style and superior performance, fuelled by German engineering, trumping fuel economy. However, that gradually began to change during last couple of years. (Glinton, 2018 ) For years, the company was also overly invested in diesel engine technology. Years after restructuring and reforming VW management approach and direction for the multinational company, the emissions scandal had some positive outcome of forcing the company to distance itself from increasingly tarnished image as diesel automotive manufacturer, and be on a lookout for new market opportunities and positioning for VW Group. This includes, but not limited to, pivoting towards more environmentally friendly electric vehicles, and even venturing into ridesharing market. (Glinton, 2018 )

Already back in 2016, at the height of Dieselgate controversy, the newly acting VW Group CEO made an announcement that the troubled company would proceed with a new plan on investing billions into developing over 30 fully-electric models of cars by 2025, while assuring all strata of stakeholders involved that the emission testing on its vehicle hence force will be evaluated, independently (Ruddick, 2016). Only time will tell, whether these post-scandal corporate reforms will be a net positive for individual societies and society stakeholders, worldwide, but the company stated intentions appear to be on the right track to make this a possibility in a long run.

## **5.4 Customers**

The customers who unknowingly bought the effected models undoubtedly suffered due to resale price of their VW vehicles drop sharply due to Dieselgate. However, since part of the legal proceedings by federal agencies against VW on behalf of American citizens resulted in a settlement deal where some 85,000 VW car *buybacks* – option given to owners to “sell” the affected models back to VW, as well as get extra cash for the trouble of doing so, and essentially acted as reparations for negatively affected U.S. customers. (Bartlett, Naranjo, & Plungis, 2017) Moreover, people who were interested in participating in buyback programs were qualified restitution payment on top of NADA trade-in value. In practical terms, that meant for average buyer that VW's total settlement amount was model's former book value, on top of rebate of

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anywhere from \$5,100 to \$9,900 that was primarily dependent on age, mileage, and car's features. (Bartlett, Naranjo, & Plungis, 2017)

So, in hindsight, the settlement can lead to interpretation as being intentionally generous and tilted towards the customers, as a way to both punish VW for deceiving corporate practices, whilst having a secondary effect of deterring other automakers from figuring that similar emissions regulations cheating is even a viable option, going forward. (Bartlett, Naranjo, & Plungis, 2017) Though deemed controversial, but nevertheless of important note, is that many industry experts also concluded that VW's emissions scandal didn't actually end up diminishing owners' car performance levels. (Brannon, 2016) A car's performance and emissions levels should not be confused as one and the same. Conversely, boosting the diesel car models' performance at the expense of higher emissions is in large part why VW made unfortunate decision to actively cheat to begin with, hoping that consumers will both take note, appreciate, and reward the company for the value of the former, and wouldn't be able to notice or ever find out about the unseen costs associated with the latter. (Brannon, 2016)

In fact, even Consumer Reports circa 2015 had little choice but to disclose that after performing testing of 2011 and 2015 Volkswagen diesel vehicles with in-built defeat devices, found improved performance in both of those models that came from lower fuel economy when compared to comparable vehicle of other auto companies that did strictly follow the EPA emissions standards. (Fisher, 2015) The 2011 model even exhibited reduced acceleration. (Fisher, 2015) All this points out, that even prior to lawsuits and subsequent settlement arrangements, the average VW consumer may have, in fact, benefited from the company's cheating on emissions.

Still, even if that's the case, the over-the-legal-limit emissions from the VW cars didn't hurt the owners per se – but it did damage the environment, meaning that it affected all of the society, without discrimination and general regard whether such a stakeholder, disregarded by VW unconventional practices, owned one of those Volkswagen models or not. (Brannon, 2016) The paper specifically deals with concept of society as a both affected and very important stakeholder, in earlier chapter.

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## 5.5 Dealers

When Volkswagen ventured into deceptive practices of hiding true emissions from their vehicles, and eventually were caught red handed in the middle of, still in many ways ongoing, scandal, it inevitably created a huge hassle and further inconveniences for some 650 VW dealerships, on nationwide scale. (Mansouri, 2016 ) Total percentage of VW diesel vehicles sold by network of dealers constituted some 20 percent of total VW vehicles sold by them around the time Dieselgate broke out. For their part, VW did followed up with an assistance package, which purposely was designed to help Volkswagen dealerships dealing with the negative fallout from the scandal. The package put together by VW early in 2016, included range of monetary assistance that took different forms and was composite of subsidies, higher than usual bonuses on sales on company vehicles, and other incentives for network of dealers that for a duration of the scandal had to cope with sluggish sales and lower profit margins. (Mansouri, 2016 )

Another measure that took into effect almost right after the scandal started, is the temporary halt of sale of diesel vehicles made in U.S. subsidiary of global VW, a move that inevitably made impact on sales by the dealers. So to deal with its negative affects of diesel vehicles temporary prohibition on sales, VW made available no-strings-attached discretionary funds for dealers, as well. The actual amount of such discretionary loans were largely based on dealership's volume. (Mansouri, 2016 )

As crisis deepened, the dealers all over the country, were naturally concerned whether even the relief program already in place was sufficient enough for their survival. Michael Horn, then CEO of Volkswagen Group of America appeared to be sympathetic to those concerns in his statements directed towards dealers with cash flow problems, however he never specified the exact details of nor the date when it will take into effect. (Craine New Service , 2015)

For example, one VW dealer in state of New Jersey pointed out that such funding was desperately needed in order to cover his dealership's operating costs, as well as used for marketing extra marketing costs. Some other VW dealers on the U.S. East Coast complained that post scandal breaking out in the news, they are either breaking even or losing money because of it. So, any discretionary funds approved by VW America corporate goes a long way to break even or generate some mediocre profitability. (LaReau & Beene, 2015)

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In the meantime, other dealers duly noted problem created by Dieselgate that was detrimental to their business model. Since foot traffic in the dealerships was essential in conversion of those walk-ins interested in acquiring VW vehicles into actually closing the sales, that traffic by consumers had significantly went down as a result of Dieselgate, so the VW's incentives programs were of some help to dealers to strike sales with now fewer pool of interested clientele (LaReau & Beene, 2015).

New York's general manager also mentioned that though the monetary assistance was primarily used to present more attractive deals with highly sceptical VW vehicle customers, also added that the remainder of funds had secondary affect of incentivizing greater motivation in sales teams and other employees, as they were working under extra pressure from the scandal, and in many ways with odds of meeting previous sales quotas now sharply against them. (Craine New Service , 2015)

Ultimately, the dealers' motivations to run both respectable and profitable enterprise selling VW vehicles to customers looking for added value and prestige that used to come with owning German-engineering automotive. Their anxiety and scorn that was unleashed by the scandal, was further put to rest in January 2017, when California's district court judge approved \$1.2 billion settlement from Volkswagen to go specifically to compensate affected dealerships. (Reuters Staff, 2017) On micro level, that meant that on average each dealership were entitled to \$1.85 million for the VW deceptive practices at the corporate level that inflicted on dealers the burden and inconvenience to deal with the fallout of increasingly smaller and harder to sell inventory. (Reuters Staff, 2017)

For Volkswagen North America part, this agreement also included continuation of making incentive payments to dealers based on volume, as well as payments already made prior to court's ruling that were made possible by company's top management on voluntary basis. (Reuters Staff, 2017) Hinrich Woebcken, then newly acting CEO of VW North American region, even made public mentioning focusing on repairing their commitments dealerships as an important step to start regaining trust and rebuilding mutually beneficial relationships with company's many other valuable stakeholders, as a way to show company's shift in vision post Dieselgate fallout. (Reuters Staff, 2017)

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All in all, the literature points that although the VW dealers were inevitably at disadvantage as a result of VW emission scandal, resulting in mass wave of tarnished goodwill towards its fleet of diesel cars, as well as the brand in general, when the scandal began to unfold. Due to both voluntary reactive actions by the top management, change in leadership, and legal proceedings in the U.S., that were ultimately skewed towards benefiting the dealers as well as other connected and external stakeholders, it is not a stretch to come away with analyses that by the year 2017, the emissions standards skirting scandal as either a net positive for dealers, at best, or at worst, a wash in terms of revenue lost and monetary retributions consequently received as part of the settlement deal VW made with U.S. lawmakers with approval from judicial bodies. However, such rather unnuanced stakeholder analysis is somewhat problematic in nature, because it mistakenly regards dealerships, and more specifically, dealers themselves, as insulated group of stakeholders from the rest of society, which they are evidently also part of.

Since, it was detected and uncovered, beyond shadow of the doubt, that emissions from various models of VW diesel vehicles, while on the road, emitted toxins into general atmosphere that were far beyond legally acceptable standards set forth by environmental regulators, and therefore highly likely presented a health hazard by impact to overall air quality and the environment, the dealers were also negatively affected to that extent, going beyond immediate monetary losses and hassle associated with the Dieselgate. (Chu, 2015) Therefore, similarly in the case of VW customers discussed earlier, this secondary impact on dealers-as-members-of-the-society stakeholder interest grants further research and deeper analyses and understanding.

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## 5.6 Shareholders



Figure 6: Volkswagen AG Share Value History from 2013-2018. Image courtesy Google Finance

Shortly, after the emission scandal broke out, the VW Group stock value began downward trajectory, as seen on Figure 6. As a direct consequence, this sent shocks to the numerous investors and shareholders' portfolios of what up to Dieselgate's beginnings have been a blue-chip investment in a company with a moderate and steady long-term growth, as well as shattered the company's relatively pristine reputation status with those shareholders. All over the world, many shareholders resorted to legal actions against Volkswagen AG, and claimed to have suffered negative impacts from the VW's corporate governance practices that led the scandal and failed their trust, as well as hurting them financially, as a result.

By early March, 2016, VW's preferred shares' value went down by almost 2 percent on Frankfurt Stock Exchange, which made VW stocks the biggest loser relative to other German DAX blue-chips. (Dörner, 2016) Since the scandal went public in September, the drop in VW preference shares, as well as ordinary shares, resulted in a loss of 30 percent of company's

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overall market value. (Monica, 2015) In real monetary terms, the Dieselgate cost the automaker, and by default its institutional and private shareholders almost €30 billion. (Rosevaar, 2017)

The allegations and legal tsunami began to unfold immediately. For example, just in March of 2016, close to 280 institutional shareholders and investors filed lawsuits against VW conglomerate with the Braunschweig's regional court in the German state of Lower Saxony. (Reuters Staff, 2016) The plaintiffs included such foreign invested institutions as CalPers, a California public pension fund, and local institutional, such as subsidiary of German insurance giant Allianz. (European Parliament, 2016) At the time of class action lawsuit, the plaintiffs collectively demanded €3.3 billion (or \$3.6 billion) as reparation for damage incurred from by the automotive conglomerate's actions. (Dörner, 2016)

Their claim was steeped on facts on the ground. That between years 2008 and 2015 VW top management breached their duties in relation to capital market. Another accusation made by the institutional shareholders, is that the companies failed in their duty to them to properly inform the shareholders in time about the scandal, prior to them hearing about it in the press. (Reuters Staff, 2016) VW took a defensive stance that such allegations are not merited against the Board, and that its top Management properly followed the German capital markets laws governing disclosure obligations were not breached. (Reuters Staff, 2016)

Still, during the first annual meeting, in Hanover, Germany, nine months after the Dieselgate's onset, VW's senior managers faced visible anger and discontent from over 3,000 shareholder that were present. (Ruddick, 2016) The bulk of criticism was concerning the handling of the emission scandal by the supervisory board up to that point, with many shareholders voicing demands for serious overhaul of its managements structure and the corporate governing policies. The head of shareholder association, DSW, famously was quoted as describing VW failed approach to corporate governance that led up to rigged emissions fiasco as "shambles" and "collective failure". (Ruddick, 2016)

Hans-Christoph Hirt, a representative from one of the globe's biggest institutional investors, Hermes, made specific criticism of Martin Winterkorn's 7.3 million euros "exit package" for global scandal and criminal charges entangled CEO, but made pledge to vote against one of the

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key motions at the meeting – the outright firing of the sitting management and the supervisory board. (Ruddick, 2016) Hirt did harshly criticized the company's disregard for universally accepted fundamentals of corporate governance, that inadvertently ended up hurting not just the shareholders, but German economy as a whole, while calling for an independent audit of the very structure of that supervisory board. (Ruddick, 2016)

The supervisory board's chairman, Hans Dieter Poetsch, received much of brunt from angry shareholders, on the personal level. For example, the director of the German Association of Ethical Shareholders called the move by VW Group to appoint a former CFO, a person who was in top management position during the emissions scandal, to oversee the internal investigation of wrongdoing as conflict of interest, and hence highly misguided (Rauwald, 2016). During the meeting, there were even active attempts to unseat Mr. Poetsch as the chairman due to shareholders' discontent. (Rauwald, 2016)

Since VW employees are partial holders of its ownership, their shareholder interests' sole representative pointed to the board what this corporate crisis boils down to, and that it is a crisis of trust, while a representative of representative of another investment group accused the company of deceiving the shareholders by practicing cost leadership, while the corporate was preaching market leadership, instead. (Rauwald, 2016) In all complaints, there was a common theme, that in order for VW regain shareholders' trust meant complete restructuring of its corporate structure and its approach to doing business fit for *das auto* market leadership in the 21<sup>st</sup> century.

Indeed, when one looks to compare its ownership structure to other major multinational corporations, Europe largest automaker remained to be an anomaly, not the general rule, especially when it came to its owners' voting distribution. (Böhme, 2016) In 2016, at the time when that turbulent shareholder meeting took place, all but ten percent of owners who held close to 300 million ordinary shares – that is the kind of shares that come with voting rights, and hence tremendous power to make major changes VW corporate governance - were represent just by three major conglomerates (See figure 7). (Böhme, 2016) When it comes to shareholder structure, VW has two-tiered corporate ownership structure between 206 million non-voting preference shares and 300 million shares that come with voting privileges.

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On top of unusual consolidation, all three: Porsche-Piëch family clan, State of Lower Saxony, and Qatari state owned holding company, were problematic in terms of alignment of their interests with interests of all other stakeholders, including the other owners present at Hanover meeting, who were clamouring for major overhauls in leadership and supervision overseeing the firm. Neither were inherently predisposed to rapid reforms and change in the way VW would do business, that would lead to re-building better relationships with its numerous stakeholders.

### VW shareholder breakdown

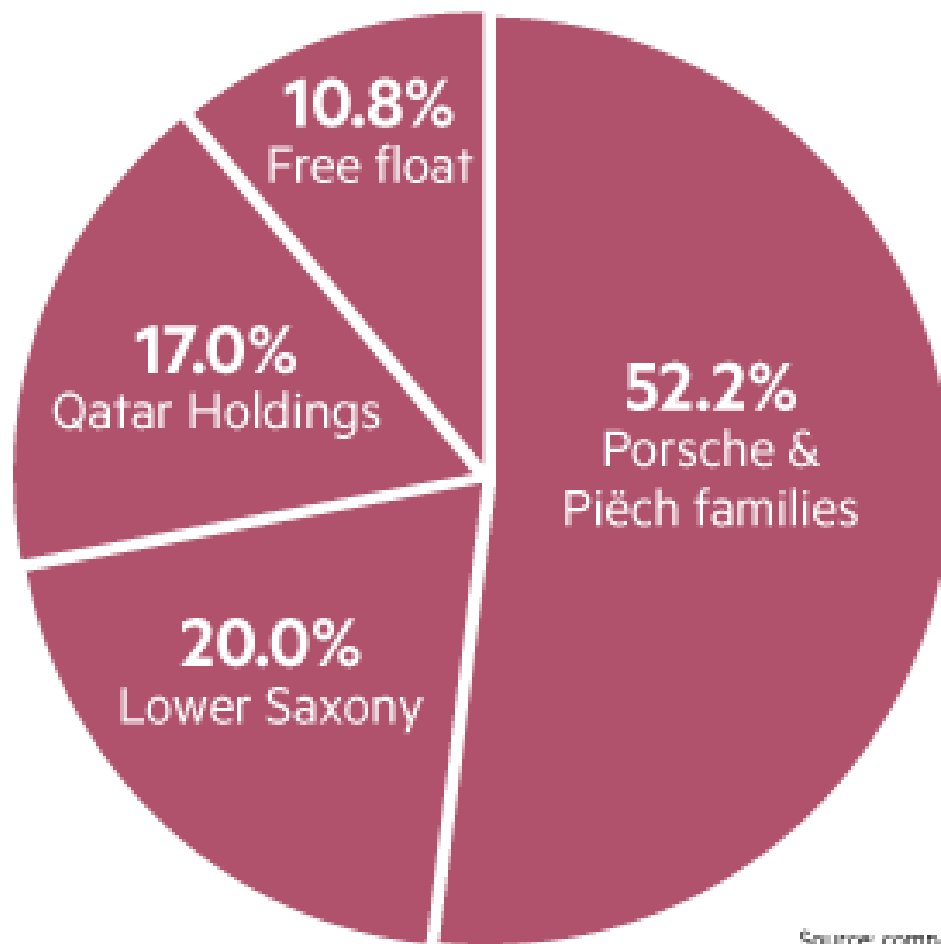


Figure 7: Volkswagen's 2016 Voting Shareholders Breakdown. Illustration courtesy Financial Times

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## 6. Findings to Second Research Question

The Volkswagen's international emissions crisis is case of corporate structure with faulty checks and balances that disincentivize top management to primarily stay focused on sustainable growth through creating net value for its stakeholders, as opposed to themselves. In order to properly assess the rules and guidelines from a perspective of an international company, such as Volkswagen Group to follow in order to both: address and manage a crisis and concerns of its stakeholders; systematic techniques to employ in order to prevent an internal problem within the organization to escalate into a full blown international Dieselgate type crisis, the research must disclose what the fundamentals of corporate governance of German corporations are. This is especially relevant, since onset and especially during the meeting of shareholders in 2016, many accusations were made that Volkswagen's top management failed to properly adhere to those fundamental principles and might have even broken some regulations, in the process.

The allegations have some support in actual data available. Even before the scandal broke out, Morgan Stanley Capital International's Corporate Governance Quality Index assessed sustainability of corporate governance practices by major corporations, and found it already to be at bottom 28th percentile of companies covered by MSCI researchers, globally. (MSCI, 2015) Shortly after an internal crisis turned into Dieselgate, that rating was further downgraded to just 2.6 points, out of 10, placing them way at the bottom of the heap, when it comes to corporate governance performance. (MSCI , 2016)

### 6.1 Germany's Corporate Governance System

Since Volkswagen Group, though a multinational conglomerate, is headquartered and maintains much of its top management in Germany, it's essential for case study to closely examine corporate governance fundamentals and acceptable practices of that country's jurisdiction. Primarily, such fundamentals and codes of proper corporate conduct are rooted in the provisions put forth by: German Corporate Governance Code; German Stock Corporation Act; and German Codetermination Act. (SGL Group, 2018)

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While the German Corporate Governance Code contains statutory requirements for the top management and supervisory boards of Germany's stock exchange listed corporations, specifically, national and internationally acceptable standards of appropriate corporate governance. (Deutscher Corporate Governance Kodex, 2018) The Code is not compulsory, therefore is not enforced through judicial means, but rather the standards of conduct are recommended and suggested to German based corporations. Still, corporations that choose to deviate from the listed recommendations have to either comply or explain the reasons behind nonconformity (Deutscher Corporate Governance Kodex, 2018).

Thus, the Corporate Governance Code's primary objective is to encourage transparency in corporate governance practices of Germany's corporate sector, as well as ensure confidence of national and international investors, and other stakeholders in the management and supervisory boards of said corporations. (Deutscher Corporate Governance Kodex, 2018) The secondary objective is to ensure a desirable level of reputation for "made in Germany" brands, as it relates to international markets. Therefore, The Code takes pains to point out the obligations of these boards to both make sure the continuation of the corporation's business activities, as well as value creation and maximization in a sustainable manner, in line with core principles of Rhine capitalism. (Kreijger, 2018) Also known as social market economy, its principles call for responsible, socially conscious, reputable business ethics and modes of doing business, not simply a compliance with the laws of the land. (Deutscher Corporate Governance Kodex, 2018)

The German Stock Corporation Act of 1965, really goes back to the German imperial chancellor Otto Van Bismarck's reforms, which themselves were mirroring existing regulations of corporations of 17<sup>th</sup> century Netherlands (Kreijger, 2018). Also known as Aktiengesetz, unlike The Code, is compulsory, and its enactment and various amendments were intended to ensure some minimal checks and balances in a corporate structure of German industrialists (Kuntz, 2017). This is done, primarily, via separating powers and acting duties between board executives and the board supervisors, and this structure referred to as *dual* or *two-tier board*, illustrated in figure 8. (Kuntz, 2017) The intention was that independent supervisors on the board would ultimately hold acting management accountable, while ensuring safeguards for interests of the shareholders. Similar structure is also compulsory or voluntarily practiced, out of simple

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preference, in many other European countries, but is virtually non-existent in English-speaking nations. (Kreijger, 2018)

### Corporate control: Germany's two-tier board system

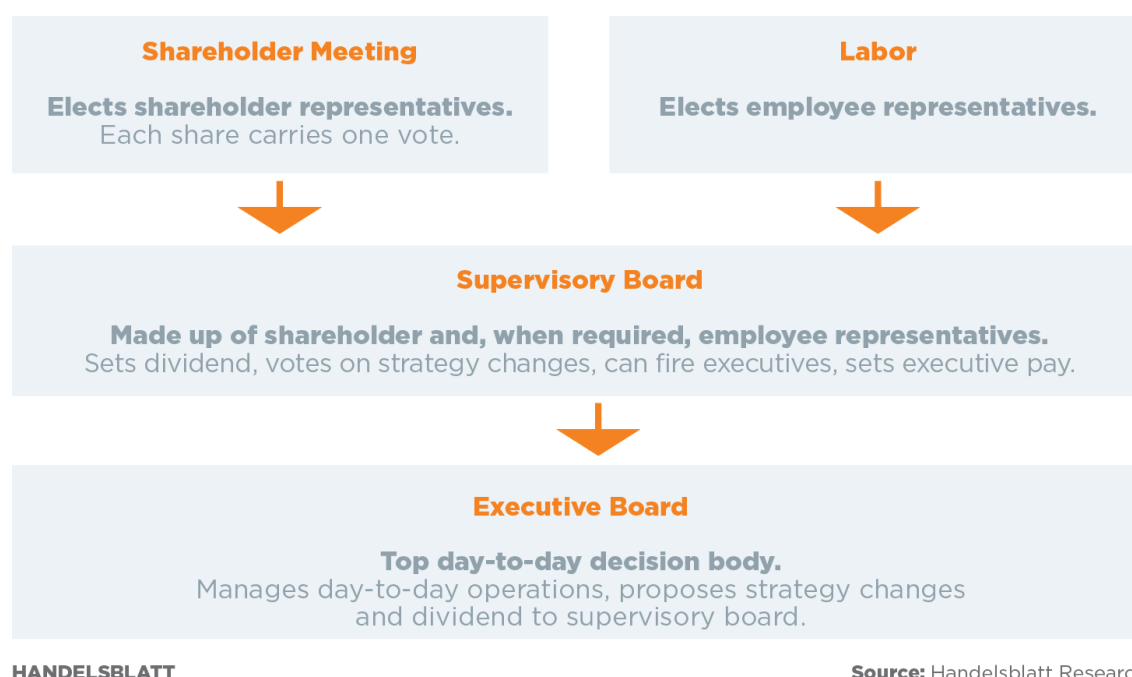


Figure 8: German dual or two-tier board structure. Image courtesy of Handelsblatt Global

In practical terms, the German government has a prohibition on persons being members of both supervisory and managerial boards, simultaneously (SGL Group, 2018). What these members are obligated to exercise are standards of care of prudence and diligence when carrying out their board duties and conducting business activities. To be compliant with stated standards, board members are directed to consider the interests of board of directors, the shareholders, interests of employees and the public's interest. (SGL Group, 2018)

The core bedrock behind German Codetermination Act of 1976, is not limited to Germany only. (Charles M. Elson, 2016) Broadly, the compulsory ruling that legislated that the employee representation should occupy half of the corporation's supervisory board's seats, as well as one seat on the executive board, thereby guaranteeing a strong voice in the firm's decision making

process. Since supervisory board ultimately sets the agenda for the firm, collectively, the employees are treated on equal footing for the general direction of the company, and so major decisions must closely align to their interests to garnish votes needed to move forward. (Charles M. Elson, 2016)

The act, locally referred to as Mitbestimmungsgesetz, sets obligation for all corporations that employ 2000 or more workers that they must include two-tiered representation structure consisting of shareholders and labour, with equal number of representatives from both set of stakeholders. (Charles M. Elson, 2016)

Specific to VW AG, when it comes to VW's 20 member supervisory board, 10 seats are reserved for workforce's representatives, and the company have been in compliance with Germany's co-determination. When the Dieselgate broke out, the director of the Germany's largest national trade union - IG Metall, that also represents VW workforce, even acted as interim chairman of the supervisory board. (Charles M. Elson, 2016)

In Germany, such unions usually referred to as works counsel or *Betriebsrat*, the representatives also go through election process, and they primarily concern themselves with workers' conditions, compensation, and job security. (Sullivan, 2017) In a best case scenario, they work out the details with the rest of the board how a particular decision put up for a discussion or a vote can benefit both stakeholders. At worst cases, using their power on the board, the workers counsel might attempt to gain benefits, or block necessary restructuring measures, on behalf of the workforce at the expense of the interests of the owners, or some other stakeholders.

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## 7. Discussion

It is undeniable fact that world's car manufacturers are currently, and have been for decades, in a cycle of cut-throat competition, constantly looking for a competitive edge over other car makers. Often this translates into companies seeking more efficient production methods, such as Japan's Lean Production System, as pioneered by Toyota in the 1980s (Car Keys , 2016), and/or finding new technologically innovative ways of boosting cars' performance and safety, i.e. Volvo's commitment to auto-breaking system to be in-built in every one of their models starting from 2015 and is further committed to eliminate crashes altogether by 2020, to both stay one step ahead and differentiate themselves in their market. (Stocksdale, 2017)

As a consequence, pro-active and long term sustainability-focused corporate organization leadership is required, as well as respected, trusted, enthusiastic and fully committed team of top tier management that actively participates and further promotes two-way communication with all of its diverse groups of stakeholders. (Bruijl, 2017) As with most many large organizations, where there's smoke there's typically fire. Mistakenly, when such organizations lose oversight and disregard the bigger picture, and get bogged down on pleasing some stakeholders at others' expense; or whose vision translates into pursuing arbitrary short-term goal, i.e. reaching status of being world's #1 in terms of cars sales; or simple short-term profit maximization at any cost, as some of which can be seen in Volkswagen's emission scandal, can lead to problems that are detrimental to the company in the long-term.

The scandal appears to be the case that long-term problems at the company's top of the chain of command and corporate governance structure of VW, and reached critical point when its, now former, CEO Winterkorn, whether unknowingly or perhaps knowingly, had direct impact on company's approach to its emission in a series of models of diesel cars. Take, for example, how various former executives under Winterkorn's corporate leadership described his managerial approach as "authoritarian", "autocratic", and that he had a non-constructive tendency to be "surrounded largely by yes-men", whilst the rest of organization were operating under "climate of fear" that went without any checks and balances due to organization's top-down structure,

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which even for Germany's long-standing auto industry, is an anomaly for doing business in the 21<sup>st</sup> century. (Ewing, 2015)

In hindsight, it's clear that organization's structure, under Winterkorn, but not limited just to his stewardship of VW, has been of top down nature, underlying what is often referred to as *silo mentality* - where decision-making was predominately in the hands of its senior managers and a handful of key advisory board members. (Handelsblatt Staff, 2018) Such structures are typically bound to be slow in responding to, especially rapid, changes occurring in the marketplace, as well as vulnerable to the blind spots. (Bruijl, 2017) Of course, the silo mentality can be reformed down the line, even in large global organizations, and retaliated against by i.e. flattening highly hierarchical structuring, introducing sense of shared goals, as well as focusing on bumping up internal communication and networking efforts (Gleeson, 2017). However, once unethical behaviors have already been exhibited, detected and as a consequence widely publicized, there will inevitably be individuals, or groups of people, that will end up being the unfortunate scapegoats of neglected internal problems within an organization. (Bruijl, 2017)

In Dieselgate's case, the conventional thinking points out to the obvious scapegoats, which were customers and shareholders who were victimized by VW's deceptive practices, ending up with falsely advertised as 'Clean Diesel' automobiles that were far from clean, and put them, and likely other people around them, at health risk, as well as investors who experienced the value of their held shares tumble, virtually overnight, with no end in sight of future rebound, or not whether the corporation will even exist in couple of years time. (Rechtin, 2016)

There is a strong case to be made that in today's highly competitive and globalized business environment in order, not just to "meet the payroll" and survive, and meet some arbitrary short term profit metric, the companies must have a forward-looking vision for sustainable growth over time, and have strategic toolbox that will make possible for them to make that vision a reality. The bigger the organization, the more divisions and brands it oversees, and in increasingly more multinational markets, the more difficulty and complexity this entails in order to maximize its sustainable profit-making enterprise. Complex systems breed more complexity, vulnerability to ever increasing and greater scale and impact of threats when

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any part, or combination of factors, of that system fails, this doesn't mean that the company is helpless and has no control of how to manage the risks or even turn them into a learning opportunity that will ultimately help them achieve value creation and further growth.

Whether large or small, every organization, has a certain number and different subsets of stakeholders. Those stakeholders hold an interest in what the company is doing, often going beyond whether or not the company is profitable at any given time. The sheer number of such interested parties, and the scale of their stake in the organization multiplies as the company continues its operation with substantial growth over time, and geographical boundaries. Ultimately, that's a good thing – such expansions, especially in a free market environment, is an indicator that the organization has tapped to and properly executing a successful business model that adds value to many of its stakeholders. The larger the scale, the impact and reach on these stakeholders the firm has, the more powerful it becomes, but that power can only be sustained and exponentially increase with time so long as the stakeholders that hold different degree and nature of interest in the organization perceive you as powerful. With greater power comes great responsibilities, and on top of the list of those responsibilities for any enterprise is to maintain its organizational reputation, while spending energy and limited resources on improving its standing with the stakeholders.

Maintaining a certain level of stakeholder goodwill towards the company is not an easy feat, but can be achieved, especially if done in a systematic manner, with a clear vision and strategy in the heart of the organization that has objective metrics used by the company to measure the current state of reputation, what metric they are trying to reach and by what time, and a strategic game-plan on how to get there. In the real-world situations, this is easier said than done. Especially, in highly complex organizational structure, such as in the case of Volkswagen AG multinational, there are virtually unlimited moving parts, and it's at least understandable that top management of such firms might lose "the plot" by deviating from having the Big Picture in mind, and get bogged up in day-to-day operations, while pursuing some short-term, and sometime arbitrary metric of performance or deadline.

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How is it then that, depending on whom you ask, the world's second largest (depending on methodology you use to derive to that number) automaker would make such high risk decision to put their auto empire on the chopping block, by willfully, and for at least a decade, participate in a conspiracy to defraud, not just the jurisdictions where they were competing for market share, but also most of its stakeholders throughout the globe?

Evidently, whether it's Dieselgate in Volkswagen AG's case, or any other organizational crisis, as a general rule is understood to be a symptom of much greater problem, not the disease. The finding in this case study, do a great deal to point out that this was certainly the case with Volkswagen's not just the corporate governance just before and at the time of the crisis, but deep down inside Volkswagen AG's long-term culture, even from its very founding and long history. Crisis, no matter how great, are both costly and to some degree manageable, organizational culture – which drives company's vision, strategy, and short term tactics - takes incredible effort for prolonged period of time to uproot and change. In practice, many once reputable organizations failed at the latter, as their attempts of corporate culture restructuring was largely superficial, resulting in nothing more than 'rearranging the desk chairs on the Titanic'.

Indeed, when case study looks through literature review, it finds countless red flags, stakeholder drivers and outspoken voices, even from within the organization, that were clamoring for very fundamental change in company's culture, which translates into how Volkswagen treats its stakeholders, but also which stakeholders' interests it tends to with more focus and care, and by what objective standard and who decides what those key stakeholders are.

Before putting these concepts for analysis, it is important to note that especially in cross-border operating, and highly complex corporations, having a singular "corporate culture" could be elusive feat. Having a relatively successful overriding corporate culture is especially harder task. According to Harvard Business Review, such culture would revolves around a clear vision – which often will appear on company's annual statements as manifesto or marketing campaigns; values – which often are set of ethics that company

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proudly adheres to and that guide them towards making their vision a reality; practices – are more concrete methods by which those values are being implemented in company's strategy; "people" – are partners who practice same values and add value to company's overreaching vision. Though a helpful roadmap to follow, what might be missing breakdown of corporate culture, is core corporate strategy. That is answering the basic question "what business are we in?", and projecting the answer through vision.

More concretely, strategic management is guideline for direction to a corporation like Volkswagen AG and entails systematic approach to determining and make explicit to the rest of the organization and its stakeholders, the objectives behind corporate governance, while the executive body develops plans and puts forth concrete practices in order to achieve such objectives. Only after corporate vision and strategy's objectives are solidly grounded can allocation of financial and human resources can take place, in order to implement the grand plan.

The red flag in Volkswagen corporate's case is either lack of unifying strategic management objective, or what more appears to be the case, misguided approach of pursuing different strategic objectives. Such as, presenting the corporation objective as satisfying all its stakeholders, while in practice failing and alienating many of its core stakeholders at the great expense of others leading up to statements and actions by top management during, still ongoing, Dieselgate scandal.

As was uncovered in the analysis, there is truism that when a company, and specifically its top executive body, are responsible to virtually everybody (that is stakeholders), it often results in management that in practice is unaccountable to no one, largely driven by personal vision, goals, and ethical compass. As in Volkswagen's case, and not exclusively when it was managed under its controversial and disgraced CEO Winterkorn, the company was rigidly hierarchical, operating in mostly self-inflicted echo-chamber and in the atmosphere of fear and conflict of interests, largely devoid of truly independent parties with power to be more just than whistleblowers to the press and government authorities, but to influence the corporate governance's transition to superior corporate conduct.

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As an unintended result of Volkswagen costly emission scandal, it opened up a can of worms in core corporate culture within the firm, and some positive changes were already implemented to fundamentally change the company's vision and strategy to sustainable growth. Among these, to replace the "insider" CEO Matthias Muller with Herbert Diess, as recently as August 2018, who have somewhat outsider perspective that comes with experience of working at Bosch and overseeing corporate restructuring at BMW. (Amaro, 2018)

According to head of autos research at BMI Research, the firm has "too many layers of control to make any decisions because of the big family shareholdings" (Amaro, 2018). So, when it comes Porsche-Pieche family clan's stronghold on corporate ownership and family rivalry affecting direction and effectiveness of the company's corporate governance, that still will be the case, though younger and more dynamic family members will take the wheel at the supervisory board going forward. The directors board, itself, will be expanded from six to 10 members, opening up an opportunity for the corporate governance to move away from its echo-chamber status quo, to possibly having more diverse thinking behind its decision-making.

These, and other, structural changes are also reflected in Volkswagen's "Together" 2025 strategy, and a corporate vision summed up as "to become a world-leading provider of sustainable mobility. The path there will be dominated by harmonious coexistence and exchange as equals. For one reason: new times call for new forms of collaboration." (Volkswagen AG, 2018) In more practical terms, the firm is shifting gears from being heavily invested in diesel technology, and pivoting toward fully electric and hybrid vehicles, as well as making concrete steps to invest in next generation solid-state batteries, that will enable electric vehicles to have more of a mass market appeal, as a viable relatively clean alternative at a price level more people will be able to afford.

Fitting to what VW leadership embarked on, Elon Musk once famously quipped "everything works on PowerPoint. You know, I could give you a PowerPoint presentation about teleportation to the Andromeda Galaxy. That doesn't mean it works." (Heisler, 2017).

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Therefore, only time will tell whether VW restructuring measures post-Dieselgate, and its pivot away from its diesel car-cantered operations to solid-state run battery cars business model will reap rewards for the company and majority of its stakeholder and their interests in such a feat succeeding.

What is known, and what was carefully studied in this paper is that as a result of emissions crisis, the already shaky reputation of VW have been heavily tarnished. When the shares are down, the reputation is the intangible asset that safeguards that the company can still recover and have sustainable long-term growth in spite of short-term loss or tactical misstep. When all said and done, VW appears to understand this, and does, on some level, appeal to goodwill of its stakeholders. In more fundamental ways, if the “strategy” and underlying objective of the company to become “number one” global automotive provider, spearheaded by Porsche family, especially under Ferdinand Piech’s stewardship, and a goal trickled to CEOs, like Winterkorn, under whose leadership VW ended up embroiled in largest corporate scandal the world have seen in past decade, then it’s a culprit behind the VW toxic corporate culture, and the misdeeds and scandals that followed them.

Overcoming Toyota in terms of sales or reaching “number 1” status in the market position, although an admirable threshold metric to reach for is not a strategy, in of itself, that spells sustainable value creation. At best, it’s a result or an outcome of a winning strategy. At worst, it’s a short-term goal that leads to short-term profitability at the expense of long-term sustained value maximization. The study, then, suggests that such misguided approach might have been deeply rooted in theoretical underpinnings of VW corporate culture.

VW, as well as many other corporate entities, at their core corporate culture built a strategy, that also affected its vision, around stakeholder theory. As Michael Jensen perfectly illustrated, that such theory leaves corporate executives with an objective that makes it highly unlikely for those managers to make decisions that lead to sustainable success of the organization they oversee, since the balancing of all, often competing, stakeholder interests, though not impossible, becomes highly unlikely in a complex organization. Also noting that the reason stakeholder theory pervades over time it’s because it’s more convenient to many

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top managers, leaving the decision-making largely to their own devices, due to stakeholder theory's in-built mechanism on how to align all stakeholders' separate interests, under unified vision, strategy, and tactics that (theoretically) will benefit everyone.



Figure 9: Martin Winterkorn on The cover of Forbes in 2013. Image courtesy of Peter Rigaud;



Figure 10: Volkswagen "Das Auto" launched in 2007 and discontinued in 2015, image courtesy Volkswagen AG

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Overseeing VW during the time when it surpassed Toyota as world's #1 seller of automobiles might motivate someone like Mr. Winterkorn (see figure 9), or Mr. Piech, and the rest of Poesche family, to get up in the morning and go to work, and even go as far as conspire to cheat global environmental regulators. This short-term goal is only shared by few stakeholders at the top of chain of command and lacks proper guidance for uniting diverse stakeholders to want to be co-partners in a win-win strategy they can get behind. The infamous Volkswagen "Think Small" (see figure 2) campaign, its top management's thinking was "think big", a superior mindset is "think long term". In other word, having a vision of sustainable value maximization. Wouldn't this hurt the relationships VW supposed to have with their stakeholders? The paper findings suggests the opposite.

Enlightened value maximization takes the long-run to value maximization as its primary objective, and sustainably by making investments of corporation's resources and energy into carefully identified set of stakeholder groups, just so long as in doing so can be shown to translate into added value for the owners, which in turn will satisfy and energize the stakeholders of the firm, and in time will make it a reality for Volkswagen AG to put "Das Auto" slogan (see Figure 10) back next to its name, if not literally, then in the perceptions of its stakeholders.

The "bug" at Volkswagen then is its management strategy and vision, a vision that gets further blurred by the theoretical underpinning, as well as Germany's corporate governance system, including its co-determination ordinance and rules and assumptions behind corporate ownership concept – that has similar principles and in-built blind spots as stakeholder theory - that incentivizes German corporations like VW AG in their misguided approach to corporate governance.

It's not just that Volkswagen needs corporate culture revamp, which the study makes a thorough case for, but that entire German social market economy needs revisiting, and possible shakeup, to achieve its mandates and industry suggestions' intended goal for making "Made in Germany" brand to be reputable again.

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## 8. Conclusion

The Volkswagen's Emission Scandal provides a real life practical example of focus for greater topic of research on stakeholders, and stakeholder relationship in the crisis of a major corporation operating on worldwide international scale. The research has a great significance to the existing body of knowledge of stakeholder management because it deals with practical ramifications on those relationships when they are affected by theoretical approaches to corporate strategies. The research provides formulations of key definitions, and extensive body of knowledge of background on the the general topic as well as the particular case being analyzed in the case study.

The research objective rest on looking at systematic ways of identifying international corporations' stakeholders, analyzing, and prioritizing them for in-depth study, and with the focus on one of world's famous cases of international corporate crisis. Furthermore, the paper attempts to create new knowledge for corporations and international business academics by examining theoretical guidelines on how to build better stakeholder relationships, and avoid potential similar international crisis scenarios from occurring by creating and maintaining excellent relationships with stakeholders through pursuing shareholder value maximization.

The research paper does this by putting forth two case study relevant research questions to meet such an research object, and providing the findings to the following questions. Who were the most relevant stakeholders in the real-life international corporate crisis, and what were their expectations, motivations, roles, and strategies in such a crisis? From theoretical and practical approaches, and from a perspective of an international corporation what is the corporate objective to follow in order to ensure sustainable value maximization, and how such an objective could've either prevented Volkswagen's emissions scandal, or could help the repair of the reputation of the firm in the future?

The findings were revealing, and inter-related between two research questions posed. The shareholders, customers, and dealers were the key players in need of utmost focus and engagement efforts from the firm, especially as a result of diminished reputation brought forth by

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the emission scandal that ensued. Though, in Volkswagen case it made significant efforts towards repairing the relationship between customers and partners, the damage done to shareholders was grave enough that this key player was primary driver behind corporate-wide effort of changing decades old corporate culture, venturing into different business models, and looking to change it's corporate governance structure towards a more long term sustainability in mind. The case also provides in-depth study of the society as a vital stakeholder for corporations, especially as it encompasses, and not mutually exclusive, from other stakeholders such as customers, shareholders, and top management.

The secondary, but relevant to stakeholder relationship management, findings pointed out to what likely was the root cause of the crisis and deminished stakeholder relationship by Dieselgate, which the paper identified as the system of far greater structural problem not only at Volkswagen AG abnormal corporate structure, that breed toxic to stakeholder relationships corporate culture that spearheaded unaccountability within the top managers, as well highly consolidated, non-diverse and conflict-of-interest stricken shareholder structure was detrimental to its sustainable reputation standing with Volkswagen other stakeholders, as it was to its long term sustainable growth. The paper also finds a link between Germany's corporate governance, and how it might have adverse than intended effect on Germany based international corporations vis-à-vis keeping its shareholders happy, and overall improved stakeholder relationships. The paper looks at theoretical underpinnings corporate strategies, Shareholder Theory and Stakeholder Theory and pinpoints pros and cons in both, while settling on alternative Enlightened Value Maximization – a less widely accepted theory as the superior model for ensuring a corporate strategy that yields sustainable growth, and acts as safeguard for corporate crisis from taking place, and highly dependent on building superior stakeholder relationships, which in turn maximizes the returns for the owners, as the corporate reputation towards the stakeholders represents a large chunk of modern day corporation's total market value, and therefore such intangible assets is inseparable from international large firms overall sustained growth and success.

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