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Tough Stance by U.S. Regulators Deepens VW's Diesel Crisis

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The road Volkswagen AG must travel to get out of its U.S. legal and regulatory morass just got rougher.

The U.S. government erected a pair of roadblocks this week against the automaker, which admitted in September that it had rigged the software of its diesel cars to pass emissions tests. The Environmental Protection Agency said Monday that VW's proposals to bring its diesels into compliance with emissions standards have been inadequate. At the same time, the Department of Justice sued, raising the specter of multibillion-dollar fines.

The message to VW: It's going to take creative proposals to fix hundreds of thousands of cars, according to environmental lawyers and automotive analysts. It may take more money than expected to settle U.S. environmental claims. And even so, VW may yet face criminal charges, said people familiar with the U.S. investigation.

"They have to show the government that they're trying to do some good, otherwise they run the risk of getting pounded on the fines," said Daniel Riesel, a partner at Sive, Paget & Riesel, an environmental law firm in New York that isn't involved in the case. "They have to satisfy the EPA."

German Fix

In all, it's clear the German carmaker is facing a much steeper climb in the U.S. than on its home continent. The company won clearance for relatively [simple repairs](#) from [German regulators](#) last month, using software upgrades for some engines and, in others, installing a pipe capped by a piece of mesh to regulate air flow. Volkswagen estimated that repair would take less than an hour to complete.

“We are confident we will find good solutions for the affected U.S. vehicles,” Herbert Diess, the head of Volkswagen’s namesake brand, said at the Consumer Electronics Show in Las Vegas. “In recent weeks we’ve made significant progress.”

Volkswagen is proposing that some U.S. cars can be fixed with a simple software upgrade, while others will require hardware. Software upgrades are less expensive. But the EPA so far isn’t playing ball, saying on Monday that talks with the company on a recall haven’t produced “an acceptable way forward.”

“U.S. regulators have taken a tougher stance on this than in Europe, partly because emission regulations for diesel cars are tougher,” said Juergen Pieper, a Frankfurt-based analyst for Bankhaus Metzler. “In Europe the focus is more on carbon dioxide.”

BP Comparison

The automaker is facing lawsuits from state attorneys general in the U.S. and investigations in at least seven countries as well as hundreds of private lawsuits. The Justice Department’s lawsuit filed Monday outlines penalties that could reach \$46 billion, according to a Bloomberg Intelligence estimate. The actual penalties aren’t likely to be that high.

In some ways, the government is following a strategy that won it billions of dollars in settlements from BP Plc over the 2010 well explosion in the Gulf of Mexico that unleashed the worst offshore oil spill in U.S. history, said David Uhlmann, a University of Michigan law professor and former head of the Justice Department’s environmental crimes section.

With BP, the U.S. sued the company in December 2010 over pollution law violations, settling Clean Water Act claims last year for \$5.5 billion. That was part of a \$20.8 billion global settlement of state and federal civil claims.

That case didn’t preclude criminal charges against BP. The U.S. filed a criminal action against BP in November 2012, almost two years after the civil complaint. BP’s agreement to pay \$4 billion and plead guilty to 14 charges, including one misdemeanor count of violating the Clean Water Act, was announced the same day the criminal case was filed.

The Justice Department is seeking an order requiring Volkswagen to take “appropriate steps,” including mitigating nitrogen-oxide emissions. Such steps might include forcing Volkswagen to install equipment to reduce pollution or buy back vehicles from owners.

‘Truly Sorry’

“We disappointed our customers and the American people, for which I am truly sorry and for which I apologize,” Diess said at the Las Vegas trade show late Tuesday. “We are doing everything we can to make things right.”

Volkswagen is working with all government agencies and is developing an independently administered program to compensate consumers for their economic losses, spokeswoman Jeannine Ginivan said in an e-mail Monday.

The company has suspended sales of its diesel vehicles in the U.S. until the matter is cleared up. That resolution could include a penalty that addresses the environmental and public-health damages from VW's polluting cars and hefty enough to deter future cheating, said Luke Tonachel, a senior analyst with the Natural Resources Defense Council in New York.

"The Volkswagen scandal has shown U.S. regulations need to be tighter and our testing needs to be improved," while also showing that "European regulation doesn't really exist," said Daniel Becker, director of the Center for Auto Safety's Safe Climate Campaign.

Expensive Option

In addition to allowing higher levels of diesel pollution than permitted in California, the European Union has a history of testing vehicle emissions [less stringently](#) than its U.S. counterparts. The tougher standards in the U.S. may mean Volkswagen will have to accept the cost of buying back some or all of the vehicles to satisfy American regulators.

"We would argue that VW should go for the broadest and even most expensive buy-back option in order to restore customer and dealer relationships in the U.S.," said Arndt Ellinghorst, a London-based analyst with Evercore ISI. "The more VW spends on fixing its U.S. problems, the lower its legal charges will be at the end."

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