

Volkswagen Dieselgate: Groupthink, Loss Aversion, and Moral Licensing in Collective Decision Traps

How Organizational Architecture Enables Systemic Institutional Deception

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ABSTRACT

In September 2015, the US Environmental Protection Agency revealed that Volkswagen AG had installed defeat device software in approximately 11 million diesel vehicles worldwide, enabling the vehicles to detect emissions tests and artificially reduce pollutant output during testing while emitting up to 40 times regulatory limits under normal driving conditions. Total costs to Volkswagen exceeded \$30 billion; criminal charges were brought against executives across multiple jurisdictions. This paper examines the Dieselgate scandal as a case study in collective decision traps — specifically, the interaction of groupthink, loss aversion, and moral licensing in hierarchical organizations under sustained competitive pressure. Drawing on Janis's groupthink framework, Kahneman's prospect theory, and Ariely's research on moral licensing, we argue that the defeat device decision was not the product of individual malice but of an organizational decision architecture that systematically suppressed dissent, amplified commitment to failing strategies, and provided ethical cover through an identity of technical excellence. The case offers a framework for understanding how organizations with strong ethical reputations become capable of systematic institutional deception.

Keywords: Volkswagen Dieselgate, groupthink, moral licensing, loss aversion, organizational silence, defeat device, collective decision traps

1. INTRODUCTION

On September 18, 2015, the United States Environmental Protection Agency issued a notice of violation to Volkswagen AG, alleging that the company had installed software — subsequently termed a 'defeat device' — in diesel-powered vehicles that enabled the vehicles to detect when they were undergoing standardized emissions testing. During such tests, the software activated full emissions controls; under normal driving conditions, emissions controls were substantially reduced, allowing the vehicles to emit nitrogen oxides at levels up to 40 times the US regulatory limit.

The affected fleet comprised approximately 11 million vehicles worldwide, spanning multiple Volkswagen Group brands including Volkswagen, Audi, Porsche, SEAT, and Skoda. US federal settlements included \$14.7 billion in consumer compensation and \$4.3 billion in criminal and civil penalties under the Clean Air Act; global total costs exceeded \$30 billion. Criminal charges were brought against executives in multiple

jurisdictions, and then-CEO Martin Winterkorn resigned within days of the EPA announcement.

The immediate narrative framing of Dieselgate as a case of deliberate corporate fraud, while accurate as a legal characterization, is insufficient as an organizational explanation. Internal investigations and subsequent legal proceedings revealed that the defeat device was not the product of a single decision by senior leadership but of a decision process that unfolded across multiple organizational levels over nearly a decade. This paper examines the organizational mechanisms — groupthink, loss aversion, and moral licensing — that enabled a company with a century-long reputation for engineering integrity to systematically deceive regulators on a global scale.

2. BACKGROUND: CLEAN DIESEL AND COMPETITIVE STRATEGY

In the mid-2000s, Volkswagen AG developed an ambitious growth strategy targeting the US market, where the company had historically held a marginal share. Central to this strategy was the 'clean diesel' proposition: a marketing position arguing that modern diesel technology could deliver superior fuel economy and performance while meeting stringent US emissions standards — advantages that would differentiate VW from dominant US and Japanese competitors.

The technical premise of the strategy was, from the outset, problematic. Meeting both US emissions standards and the performance and fuel-economy targets required by the marketing strategy simultaneously was technically infeasible within the cost parameters Volkswagen had established. Engineers communicated this constraint to management. The response was not to revise the strategy but to require a solution — an instruction that, under the prevailing organizational culture, was understood not as an invitation to raise fundamental objections but as a directive to find a technical workaround.

The defeat device software — developed by engineers within the organization and implemented without, according to subsequent investigation, explicit authorization at the most senior leadership level — was the result of this dynamic. The organizational system had created conditions in which finding an illegitimate solution was less costly, for the individuals involved, than acknowledging that the legitimate solution did not exist.

3. THEORETICAL FRAMEWORK

3.1 Groupthink and the Suppression of Dissent

Janis's (1972) foundational research on groupthink identifies a cluster of symptoms characteristic of cohesive, high-performing groups facing decisions under pressure: illusions of invulnerability, collective rationalization, belief in the inherent morality of the group, stereotyped views of out-groups, pressure on dissenters, self-censorship, and illusions of unanimity. The absence of explicit dissent is interpreted as consensus.

Volkswagen's organizational culture exhibited several of these features with particular clarity. The company's internal culture — shaped by decades of engineering success, strong union representation, and concentrated ownership — was characterized by high cohesion and explicit normative pressure toward organizational loyalty. Dissenting voices faced social costs that were real and well understood. Internal emails subsequently disclosed during US legal proceedings showed that some engineers had expressed reservations; these reservations were not escalated through formal channels and did not alter the organizational trajectory.

Morrison and Milliken's (2000) organizational silence framework provides a complementary explanation: when employees believe that raising objections will not lead to change and may damage their standing, silence becomes the rational response. The organizational condition that produced silence at Volkswagen was not unique — it is structurally produced whenever the costs of dissent exceed the perceived probability of influence.

3.2 Loss Aversion and Commitment to a Failing Strategy

Kahneman and Tversky's (1979) prospect theory, and Kahneman's (2011) subsequent synthesis, establish that loss aversion — the asymmetric weighting of potential losses relative to equivalent gains — is a robust and predictable feature of human decision-making. At the organizational level, loss aversion produces a systematic tendency to escalate commitment to established strategies even as evidence of their failure accumulates.

By the time the defeat device was implemented, Volkswagen had made substantial investments — financial, reputational, and strategic — in the clean diesel proposition. Reversing course would have required acknowledging that the strategy was fundamentally flawed, that significant engineering resources had been misdirected, and that the US market growth ambitions were unachievable on the proposed timeline. The psychological and organizational cost of this acknowledgment — experienced as a loss — exceeded, in the subjective calculus of those involved, the cost of the workaround.

Tversky and Kahneman's (1981) framing research adds a further dimension: the decision to implement the defeat device was not framed internally as 'shall we commit fraud' but as 'how do we solve the technical problem that is blocking our strategy.' The framing determined the option set that was considered, and excluded from deliberation the option of abandoning the strategy itself.

3.3 Moral Licensing and Engineering Excellence

Ariely's (2008) research on moral licensing identifies a mechanism by which prior positive moral behaviour creates a subjective sense of ethical credit that is subsequently drawn upon to justify ethical compromises. The logic is not explicit — individuals do not consciously think 'I have been good, therefore I can be bad' — but operates as an implicit relaxation of ethical vigilance following behaviour perceived as virtuous.

Volkswagen's century-long identity as a manufacturer of engineering excellence — durable, reliable, technically superior products — functioned as precisely this kind of moral license. The implicit reasoning was: 'A company that makes cars of this quality, that has served customers this reliably for this long, cannot be doing something fundamentally wrong.' The engineering excellence identity did not merely coexist with the defeat device decision — it actively provided the ethical framework within which the decision became rationalizable.

This mechanism also explains the persistence of the deception once implemented. Each year of apparent regulatory compliance without detection reinforced both the organizational confidence that the workaround was manageable and the moral licensing effect that made reversal seem unnecessary.

4. THE ORGANIZATIONAL ARCHITECTURE OF SYSTEMIC DECEPTION

A feature of the Dieselgate case that distinguishes it from simpler fraud narratives is the apparent absence of a single decision point at which the organization made a deliberate choice to deceive regulators. Legal proceedings established that the defeat device software was implemented, modified,

and extended over approximately nine years, across multiple vehicle platforms and markets, by teams of engineers and managers who operated with different degrees of explicit awareness of what the software did.

This distribution of knowledge and agency is characteristic of what organizational scholars term systemic deception — institutional dishonesty that is maintained not through a coordinated conspiracy but through a division of moral labour in which no single actor bears full responsibility for the aggregate outcome. Each individual actor could rationalize their contribution as a small technical decision within their domain; the ethical character of the total system was visible only from perspectives that the organizational structure did not create or reward.

The board's limited oversight of the technical specifics of the defeat device — a limitation that has legal as well as organizational dimensions — is consistent with this pattern. Governance structures that concentrate technical oversight within engineering functions, without creating cross-functional mechanisms for ethical review of technical decisions with regulatory implications, are structurally unable to detect this class of organizational failure.

5. OUTCOMES AND INSTITUTIONAL CONSEQUENCES

Following the EPA announcement, Volkswagen's share price fell approximately 35% in the two trading days of September 21–22, 2015, erasing roughly €26 billion in market capitalization. US federal settlements reached \$14.7 billion in consumer compensation and \$4.3 billion in criminal and civil penalties under the Clean Air Act (US DOJ, 2017). Global total costs, including vehicle buybacks, modifications, European regulatory settlements, and legal fees, exceeded \$30 billion.

Criminal proceedings were brought against executives across multiple jurisdictions. In the United States, Oliver Schmidt — who managed Volkswagen's environmental and engineering office in the US — was convicted and sentenced to seven years in federal prison. Former Audi CEO Rupert Stadler was convicted on fraud charges by a Munich court in 2023. Former CEO Martin Winterkorn faces fraud and conspiracy charges in the United States; as a German citizen, he has not been extradited and faced separate proceedings in Germany.

The reputational consequences for Volkswagen extended well beyond the financial costs. The 'clean diesel' proposition that had anchored the US growth strategy was irreparably damaged. More broadly, consumer trust in diesel technology across Europe — where diesel vehicles represented a substantial share of the passenger car fleet — declined sharply, accelerating the regulatory and commercial shift toward electrification across the European automotive industry.

6. KEY LESSONS FOR LEADERSHIP PRACTICE

Strategy reversibility as an ethical requirement. The Dieselgate case illustrates how commitment to a publicly announced strategy can become a structural barrier to ethical course correction. Organizational processes that make it costly to acknowledge strategic failure — through loss aversion, reputational investment, and internal narrative pressure — create conditions in which illegitimate solutions displace legitimate ones. Building explicit strategy review mechanisms that allow course correction without requiring acknowledgment of failure is a governance imperative in high-stakes competitive environments.

Dissent channels as regulatory infrastructure. The organizational silence that prevented internal objections from reaching decision-makers was not produced by individual timidity but by structural conditions. Creating protected dissent channels — with genuine anonymity protections and demonstrated responsiveness — is not merely a cultural aspiration but a structural requirement for organizations making technical decisions with regulatory implications.

Cross-functional ethics review for technical decisions. Defeat device software was a technical decision made within engineering functions. Its regulatory and ethical implications were not systematically reviewed by functions with competence in those domains. Organizational structures that isolate technical decision-making from regulatory and ethical oversight create structural conditions for this class of failure.

Identity resilience versus identity protection. VW's engineering excellence identity, rather than functioning as a constraint on ethical compromise, functioned as a moral license for it. Organizations should distinguish between identity resilience — the capacity to maintain core values under pressure — and identity protection — the use of reputational capital to rationalize ethical deviation.

7. CONCLUSION

The Volkswagen Dieselgate scandal is frequently described as a story of corporate fraud. At the level of legal characterization, this is accurate. At the level of organizational analysis, it is incomplete. Dieselgate was produced by an organizational system in which competitive pressure, commitment escalation, dissent suppression, and moral licensing interacted to make a fraudulent solution organizationally thinkable — and, over nine years, organizationally normal.

For leaders in competitive, regulated industries — automotive, pharmaceutical, financial services, energy — the case offers a diagnostic framework for identifying the conditions under which their own organizations might be susceptible to analogous failure patterns. The key diagnostic question is not 'are our people honest?' but 'have we built organizational structures that make it easier to find a legitimate solution than an illegitimate one, and easier to raise objections than to remain silent?' Where the answer is uncertain, the conditions for a collective decision trap exist.

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