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13 UNITED STATES DISTRICT COURT
14 NORTHERN DISTRICT OF CALIFORNIA
15 SAN FRANCISCO DIVISION

16 IN RE: VOLKSWAGEN “CLEAN
17 DIESEL” MARKETING, SALES
PRACTICES, AND PRODUCTS
18 LIABILITY LITIGATION

CASE NO. 3:15-md-02672-CRB
Hon. Charles R. Breyer

19 **THIS DOCUMENT RELATES TO:**

**EXPERT REPORT OF HON. LOUIS J.
FREEH (RET.)**

20 *All Cases*
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Attached as Exhibit 1 is the expert report of Hon. Louis J. Freeh (Ret.).

EXHIBIT 1

Expert Witness Report
Hon. Louis J. Freeh (ret.)
December 2, 2019

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Assignment

I have been retained by the Knight Law Group (“Knight”) to provide expert testimony in the case entitled *In Re: Volkswagen “Clean Diesel” Marketing, Sales Practices, and Products Liability Litigation*, Case No. 3:15-md-02672-CRB (N.D. Cal. 2015) (“*Clean Diesel*”). The overall subject matter of my testimony is the plea agreement entered into between the United States and Volkswagen AG (“VW AG”) (signed January 11, 2017 and approved by the United States District Court for the Eastern District of Michigan at a hearing held April 21, 2017) in *United States v. Volkswagen AG*, Case No. 2:16-cr-20394-SFC-APP (E.D. Mich. 2016) (“*US v. VW AG*”) and the sentence imposed by the Court in that case, which was based upon, and adopted, the fine and other components of the plea agreement.¹

More specifically, I have been asked: 1) to compare the punishment and fine imposed on VW AG with the range of fines provided by the applicable Federal Sentencing Guidelines Manual (U.S. Sentencing Comm’n 2016) (“Sentencing Guidelines”); 2) to discuss other components of the sentence (which was based upon the Court’s acceptance of the plea agreement) and address whether those components of the sentence accurately reflected VW AG’s wrongdoing; 3) to opine on whether evidence in this case indicates that VW AG did not truthfully admit the full scope of its fraud in the plea agreement; and 4) whether VW AG is continuing to engage in wrongdoing by improperly selling cars that were the subject of the *US v. VW AG* plea agreement as “certified pre-owned” in violation of applicable law and the plea agreement.

Qualifications

- I served from 1981-91 as an Assistant United States Attorney, and later, Associate United States Attorney and Deputy United States Attorney, in the United States Attorney’s Office for the Southern District of New York from 1981 to 1991.
- In 1991, I was appointed by President George H.W. Bush to be a United States District Court Judge for the Southern District of New York.
- In 1993, I was appointed by President William J. Clinton as the fifth director of the Federal Bureau of Investigation and served until 2001.
- Since 2001, I have been in private practice.
- My complete bio is attached as Exhibit 1.
- Publications authored in the past 10 years:
 - Louis J. Freeh and José Hernandez, “Compliance-Monitor”, *Corporate Compliance*, 2016;
 - Louis J. Freeh, Gregory Paw, and Sergio Salerno, “New Italian Legislation Addresses Corruption”, 2012; and
 - Louis J. Freeh, “An Incomplete Investigation”, *Opinion Journal*, Nov. 28, 2012.

¹ I am not rendering an opinion concerning the United States District Court for the Eastern District of Michigan (Hon. Sean F. Cox)’s acceptance of the plea agreement. Any criticism of the plea agreement and sentence in *US v. VW AG* is not intended to be a criticism of the United States District Court for the Eastern District of Michigan which accepted the plea agreement and imposed a sentence in accordance with the terms of that plea agreement.

- Cases in which I have testified as an expert at trial or by deposition in the past 4 years:
 - 2017: Confidential testimony before the World Bank's International Centre for Settlement of Investment Disputes (ICSID);
 - 2016: *Wynn Resorts, Limited vs. Kazuo Okada et al.*, Eighth Judicial District Court in Clark County, Nevada (Case No. A-12-656710-B); and
 - 2015: *Thema International Fund PLC vs. HSBC Institutional Trust Services (Ireland) Limited, et al.*, Ireland High Court (Commercial) (Record no. 2009/3152P).

Compensation

In connection with the foregoing, I am being compensated by a flat fee of fifty thousand (\$50,000) for the preparation of this expert report, as well as the time spent reviewing and analyzing documents, testimony, and legal authorities underlying the report. Additionally, I will be compensated at the rate of \$1850 per hour (plus travel expenses) for any future testimony, deposition, consultation, along with related time and preparation. My compensation is not dependent on the outcome of this case.

Documents Reviewed

I reviewed the following documents:

- Sentencing Guidelines (attached as Exhibit 2);
- *US v. VW AG* Third Superseding Information (filed January 11, 2017) (attached as Exhibit 3);
- Plea Agreement in *US v. VW AG* (signed January 11, 2017 and approved by the United States District Court for the Eastern District of Michigan April 21, 2017) (attached as Exhibit 4);
- Transcript of *US v. VW AG* sentencing proceedings (dated April 21, 2017) (attached as Exhibit 5);
- VW AG Fifth Superseding Indictment (filed March 14, 2018) (attached as Exhibit 6);
- Email from Oliver Schmidt to Michael Horn and David Geanacopoulos (dated May 15, 2014) (attached as Exhibit 7);
- Applicable federal statutes, including 18 U.S.C. §§ 371; 542; 1512; § 3572 (attached as Exhibits 8-11);
- Plea Agreement of James Robert Liang in *United States v. Liang*, Case No. 2:16-CR-20394-SFC-APP (E.D. Mich. 2016 dated September 9, 2016) (attached as Exhibit 12);
- VW Group of America, Inc. ("VW America") Balance Sheet for 2017 (attached as Exhibit 13);
- Testimony of Michael Horn (President and CEO of VW America) before the House Committee on Energy and Commerce, Subcommittee on Oversight and Investigations, October 8, 2015 (attached as Exhibit 14);
- Cal. Civ. Code §§ 1792; 1795; 1791.1; 1790.1; 1794; 1770; 1780 (attached as Exhibits 15-21);
- Cal. U. Com. Code §§ 2714; 2715 (attached as Exhibits 22 and 23);

- Cal. Veh. Code §§ 11713.18; 11700.03 (attached as Exhibits 24 and 25);
- The Certified Vehicle Inspection and Condition Report from Seth Manders' vehicle (attached as Exhibit 26);
- vw.com printout re: CPO vehicles (attached as Exhibit 27);
- vw.com searchable CPO inventory (attached as Exhibit 28);
- autotrader.com article re: cost of CPO vehicles (attached as Exhibit 29);
- Exemplar Carfax report (attached as Exhibit 30);
- Consumer Class Action Settlement Agreement and Release filed July 26, 2016 in "Clean Diesel" (attached as Exhibit 31); and
- The complaint filed in *Manders v. Volkswagen Group of America ("Manders")*, Case No. 3:19-cv-07488 (N.D. Cal. 2019) (attached as Exhibit 32);
- The complaint filed in "Clean Diesel" (attached as Exhibit 33);
- The long-form notice regarding VE and Audi 2.0-liter TDI Diesel vehicles (attached as Exhibit 34); and
- The eligibility and modification status report for a 2015 TDI VW Jetta sedan (attached as Exhibit 35).

Expert Opinions re: VW AG's Sentence Under the Plea Agreement

- The plea agreement did not accurately calculate the applicable fine range pursuant to the Sentencing Guidelines.
- The fine imposed by the court in *US v. VW AG* (\$2.8 billion) was far below that which could have been imposed under the Sentencing Guidelines, USSG §8C2.5.
- The fine range resulting from a proper calculation under the Sentencing Guidelines should have been \$34,174,676,748 to \$68,345,353,496, which is 2-4 times the actual pecuniary loss of \$17,086,338,374.
- The Court accepted the fine agreed upon in the plea agreement entered into by the parties at a time when the involvement of upper management of VW AG and VW America in the underlying fraud had not yet been established. Therefore the sentencing Court did not apparently consider this important fact when imposing sentence.
- Neither the plea agreement, nor the fine imposed pursuant to that agreement by the Court, provided for restitution to the victims of VW AG's fraud.
- VW AG did not admit the full scope of its fraud in the plea agreement because it concealed the role upper management played in the underlying fraud. Whether this concealment was intentional or not, the sentencing Court was not aware of this important fact at the time of sentence.

- VW AG and VW America are continuing to engage in wrongdoing by improperly selling cars that were the subject of *US v. VW AG* as “certified pre-owned” cars in violation of applicable law and the *US v. VW AG* plea agreement. Obviously, this conduct and course of corporate dealing was not known or contemplated by the Court at the time of sentencing.

Executive Summary

In *US v. VW AG*, VW AG was charged in a Third Superseding Information (filed January 11, 2017) with three counts: 1) Conspiracy in violation of 18 U.S.C. § 371; 2) Obstruction of Justice in violation of 18 U.S.C. § 1512(c); and 3) Introducing Imported Merchandise into the United States by Means of False Statements in violation of 18 U.S.C. § 542. (Exhibit 3: *US v. VW AG* Third Superseding Information.)

On January 11, 2017, VW AG entered into a plea agreement with the Department of Justice and the United States Attorney’s Office for the Eastern District of Michigan under Federal Rule of Criminal Procedure 11. (Exhibit 4: VW AG Plea Agreement.) On March 10, 2017 VW AG pled guilty to all counts in the Third Superseding Information. (Exhibit 5: Transcript of *US v. VW AG* sentencing proceedings, p. 6:11-18.) At the sentencing hearing on April 21, 2017, the United States District Court for the Eastern District of Michigan accepted the plea agreement and imposed a sentence on VW AG consistent with the terms of that plea agreement. (*Id.* at pp. 25:17-31:21.) As part of the sentence, the Court imposed on VW AG the previously agreed-upon criminal fine of \$2.8 billion. (*Id.*)

The fine of \$2.8 billion was far below the minimum fine provided for by the applicable Sentencing Guidelines. Moreover, the calculation of the fine range in the plea agreement (\$17,086,338,374 to \$34,174,676,748) did not correctly calculate the potential fine. The range of fines imposed due to VW’s criminal conduct should have been 2-4 times the actual pecuniary loss of \$17,086,338,374, resulting in a fine range of \$34,174,676,748 to \$68,345,353,496.

Multiple factors set forth in the Sentencing Guidelines weighed in favor of a fine high within that range, given the offense level of VW AG’s conduct and the amount of actual loss. The actual pecuniary loss (from which the base fine is derived) was improperly reduced in the plea agreement from \$17,086,338,374 to half that amount (\$8,543,169,187) based on what the plea agreement characterized as the “litigation risk” of a contested sentencing proceeding. No such reduction is provided in the Sentencing Guidelines or by the case authority cited in the plea agreement.

Because the Sentencing Guidelines provide that fines should be adjusted upward given numerous policy factors present here (e.g., where the offense causes non pecuniary harm or impacts vulnerable victims, where the offender’s culpability score is higher than 10, where the offender has substantial financial resources, etc.), VW AG’s criminal conduct exposed it to a fine potentially more than 24 times greater than the amount of the \$2.8 billion actually imposed.

In addition, at the time of sentencing, the Court expressed concern that the degree of involvement by upper management in the underlying fraud had not been established. (Exhibit 5, p. 26:16-22.) Subsequently, the United States Attorney’s office for the Eastern District of Michigan indicted members of the VW AG upper management board, including Martin Winterkorn, former Chief Executive Officer of VW AG. (Exhibit 6: VW AG Fifth Superseding Indictment.) Also, in the class action case, “*Clean Diesel*,” evidence established that the CEO and general counsel of VW America perpetuated the fraud that was the subject of VW AG. (Exhibit 7: Email from Oliver Schmidt to Michael Horn and David Geanacopoulos.) So at the time of sentencing the Court was not aware that senior management of VW AG would later be shown to be participant in the conduct which was subject to the sentence imposed by the Court.

I understand that, in accordance with the Class Action Settlement Agreement and Release (Amended) in “*Clean Diesel*” dated July 26, 2016 (“Class Action Settlement”), Volkswagen repurchased certain TDI Diesel Vehicles from their owners. I understand that Volkswagen has been named as a defendant in *Manders*. (Exhibit 32.) Plaintiff in that action alleges that Volkswagen has unlawfully sold TDI Diesel Vehicles reacquired by Volkswagen pursuant to the Class Action Settlement as “certified pre-owned” vehicles, in violation of both California law and the provisions of the VW AG plea agreement, which prohibits Volkswagen from engaging in fraud in the sales and marketing of its vehicles. (Exhibit 4, p. 20, ¶ B.) Again, this course of conduct and corporate dealing by VW AG was not known to or considered by the Court at the time of sentence.

Underlying Facts and Analysis Supporting Opinions

1. Application of the Sentencing Guidelines

- a. The Sentencing Reform Act of 1984 (Title II of the Comprehensive Crime Control Act of 1984) delegated authority to the United States Sentencing Commission to develop guidelines to determine the appropriate range of sentences to impose for criminal offenses. The Sentencing Commission is currently empowered by 28 USC § 994.
- b. *United States v. Booker*, 543 U.S. 220 (2005) rendered the Sentencing Guidelines advisory in nature, stating that although district courts were not bound to apply them, courts must take the Sentencing Guidelines into account when sentencing.
- c. The district court, in determining the appropriate sentence in a particular case, must consider the properly calculated guideline range, the grounds for departure provided in the policy statements, and then the factors under 18 U.S.C. § 3553(a). *Rita v. United States*, 551 U.S. 338, 351 (2007). A sentence is presumed to be reasonable if it falls within a properly calculated guideline range. *Id.* at 347-48.

2. Methodology of calculating a fine pursuant to the Sentencing Guidelines

- a. When calculating a fine for an organization such as VW AG in a case such as *US v. VW AG*, the Sentencing Guidelines (specifically, §§8A1.2; 8C2) generally instruct courts to consider the following factors:
 - i. Offense level;
 - ii. Base fine derived from pecuniary loss;
 - iii. Culpability score; and
 - iv. Aggravating and/or mitigating policy factors.
- b. Here, the parties miscalculated the fine to be imposed on VW.
 - i. The parties correctly determined VW AG’s offense level (level 41).
 - ii. However, the parties incorrectly reduced the pecuniary loss amount by 50% based on “litigation risk [of a] contested sentencing proceeding” – a factor which is not acknowledged in the Sentencing Guidelines.
 - iii. The parties correctly determined VW AG’s culpability score (as a level 11) resulting in a multiplier of 2-4x the loss amount to be added to the base fine.

The Sentencing Guidelines provide that a culpability score of greater than 10 should result in the imposition of a fine on the higher end of the range. (Sentencing Guidelines §8C2.8.)

3. The parties correctly calculated the offense level.

- a. The calculated offense level 41 under §8B1.1 (with no criminal history points) carries the third-highest range in the applicable sentencing table, reflecting the extraordinary degree of criminality of VW AG's conduct.
- b. The only two higher sentencing ranges are 30 years to life (for level 42); and life (level 43).
- c. VW AG's offense level (41) would carry an imprisonment sentence of 324-405 months for an individual.

4. The base fine, derived from amount of pecuniary loss, should have been \$17,086,338,374.

- a. The base fine is equal to the pecuniary loss caused by the offense. (Sentencing Guidelines §8C2.4.)
- b. The plea agreement incorrectly stated that the pecuniary loss was \$8,543,169,187, only 50% of the actual loss. To effect this discount, the plea agreement relied on a factor not recognized by either the Sentencing Guidelines, or the authorities relied upon by the plea agreement.
- c. The plea agreement stated that the 50% reduction was "for the litigation risk that both parties would bear were there a contested sentencing proceeding," (Exhibit 4: Plea Agreement, p. 9 fn. 1), which is not a factor addressed in Sentencing Guidelines §2B1.1.
 - i. The commentary on downward departures under Sentencing Guidelines §2B1.1 does not support a reduction in loss amount for 'litigation risk.' Moreover, unlike 'trial risk,' it is not clear what the parties to the agreement meant when they referenced, without explanation, litigation risk related to "a contested sentencing proceeding."
 - ii. Nor do the authorities cited in the plea agreement support such a material reduction in loss amount for litigation risk.²

² In *US v. Giovenco*, 773 F.3d 866 (7th Cir. 2014), the offender engaged in a scheme to obtain city contracts reserved for "minority owned businesses" for his company which was not minority owned or controlled. The offender and his accomplices received approximately \$8.3 million over the course of three years through their small business for such fraudulently-obtained contracts. They were convicted of mail fraud. The court determined that the amount of loss was \$8.3 million (\$2.2 million net profit). However, the court's "downward departure" in sentencing was not in the amount; rather, following the Sentencing Guidelines §2B1.1, the court determined that, based on the amount, it would impose a 16 offense level increase, rather than a 22 offense level increase. The Seventh Circuit held the 16-level increase was within the district court's discretion, reasoning that the court has discretion to modify the amount of loss to more accurately reflect the economic realities of the crime. The court here did not modify the loss amount based on economic realities, but rather reduced the amount by 50% based on the "litigation risk" of a contested sentencing proceeding. "Litigation risk" is not mentioned in the grounds for a downward departure in *Giovenco*, nor can litigation pose an \$8.54 billion risk to the parties. It does not bear on the issue of culpability.

- d. Because the parties incorrectly reduced the amount of pecuniary loss by 50%, the base fine should have been \$17,086,338,374 instead of \$8,543,169,187.
- 5. The plea agreement failed to properly account for VW AG's culpability score (11) in determining the correct fine within the applicable range.**
- a. The range of the fine (as a multiple of the loss amount) under §8C2.5 is based on the culpability score (11) calculated under §8C2.1. The plea agreement correctly calculated the culpability score under §8C2.1, as follows (Exhibit 4: Plea Agreement, p. 9):
- i. base culpability score: 5
 - ii. the unit of the organization within which the offense was committed had 5,000 or more employees and an individual within high-level personnel of the unit participated in, condoned, or was willfully ignorant of the offense: +5
 - iii. obstruction of justice: +3
 - iv. the organization fully cooperated in the investigation and clearly demonstrated recognition and affirmative acceptance of responsibility for its criminal conduct:³ -2
- TOTAL: 11**
- b. Based on the culpability score of 11 (in the highest possible category), the minimum multiplier is 2x and the maximum is 4x the actual loss amount of \$17,086,338,374. (Sentencing Guidelines, §8C2.6.)
- c. The resulting fine range should have been \$34,174,676,748 to \$68,345,353,496, rather than the lower range agreed upon in the plea agreement of \$17,086,338,374 to \$34,174,676,748.
- d. Also, the plea agreement does not apply or acknowledge Sentencing Guideline §8C4.11, which provides for an upward departure in the case of "exceptional organizational culpability" (where an organization's culpability score is greater than 10).
- 6. Aggravating policy factors set forth in the Sentencing Guidelines clearly weigh in favor of a fine closer to 4x pecuniary loss, rather than 2x.**

In *US v. Prospero*, 868 F.3d 32 (1st Cir. 2012), the court adopted a loss figure of \$5.2 million, but specifically stated that it would not allow the loss figure to drive its sentencing decision, reasoning that the loss amount was an "unfair proxy for culpability." The offenders were convicted of mail fraud, highway project fraud, and conspiracy to defraud the government for providing noncompliant concrete and fabricating documentation to show that the concrete was compliant. The base offense level was 7. The loss amount increased the offense level by 18. The offenders received an additional increase of 4 levels for being organizers in the scheme, for a total adjusted offense level of 29. Given the lack of prior criminal history, the district court calculated it as 87 to 108 months imprisonment. However, the court adjusted the sentence to include no imprisonment based on the character letters, low likelihood of recidivism, and other similar factors. The court did not change the loss amount, but rather decided that it would not take it into consideration in part because the final project met specifications despite the nonconforming concrete. As such, this case does not serve as precedent for the court to lower the loss amount by 50% based on litigation risk.

³ As discussed *infra* Section 8, VW AG did not fully cooperate because it failed to disclose the involvement of upper management in the fraud.

- a. The fine to impose within the 2-4x range is determined by policy factors set forth in Sentencing Guideline §8C2.1.
- b. The relevant policy factors set forth in §8C2.1 include, *inter alia*:
 - i. the need for the sentence to reflect the seriousness of the offense, promote respect for the law, provide just punishment, afford adequate deterrence, and protect the public from further crimes of the organization;
 - ii. the organization's role in the offense;
 - iii. any collateral consequences of conviction, including civil obligations arising from the organization's conduct;
 - 1. If criminal and civil sanctions are unlikely to make victims whole, this may provide a basis for a higher fine within the guideline fine range.
 - iv. any non pecuniary loss caused or threatened by the offense;
 - v. whether the offense involved a vulnerable victim;
 - vi. any culpability score under §8C2.5 (Culpability Score) higher than 10;
 - vii. any factor listed in 18 U.S.C. § 3572(a); which include, *inter alia*:
 - 1. the defendant's financial resources;
 - 2. the burden the fine would impose on the defendant;
 - 3. any pecuniary loss inflicted on others by the offense;
 - 4. whether restitution is ordered or made and the amount of such restitution;
 - 5. the need to deprive the defendant of illegally obtained gains from the offense;
 - 6. whether the defendant can pass on to consumers or other persons the expense of the fine; and
 - 7. the size of the organization and any measure taken by the organization to discipline any officer, director, employee, or agent of the organization responsible for the offense and to prevent a recurrence of such an offense; and
 - viii. whether the organization failed to have, at the time of the instant offense, an effective compliance and ethics program within the meaning of §8B2.1 (Effective Compliance and Ethics Program).
- c. The foregoing factors weigh heavily in favor of imposing a higher fine within the 2-4x fine range, for example:
 - i. Environmental harm from the NOx emissions caused non pecuniary loss.
 - ii. Judge Cox, at the sentencing hearing, acknowledged the vulnerability of the victims:

1. “[I]t is the little guy who’s been hurt. First it’s the consumer . . . who’s not looking to buy a high-end car.”
2. “And again . . . the man or woman at VW who labors to make the car. Upper management is not going to take a big hit by the billions of dollars that this fraud has cost VW. But the labor at VW is going to lose millions of dollars, millions of euros in bonus money. . . . [A]s always when it seems to involve corporate greed, it’s the little guy that’s hurt, hurt the most.”

(Exhibit 5: Transcript of Sentencing Hearing, pp. 27-28.)

- iii. The culpability score is higher than 10.
- iv. Under 18 U.S.C. § 3572(a), a sentence can take into account the defendant’s financial resources (here, VW has massive financial resources, with Exhibit 13: VW America Balance Sheet for 2017 showing that as of December 31, 2016, VW America had assets totaling \$13,113,350,144), and whether the defendant can pass on to consumers the expense of the fine.
- v. The fine paid did not make restitution to the deceived purchasers. (Exhibit 5: Transcript of Sentencing Hearing, p. 8:2-6.)

7. The actual criminal fine imposed (\$2.8 billion) is substantially less than the lowest possible fine within the 2-4x fine range, when the fine range should have been \$34,174,676,748 to \$68,345,353,496.

- a. The plea agreement incorrectly reduced the base fine by 50% to \$8,543,169,187, when it should have been \$17,086,338,374;
- b. VW AG received an improper discount of 20% off the bottom of the applicable Sentencing Guidelines range reflecting its cooperation in the investigation (Exhibit 4: Plea Agreement, p. 11);
 - i. The plea agreement should not have applied this discount because VW AG failed to disclose that both its CEO and the CEO of VW America were involved in the fraud, as discussed *infra* Section 8, thereby defrauding the United States Attorney’s Office, and indirectly, the Court, into giving it a more lenient plea agreement.
- c. After application of the 20% discount, VW AG received a credit for \$11 billion, based on the present day value of a class-action settlement and a trust set up to remediate harm caused by the fraud. (*Id.*)
- d. However, even accounting for the \$11 billion credit, the correct fine range should have been \$23,174,676,748 to \$57,345,353,496.

8. At the time of the sentencing, Judge Cox of the United States District Court for the Eastern District of Michigan did not know that employees at the level of the VW AG Management Board were involved in the emissions-related fraud, but now it is clear that the fraud went to the top of the company’s hierarchy; thus, due to the company’s failure to disclose the extent of management’s fraud, the sentencing Court did not account for the criminal conduct reaching the highest levels of the organization.

- a. The Statement of Facts only implicated employees below the level of the VW AG Management Board.
 - i. VW AG was led by a Management Board that was supervised by a Supervisory Board. (Exhibit 4: Plea Agreement, Statement of Facts, 2-2, ¶ 1.)
 - ii. For the purpose of the Statement of Facts, references to “supervisors” are to “senior employees below the level of the VW AG Management Board.” (*Id.*)
- b. Judge Cox expressed concern related to this factor, as follows:
 - i. “This is a case of deliberate, massive fraud perpetrated by VW management. We don’t know how far up the corporate ladder it goes. Hopefully, the DOJ and probably more importantly, hopefully, the German government will do its duty and find out and prosecute those who are responsible for this massive fraud, this deliberate, massive fraud. . . .”

(Exhibit 5: Transcript of Sentencing Hearing, p. 26:16-21.)
- c. The Fifth Superseding Indictment in *US v. VW AG* filed March 14, 2018 demonstrates that the fraud underlying *US v. VW AG* went to the very top of the corporation. (Exhibit 6: Fifth Superseding Indictment, pp. 9-10.) However, those allegations, set forth below, were subsequent to the plea agreement signed on January 11, 2017, on which the Court’s sentencing proceeding was based.
 - i. Defendant Heinz-Jakob Neusser sat on the management board for VW Brand and was head of Engine Development for VW AG and supervised approximately 10,000 employees. (*Id.* at p. 9.)
 - ii. Defendant Martin Winterkorn was Chief Executive Officer and Chairman of the Management Board of VW AG. (*Id.* at p. 10.)
 - iii. Both defendants (along with others) conspired to conceal the defeat device from U.S. regulators. (*Id.* at pp. 11-26.)
- d. Facts uncovered during “*Clean Diesel*” have revealed that top executives of VW America appear to have been involved, which has not been accounted for by the plea agreement.
 - i. Specifically, on May 15, 2014 (shortly after the publication of a study revealing the vehicles’ inconsistent emissions performances), the Chief Executive Officer (Michael Horn) and general counsel (David Geanacopoulos) of VW America received an internal email from Oliver Schmidt, general manager of the Environment and Engineering Office of VW America, on the subject of the vehicles’ inconsistent emissions performances and “Possible Consequences/Risks” associated therewith. (Exhibit 7: Email from Oliver Schmidt to Michael Horn and David Geanacopoulos, p. 1.)
 - ii. The email referenced potential monetary penalties and costs of up to \$25.8 billion for buybacks of the vehicles. (*Id.* at p. 2.)
 - iii. The email also referenced as a potential risk regulators carrying out “their own engineering tests (defeat device testing/analysis).” (*Id.*)

- iv. In a section titled “Further course of action,” Mr. Schmidt suggests 3 alternatives, 2 of which involve refusing to answer questions from regulators or answering them without acknowledging the problem, in other words, not cooperating but rather obstructing any government investigation. (*Id.* at p. 5.)
- v. Mr. Horn and Mr. Geanacopoulos did not disclose the information in Exhibit 7 to regulators until after it was publicly exposed in September 2015. In September 2015, VW admitted to a defeat device in the 2.0 liter cars but not the 3.0 liter cars. This occurred when it became clear that the California Air Resources Board (CARB) was not accepting VW’s excuses and would not certify the 2016 model year TDIs. Audi did not admit a defeat device in the 3.0 liter TDIs until November 2015.
- vi. According to the plea agreement of VW America’s Leader of Diesel Compliance, James Robert Liang, VW America employees falsely and fraudulently continued to certify to the Environmental Protection Agency and the CARB that the vehicles complied with emissions standards until model year 2016. (Exhibit 12: Liang Plea Agreement, p. 6.) However, nowhere in the VW AG plea agreement or Mr. Horn’s Congressional testimony, (Exhibit 14), is there any mention that Mr. Horn and Mr. Geanacopoulos participated in the coverup.

9. VW America’s Certification of Pre-Owned Vehicles demonstrates Continued Wrongdoing.

a. Assumed facts

- i. I understand that Volkswagen has control over the certification for used vehicles that Volkswagen and its dealers are marketing as certified pre-owned (“CPO”).
- ii. I am informed by Knight that the CPO program is set up and managed by VW America through its authoring, publishing, and distributing a Volkswagen Certified Pre-Owned Program Manual to each of its dealerships.⁴
- iii. I am also informed by Knight that participation in a manufacturer’s CPO program is also usually defined in the franchise agreement with its authorized dealerships⁵. According to Volkswagen’s website:⁶

⁴ I understand that Knight does not currently have a copy of this manual since discovery has not occurred in the *Manders* case. The existence of such manual is referenced in Certified Vehicle Inspection and Condition Report from Mr. Manders in several places including the red text and the bottom left section of the checklist. That document is attached hereto as Exhibit 26.

⁵ I understand that Knight does not currently have the franchise agreement from *Manders* to provide, but intends to obtain it in discovery in *Manders*.

⁶ A print out of VW America’s webpage regarding CPO vehicles is attached hereto as Exhibit 27.

Volkswagen Certified Pre-Owned vehicles are put through a comprehensive, 100+ point dealer inspection. Should a car not perform according to our strict VW standards, we won't certify it until we can correct the issues – using Genuine Volkswagen Parts, of course.

Our 100+ Point Dealer Inspection process includes:

- Checking engine performance for starting issues, knocking, and vibration
- Checking transmission for performance malfunction or noise
- Testing brakes for proper function, stopping distance, and vibration
- Steering tests for noise, effort, vibration, and pulling
- Recommended or required maintenance updates

- iv. I am also informed by Knight that VW America requires its authorized dealerships to record the findings of the Certified Vehicle Inspection and Condition Report on a carbon copy form that is authored and distributed by VW America.⁷
- v. I am also informed by Knight that this form is then submitted to VW America to approve for certification under the CPO program.

b. Additional factual background

- i. According to VW America's website, in addition to an existing manufacturer's warranty, CPO vehicles are marketed and sold with an additional Comprehensive Limited Warranty, issued by VW America.⁸
- ii. Also according to VW America's website, CPO TDI vehicles model year 2016 and earlier are sold with a two-year unlimited-mile warranty.⁹
- iii. Once a vehicle has been approved by VW America as a CPO vehicle, it is advertised as a CPO used vehicle on both the Volkswagen authorized dealership's website and on the searchable CPO inventory on VW.com.¹⁰
- iv. Volkswagen markets their CPO vehicles as superior quality vehicles that have gone through rigorous inspection and testing.¹¹
- v. I understand that consumers are persuaded to purchase CPO vehicles based on representations of instilling confidence in well tested, reliable vehicles. As a result, it is my understanding that a CPO vehicle is generally sold for 20% more (on average, \$3,000.00 more) than a similar non-CPO vehicle.¹²

⁷ The Certified Vehicle Inspection and Condition Report from Mr. Manders' vehicle is attached hereto as Exhibit 26.

⁸ VW.com/certified-pre-owned/ website print out (Exhibit 27.)

⁹ VW.com/certified-pre-owned/ website print out (Exhibit 27.)

¹⁰ A print out of the vw.com searchable CPO inventory is attached hereto as Exhibit 28.

¹¹ VW.com/certified-pre-owned/ website print out (Exhibit 27.)

¹² An article published on Autotrader.com that shows the average increased cost of CPO vehicles is attached hereto as Exhibit 29.

1. I am informed by Knight that Volkswagen's Certified Vehicle Inspection and Condition Report is unique because it has several specific references to TDI vehicles. In the first pre-inspection checklist section, the dealership is required to mark "yes" or "no" to the statement "Vehicle is not a Manufacturer Buyback or was subject to a cash settlement. (Lemon Law)."¹³
 2. I am informed by Knight that Volkswagen's form is unique because it includes an "*" that states: "A TDI vehicle that was repurchased pursuant to a TDI Consumer Settlement Program is not considered a manufacturer buyback due to mechanical failure and state Lemon Law (see program manual for details)."¹⁴
- vi. The TDI class settlement agreement states: "After modifying a bought-back or returned Eligible Vehicle in accordance with an Approved Emissions Modification, Volkswagen may then elect to (i) resell the bought-back or returned eligible Vehicles in the United States, if properly labeled to disclose the Approved Emissions Modification."¹⁵ The class settlement agreement is silent on the issue of whether a manufacturer can market the vehicle as certified pre owned.
- c. If the foregoing is true, in my opinion VW America is still engaged in wrongdoing.
- i. Based on the information above, it appears that, without apparent factual or legal support, VW America has chosen to assume that the TDI class settlement did not qualify as a reacquisition of the TDI vehicles under federal or state warranty laws and expressly gave its authorized dealerships permission to market and sell the vehicles as CPO used vehicles in the face of California Vehicle Code section 11713.18.
 - ii. In *Manders*, the plaintiffs contend that identifying and marketing TDI vehicles as CPO is not only a violation of California Vehicle Code section 11713.18, but also a violation of the CLRA in that it is deceptive advertising. If true, then VW America is clearly still engaged in wrongdoing.

10. The Scope of Continued Wrongdoing.

a. Assumed facts

- i. I am informed that Knight conducted a search of Volkswagen dealership inventory available through both California dealership websites and Volkswagen America's website over the course of approximately a six month period during 2018 and 2019.
- ii. I am also informed that Knight specifically searched for diesel vehicles that were advertised as certified pre-owned vehicles.

¹³ Certified Vehicle Inspection and Condition Report (Exhibit 26.)

¹⁴ Certified Vehicle Inspection and Condition Report (Exhibit 26.)

¹⁵ Approved Settlement, section 4.4.3 (Exhibit M.)

- iii. From that search, Knight informs me that it took steps to confirm that the vehicles were, in fact, part of the Volkswagen class action buyback program.
- iv. I am informed that, to do this, Knight purchased and reviewed the Carfax report for the selected vehicles and identified only those vehicles which showed that title was transferred in Auburn Hills, Michigan during the buyback period following the class action settlement.
- v. I am informed that Auburn Hills Michigan was the headquarters for the class action settlement buyback program.¹⁶
- vi. I am informed that Knight's review revealed the following:
 1. 246 TDI vehicles advertised for sale in California as "certified pre-owned" vehicles which were originally sold in California and subsequently bought back under the Volkswagen class action settlement.^{17 18}
 2. 50 TDI vehicles advertised for sale in California as "certified pre-owned" vehicles which were originally sold outside of California and subsequently bought back under the Volkswagen class action settlement.¹⁹
- b. Assuming that these vehicles were reacquired by VW America under the Class Action Settlement pursuant to federal or state warranty law, and were thus ineligible to be "certified," it appears that VW America is continuing to engage in wrongdoing to this day.
- c. Taking advantage of a 'silent' class settlement agreement which does not address the issue of whether Volkswagen can market a TDI vehicle as 'certified pre-owned,' VW America has elected to sell CPO cars by unilaterally declaring in the Certified Vehicle Inspection and Condition Report (by using an * indicator), that a TDI vehicle repurchased pursuant to a TDI Consumer Settlement Program vehicles is "not considered" a 'manufacturer buyback' due to mechanical failure and state Lemon Law. Of course, this

¹⁶ An exemplar of the Carfax report with the Auburn Hills, Michigan reference highlighted is attached hereto as Exhibit 30, page 2.

¹⁷ I am informed that Knight found an additional 81 vehicles being marketed as certified pre-owned that were arguably class vehicles based on their year, make, and model, but that Knight was unable to confirm the Auburn Hills transfer on the Carfax report. I am also informed that, in Knight's experience, Carfax reports do not always contain complete information (and have a disclaimer that states such). Accordingly, some or all of those 81 vehicles could have also been bought back under the Volkswagen class settlement, but without doing a further inquiry, Knight was unable to confirm that fact.

¹⁸ I am informed that Knight has the supporting documentation of the 246 California vehicles. I am also informed that Knight has a print out of the website advertising the vehicle as "certified pre-owned" and the Carfax report showing the original California purchase location and the Auburn Hills, Michigan class settlement title transfer. A sample of an advertisement and Carfax report from this group is attached hereto as Exhibit 30.

¹⁹ I am informed that Knight has the supporting documentation for the 50 vehicles initially purchased out of state, reacquired under the Approved Settlement, and now marketed for sale in California.

is VW America's conclusion and does not appear to have been confirmed by any state or federal regulator or law enforcement official.

Under this convoluted disclosure, the ordinary purchasers of a TDI now 'certified' used vehicles would not have reason to know that their purchases were previously fitted with a Volkswagen 'defeat device.' Therefore it appears that the marketing and sale of these TDI vehicles is at least in violation of California law. Under the California Consumers Legal Remedies Act (CLRA), for example, a vehicle cannot be sold to a consumer by "misrepresenting the source, sponsorship, approval or certification..." (California CLRA, Sec.1770 (a)(2)). Additionally, under the California Vehicle Code, Sec. 11713.18, a car cannot be sold as 'certified' it is "reacquired" by the automaker in compliance with federal or state warranty law. Volkswagen, deciding that the TDI vehicles are not a "manufacturer buyback," fails to accurately disclose the source for these cars being sold, or the relevant history which a consumer is entitled to know. Therefore this conduct by VW America and its authorized dealers, in my opinion, constitutes deceptive sales practices and wrongdoing given all the facts and circumstances. This is precisely the concerns which Judge Cox expressed regarding the Volkswagen 'culture,' which was the source of its sentenced criminal conduct.

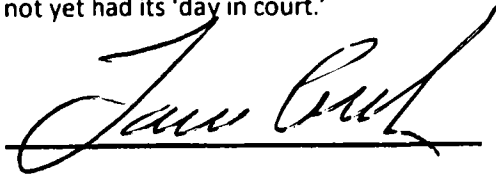
Conclusion

The Hon. Sean F. Cox imposed sentence on defendant Volkswagen AG on April 21, 2017 in United States v. Volkswagen AG, after the defendant pled guilty under a January 11, 2017 plea agreement with the United States Department of Justice. Judge Cox rightly relied upon the potential fine calculations and offense severity level set forth by the Government and the Defendant in the written plea agreement. Based upon my review of the said agreement, the relevant Sentencing Guidelines and the facts relating to Volkswagen's criminal conduct, the base potential fine as well as the offense severity were incorrectly calculated and stipulated to in the agreement. And while 'downward departures' are appropriately utilized by both the Government and the Court to reduce a potential sentence, here the Government mistakenly limited the Defendant's potential criminal exposure by citing a 'sentencing litigation risk,' which is not only unexplained, but is not a proper downward departure factor under the Sentencing Guidelines. Similarly, the offense severity category was misstated.

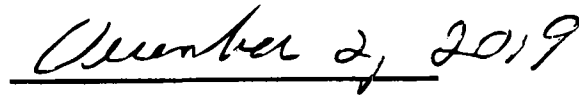
More importantly, the full scope of Volkswagen's criminal conduct at the time of sentencing, and directly related to the charges to which it pled guilty, was not known to Judge Cox. At sentencing, Judge Cox noted his concern that the "deliberate, massive fraud perpetrated by Volkswagen" had not been fully disclosed: "We don't know how far up the corporate ladder it goes. Hopefully, the DOJ and probably more importantly, hopefully, the German government will do its duty and find out and prosecute those who are responsible for this massive fraud... (Exhibit 5 at 26). As explained in this report, events subsequent to the sentencing disclosed that the criminal conduct supposedly sanctioned at the April 21, 2017 sentencing was not fully revealed to the Court, and that other senior leaders of the company's Management Board were complicit. Whether these facts were intentionally or negligently concealed from Judge Cox, Volkswagen certainly enjoyed more favorable sentencing circumstances than the then existing facts entitled it to have.

Finally, as set forth in this report, well after sentencing in the criminal case, Volkswagen has continued to engage in wrongdoing by improperly selling cars in the United States which were the subject of the plea agreement as "certified pre-owned," in violation of applicable law and prior agreements. Judge Cox was particularly concerned about Volkswagen's willingness to continue its corporate misdealing even after the imposition of the criminal penalties: "I've considered the need to protect the public from further crimes by the defendant. Yes, Volkswagen has a lot to do to adjust its corporate culture from what I've learned, which it is doing...and I don't think Volkswagen, at least, will be in this type of situation again." (Exhibit 5 at 29.)

Despite the 2017 criminal sentence, and the Court's hope for future changed conduct, and based upon incorrect sentencing calculations and concealed evidence at sentencing, plus willful post-sentencing corporate misconduct, the full measure of justice for Volkswagen's deliberate, massive fraud has not yet had its 'day in court.'



Louis J. Freeh



Date