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On Corporate Wrongdoing in Europe and Its Enablers

In the last two decades, several instances of prolonged and severe corporate wrongdoing by European companies have come to light: from Dieselgate to corruption, money laundering through large European banks, recidivist bid and price rigging, and most recently Wirecard. What allowed European firms to engage in so much wrongdoing? In this brief, we consider some important institutional drivers behind corporate wrongdoing, focusing on the European countries with the largest share of corporate infringers.

The harm from and extent of corporate wrongdoing in the EU.

In June 2020, the German firm Wirecard AG's stock price fell from €104 to below €2 in the span of nine days after the firm admitted it could not locate $2 billion missing from its accounts. The firm has since then been accused of a wide range of infringements including money laundering, corruption, and fraudulent inflation of profits and sales, with some allegations going back over a decade. The Germany financial supervisor BaFin has been criticized as allegations about fraud had been made several times in prior years. Yet, BaFin failed to identify the problem and even banned short-selling of the stock, as well as accused journalists who were critical of the firm of market manipulation.

This scandal occurred against a backdrop of several other prolonged corporate scandals and has led many to wonder how extensive corporate wrongdoing is and how to combat it more effectively.

Corporate wrongdoing has a range of negative effects in competitive markets that are frequently overlooked in the public debate. Beyond the immediate damages of corporate wrongdoing, such as the draining of public resources in the case of tax evasion, money laundering, corruption, air pollution and associated health harm in the case of environmental law violations, there are also more general negative effects of corporate wrongdoing.

It attracts investors to the worst part of the industry, as firms that engage in profitable wrongdoing often do better than their competitors. Also, it forces out honest competitors and increases market entry thresholds for new competitors. These effects become more pronounced when the wrongdoing is prolonged, so, in an ideal world, regulators need to act fast.

Instead, several recent cases of European corporate wrongdoing lasted for many years before being detected and sanctioned, and there is a worrying degree of recidivism in several regulatory areas, including financial regulation with several banks being recidivists, but also in antitrust (Marvão, 2016).

What are the drivers and enablers behind these many prolonged cases of wrongdoing, and why do firms feel emboldened to engage in recidivism?

One way to gain some insight is to identify European countries whose firms are most frequently fined for wrongdoing and review the legal, cultural, and political contexts of those countries.

We tackle this issue by using data from Violationtracker, a database with over 400 000 actions by US enforcement agencies and prosecutors (such as the Securities and Exchange Commission and the Department of Justice). Many of these sanctions are against firms with headquarters in EU countries. In Nyreröd and Spagnolo (2021a), we added the fines for firms with headquarters in all respective EU countries for the period 2000-2020. After excluding countries like Switzerland, well known as homes of extensive financial crime linked to their status of international tax havens and off-shore centers, we find that the United Kingdom is the gold medalist in corporate wrongdoing, with Germany coming in second place.

Table 1. *Fines across the top six EU countries (2000-2020).*

	Country	**Total fines**
1	United Kingdom (1811)	$69 298 977 830
2	Germany (2332)	$50 309 697 861
3	France (1119)	$19 931 690 635
4	Netherlands (1433)	$5 811 672 653
5	Italy (243)	$2 100 188 326
6	Sweden (293)	$2 034 164 118

Note: Author's calculation based on data retrieved from Violationtracker.org. Number of fines in parentheses.

Interestingly, the top of the ranking is preserved no matter which metrics we use. In Nyreröd and

Spagnolo (2021a) we weigh the fines by population, GDP, and exports to the US, and the UK and Germany remain stable at the top, with the UK's first position becoming more pronounced. Therefore, we focus on these two countries, although many of the problems we identify apply to a varying degree to most other EU countries.

Because of the recent headlines made by the Wirecard case we start with the runner-up, Germany.

Germany

The Wirecard case follows a long tradition of large "household" names such as Siemens, Deutsche bank, Thyssenkrupp, and Volkswagen that have engaged in systemic wrongdoing over extended periods of time and are responsible for most of the fines shown in Table 1.

In one of the largest corruption scandals in history, Siemens was fined $1.6 billion by the Department of Justice in 2008 for systematically paying bribes to government officials around the world, amounting to more than $1.4 billion since the mid-1990s. According to the Securities and Exchange Commission's investigation, bribery at Siemens was "standard operating procedure" for decades, and the SEC concluded that "the company's tone at the top […] created a corporate culture in which bribery was tolerated and even rewarded at the highest levels of the company" (SEC, 2008).

In 2015 the Dieselgate scandal unraveled, where it was discovered that several car manufacturers had installed "defeat devices" to cheat emissions tests. Volkswagen had installed the device in 11 million vehicles, some of which emitted up to 40 times more than emissions standards allowed (Gates et al, 2017).

Germany's largest lender Deutsche Bank has since 2000 paid a whopping $18 billion in fines in the US for alleged infringements ranging from facilitating money laundering and tax evasion, to concealing bribe payments and misleading investors (DoJ, 2021). This is by far the greatest amount paid by any EU bank in the period 2000 – 2020 (Violationtracker.org, 2021)..

Finally, there is the steel conglomerate ThyssenKrupp, which was handed a €479 million fine for bid-rigging by the European Commission in 2007, the highest EU bid-rigging fine ever at the time. The size of the fine was motivated by the fact that, in 2007, Thyssenkrupp was already a repeat offender. In 2019, Thyssenkrupp and three other steel manufacturers were fined $719 million for price-rigging between 2002 to 2016. The firm has also been accused of bribe payments on several occasions (see Nyreröd and Spagnolo 2021a for details).

In reviewing local factors that have enabled these incidents, we find that Germany appears to have a particularly lenient stance toward corporate wrongdoing and a notably hard one against whistleblowers disclosing it. With respect to corruption, for example, bribe payments could be deducted from tax in Germany up until 1999 if paid to foreign officials, and up until 2002 if paid to recipients in the business world (Berghoff, 2017). In October of 2003, the United Nations adopted the Convention Against Corruption. On average, European countries had ratified this treaty halfway through 2007, but Germany was one of the last to ratify the treaty, it did it only in 2014 (UNODC, 2020).

Perhaps more importantly, Germany's institutional environment seems focused on punishing and deterring whistleblowers, rather than listening to their reports in order to fight corporate wrongdoing. This is likely a crucial enabler of the prolonged wrongdoing we discuss in more depth in Nyreröd and Spagnolo (2021a). It is well known that whistleblowers are essential to detecting corporate wrongdoing (ACFE, 2020). Yet, Germany has some of the worst whistleblower protection laws in the EU (Transparency International 2013, Wolfe et al 2014), and one of the worst records in Europe in terms of mistreating the (obviously few)

whistleblowers that dared to denounce corporate wrongdoing (Worth 2020a).

The German opposition to the protection of(truth-telling) whistleblowers from employers' retaliation was on full display when a public consultation was held on the new EU Directive on whistleblower protection (2019/1937). German industry representatives were particularly active in arguing against it, suggesting that whistleblower protection is not necessary and that the new regulations are a clear signal of mistrust towards companies (BDI, 2019). The German parliament discussed improving the poor whistleblower protections in 2013 but did not enact any improvement of whistleblower protection laws. There are several instances of retaliation against truth-telling whistleblowers where they had very little legal recourse (Worth 2020a; Nyreröd and Spagnolo, 2021a).

The hostile regulatory and political environment to whistleblowers is likely a main factor that has enabled so many German corporations to engage in such prolonged wrongdoing with no records of employees reporting it.

The United Kingdom

We now turn to the winner of our contest, the UK. Over $26 billion of the total fines paid by UK firms in Table 1 is accounted for by the British Petroleum's (BP) Deep Horizon oil spill in 2010 in the Mexican Gulf. It is estimated that 5 million barrels of oil were released into the ocean, a spill regarded as one of the largest environmental disasters in history.

Internal investigations at BP during the decade preceding this spill had warned senior BP managers that the company repeatedly disregarded safety and environmental rules and risked a serious accident if it did not change its ways. A 2004 inquiry found a pattern of intimidating workers who raised safety or environmental concerns (Lustgarten and Knutson, 2010). The company allegedly flouted safety standards by neglecting aging equipment, delayed inspections to cut production costs, and falsified inspection records. Even before the 2010 spill, officials at the US Environmental Protection Agency had considered debarring BP from receiving government contracts (Lustgarten, 2012). Since 2000, BP has been fined 158 times for environment-related offenses in the US, and again over 60 times since the oil spill in 2010.

Then there is the UK banking sector, with many large banks continuously engaging in wrongdoing, and seemingly more so than elsewhere. CASS (2020: 6) shows how, since 2011, the conduct costs of UK banks have far exceeded that of banks based in the US and Euro area when compared to GDP. In 2017, conduct costs for UK banks represented 0.88% of the UK's annual GDP, while conduct costs for US and Euro area banks represented around 0.10% or less. In 2018, the conduct costs for UK banks shrank and constituted around 0.55% of the UK's annual GDP.

In 2010, it was discovered that HSBC had systematically laundered money for some of the bloodiest drug cartels in history through its Mexican subsidiary. Despite numerous internal warnings, complaints from regulators, and internal flags, HSBC Mexico continued laundering money for organizations like the Sinaloa cartel, who not only flood the US with illegal drugs but is considered responsible for the gruesome killings of tens of thousands of people, often innocent civilian casualties at home. The UK's then-chief financial minister, George Osborne, pleaded with the US Treasury Secretary and others that they do not impose criminal sanctions on HSBC (US Congress 2016).

Another major scandal involving UK banks that have cost regular people billions of pounds was the misselling of "payment protection insurance". This aggressively marketed insurance had profitability of approximately 90% (Laris, 2020). Several barriers were created to inhibit people from claiming the insurance, such as contract exclusions or administrative barriers, and many people who bought these insurances either did not need them or were unsuitable. As of January 2011,

UK banks and financial institutions had paid out £37.5 billion in compensation to customers who were wrongly sold the insurance (Coppola, 2019).

One of the main drivers of corporate wrongdoing in the UK appears to have been the lack of effective corporate sanctions. The "identification principle" requires the identification of a directing mind and will of the company (typically a director), and then proving criminal liability through this person's conduct and state of mind. This principle has been singled out by several experts as making it "impossibly difficulty" for prosecutors to find companies guilty of serious crimes, especially crimes in large companies with devolved business structures (The Law Commission, 2015: 15). Several UK institutions, such as the UK's Serious Fraud Office and the Crown Prosecution Service, have also pointed to the identification principle as a central hurdle to their ability to bring corporate prosecutions (Corruption Watch, 2019).

Moreover, effective business lobbying and close connection between politicians, regulators and the financial sector have been prevalent in the UK for a long time and may have exacerbated the already accommodating regulatory environment. Several well-known high-level politicians that affected financial regulation and its implementation for years ended up being hired with handsome pay by financial institutions afterwards (see Nyreröd and Spagnolo 2021a for details).

Regarding regulators, Miller & Dinan (2009: 29) notes that of the 36 people that served on the board of the Financial Services Authority (FSA) between 2000 and 2009, 26 of the members had connections at board or senior level with the banking and finance industry either before or after their term of office, whilst nine continued to hold appointments in financial corporations while they were at the FSA".

The UK also has an outdated and ineffective whistleblower protection law, the "public interest disclosure act" of 1988 (see e.g., Lewis 2008, Thomas Reuter Foundation and Blueprint for Free Speech 2016, All Parliamentary Committee 2020). At the same time, important UK regulatory agencies have been proactive in neglecting the mounting independent academic research highlighting the effectiveness of the US whistleblowers rewards programs (see Nyreröd and Spagnolo 2021b).

Conclusion

Corporate wrongdoing appears widespread in Europe, and recent cases have been prolonged, severe, and sometimes industry-wide.

The UK and Germany stand out, but other EU countries are no angels. In the case of Germany, an acute aversion to whistleblowers by government institutions appears as a central driver that has enabled corporate wrongdoing. With respect to the UK, ineffective corporate sanctions laws, regulatory/political capture, and a lack of whistleblowers, appear to have driven or enabled firms to engage in prolonged corporate wrongdoing. Similar enablers and drivers are likely present in other EU countries to varying degrees.

There is now an EU Directive on whistleblowing, requiring all member states to put in place retaliation protections for those reporting on corporate wrongdoing. But protections have proven insufficient in a variety of ways and are unlikely to be a game-changer in terms of combating corporate wrongdoing (see e.g., GAP and IBA, 2021).

In the light of the strong independent evidence on the effectiveness of whistleblower reward programs at increasing detection and deterring wrongdoing (see, e.g., Nyreröd and Spagnolo 2021b for a survey), EU Member States seriously concerned about corporate wrongdoing should consider introducing them in a wide variety of regulatory areas.

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