

ACCOUNTING in the headlines

Which contingent liabilities resulting from the Volkswagen (VW) emissions cheating scandal would be recognized or disclosed in Volkswagen Group's financial statements?

Volkswagen manufactures the iconic Beetle in addition to other models including the Passat, the Jetta, and others. Volkswagen Group ([VW](#)) has been embroiled in an emissions cheating scandal discovered in 2015. Essentially, what happened is that VW's engineers developed and inserted software in VW car engines to cheat on the emissions testing process, making its cars seem much more emission-friendly than they actually are.

The VW engine software decides if the car is being tested by monitoring the car's speed, its engine operation, air pressure in the engine area, and the position of the steering wheel. If the software detects a testing situation, the software will adjust the engine performance, causing the emissions to be much lower than with normal engine performance. If the car were to be driven using the lower parameters, its driving performance would be greatly reduced.

The emissions adjustments are not minor. The VW car engines can emit nitrogen oxide pollutants up to 40 times above what is allowed in the US.

VW has admitted that up to 11 million vehicles worldwide have the cheating software. In addition, in November 2015, VW said it had also found "irregularities" in testing to measure carbon dioxide emissions levels in some VW gas-engines. These discrepancies could affect 800,000 gas-engine vehicles in Europe. Until November, only diesel engines had been implicated.

VW has announced that it is going to be giving every US VW owner a \$500 voucher good at its dealer stores. In addition, each owner will receive a \$500 VISA gift card that can be used anywhere.

VW is facing lawsuits from multiple class action lawsuits. Some of these lawsuits are seeking damages from the reduced resale value of the VW cars post-emissions scandal. Others are related to reduced efficiency and increased eco footprints of the vehicles.

The Environmental Protection Agency (EPA) in the US has the power to fine the company \$37,500 for each vehicle that does not meet emissions standards (maximum about \$18 billion dollars.) The IRS can fine VW for the tax credits that were awarded to car purchasers (the cars originally qualified for certain fuel-efficiency credits, but would not meet the tax credit standards with the true emissions levels.)

The Federal Bureau of Investigation (FBI) has opened a criminal probe of the VW emissions matter. In addition, several European regulatory agencies are investigating VW for violations.

Note: Volkswagen Group is a multinational company based in Germany. It prepares its financial statements in accordance with International Financial Reporting Standards (IFRS.)

Questions

1. What contingencies can you identify stemming from the VW emissions scandal?
2. Sort the contingencies you listed into two categories: probable and possible. (For the purpose of this question, "probable" is defined as "more likely than not," which means that the chance is more than 50% that this contingent event will occur.) Which set of contingencies would VW Group recognize or disclose in its financial statements?

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