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CASE STUDY: **The Spin-off of Volkswagen Financial Services**

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The conclusion of this project symbolizes the accomplishment of an objective and reflects a really important moment of my academic path. Thus, I would like to show my thankfulness to my academic supervisor Melissa Prado for the helpful remarks during this learning process. I would like also to recognize the support of my colleagues from Volkswagen that always helped me during this period. I would like to thank to my friends and family for the patience throughout this period. Lastly, I would like to thank to my parents for their constant love, support and for always giving me opportunities to growth.

The Spin-off of Volkswagen Financial Services

Abstract

The Volkswagen Financial Services AG (VWFS) competitive positioning was negatively affected by the regulatory responsibilities imposed by European Central Bank (ECB). ECB Regulations did not fit business model and global footprint of VWFS AG. Thus, the purpose of this work project is to study the solution adopted by VWFS AG to overcome this problem – Spin-off of VWFS AG. This project takes the form of a case study, being divided between the case narrative and teaching notes. Initially, the history of VWFS AG and VWFS Portugal will be presented. Subsequently, the motivations, risks and benefits behind the restructuration will be analyzed.

Key words: Spin-off; Volkswagen; Regulations; European Central Bank

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Chapter 1 – Case Study

1.1 – Volkswagen Financial Services AG

In 1949, in order to stimulate the sales of motor vehicles, "Volkswagen Finanzierungsgesellschaft mbH" was founded to grant loans. "Volkswagen Leasing GmbH" was established in 1966. In 1973, a company with a full banking license replaces the company founded in 1949, with the registration of "Volkswagen Kredit Bank GmbH". Later, in 1990, this company changed its name to "Volkswagen Bank GmbH". A restructuration of the financial services division happened in 1992, transferring the companies Volkswagen Bank GmbH (VWB) and Volkswagen Leasing GmbH (VWL) to the holding company "Volkswagen Finanz GmbH" created in 1991. Hence, all activities regarding Volkswagen financial services in Germany were aggregated in this company. In 1993, the company takes a big step by initiating international activities, covering the Slovak Republic and Great Britain.

Volkswagen Financial Services AG (VWFS AG) was launch in March of 1994, in order to manage financial service business in Europe. The company expanded its activities to Spain, Italy and France. Netherlands market is also integrated in 1995. In 1996, the markets of Asia-Pacific region and Japan were added to VWFS AG range of activities and the company receives for the first time a rating, being able to participate in the international capital markets in their own right. The "Auto Credit" product was launched by Volkswagen Bank GmbH, which diminishes the risk associated with a used vehicle at the end of the contract for the customer. The first product combining insurance services appears in 1997 launched by VWFS AG, at the same time that VWB starts new business activities in Poland and Belgium. In 2000, VWFS starts business activities in Switzerland

and Turkey and expands one more time its business, having then the motor vehicle insurance.

VWB introduces transactions managed via mobile phone and Portugal becomes a new market for business activities. In Australia, the business activities of VWFS started in 2001 and a branch office of VWB is established in the Irish market. The foundation of VWFS Taiwan took place in 2002. The Russian market was integrated in 2003 and the holding company (VWFS) also begins to have control of the Swedish market. In 2004, "Volkswagen Finance China Co Ltd" obtained its business license and substituted the existing representative office in China. VWB started their business activities in Greece. In 2005, Volkswagen Financial Services started to coordinate the group's worldwide financial services, that were previously coordinated by Volkswagen AG. Banking and leasing business started in Mexico in 2006, followed by Brazil in 2007 with the financial services activities. Mobility packages are created in 2008 for used Volkswagens, combining financing or leasing contracts with the "Best Service" packet (including servicing, oil change and original VW parts). The Indian and Norwegian markets are introduced in 2009 within VWFS AG. In the same year, the first supra-regional natural gas fuel card is introduced by VWL for corporate customer (customer with an exposure higher than 500.000€). VWFS started its business activities in Lithuania, Latvia and Estonia together with Nordea Finance in 2010. South Korea had also become one of the locations where VWFS was present.

In 2013, "Ducati Financial Services" starts its business in Germany under the control of VWFS AG. "MAN Finance International GmbH" was acquired by VWFS AG in 2014, and the renting business for MAN Truck & Bus was introduced. In 2017, a new structure was adopted, and VWB was then a wholly owned subsidiary of Volkswagen AG instead of VWFS AG. A new company was also created "Volkswagen Financial Services Digital

Solutions GmbH", whose aim is to develop selected services and made them available to its parent companies (VWB and VWFS AG) **(Exhibit 1)**. The group's brands are divided in Volume (VW, Skoda, Seat, VW LCV and Moia), Premium (Audi, Lamborghini and Ducati), Super Premium (Porsche, Bentley, Bugatti) and Truck and Bus (MAN and Scania), with the company present in 51 countries. As previously mentioned, one of these 51 countries is Portugal. Hence, the history of VWFS Portugal will be further studied.

1.2 - Risks associated to VWFS and its activity

The development of the automotive sector is dependent on the global economic development. Thus, disturbances in the global economy, geopolitical tensions and country specific challenges can impact negatively on the VWFS business. Also, the upcoming withdrawal of the UK from the EU can influence negatively the economic conditions in UK and Europe since new uncertainties and instability in the UK and the EU can rise market volatility and lead to disturbances for global financial markets. In its turn it can lead to a negative effect on the operations and financial conditions of VWFSAG Group. VWFSAG Group is dependent on sales by Volkswagen Group, so any risk influencing the vehicle delivery of the business of Volkswagen Group will probably impact the generation of new contracts and then VWFSAG Group business. Changes in consumer preferences as new trends for smaller vehicles or vehicles with smaller engines can also have impact in VWFSAG Group profitability. Moreover, VWFSAG Group is exposed to strategic risks related business development, products, pricing and investments in infrastructure or personnel. This type of risks involves a direct or indirect loss caused by strategic decisions leading to a failure to reach strategic objectives. It also implies risks resulting from integration or reorganization of technical systems, personnel and corporate culture. Thus, wrong decisions regarding products related to regulatory or competitive criteria may decrease profitability due to reputational damage or missed customer needs.

The process of digitalization is very important and will have for sure a noteworthy impact on financial services sector. The digital world will change the processes of current sales and services, customers expect to have information on online platforms independent of time and location and a range of sales channels. VWFSAG challenge is to meet the customer needs in time, otherwise it can affect the business and financial conditions. VWFSAG is exposed to operational risks as process risks (unsuitability of failure of internal process), personnel risks (people risks), external risks (e.g. terrorist attacks) and technology risks (systems). Litigation risks may derive from legal disputes, official proceedings with various stakeholders or governmental investigations. These are important risks since VWFSAG Group works with internal and external information and manage their operations with technological systems. Its customers or other contractual counterparties can have their credit quality deteriorate or may even default, which is a risk for VWFSAG. All these risks can have an adverse effect on the business activity. Decreases in residual values or in sales related to returned vehicles can have a negative impact on the business. For example, if the customer chooses the return option after a leasing contract, generally VWFSAG Group bears the risk that the market value of the vehicle to sold at the end of the term is lower than the contractual residual value when the contract was signed. A negative change in consumers preferences can lead to higher residual values risks, since the demand is determined by the customers which influence the prices of used cars.

Increased capital requirements regarding local regulations and measures can impact business profitability. Government regulations are always changing and VWFSAG Group needs to comply constantly with the requirements, which has the implied risk of not following the refereed laws appropriately. Tax laws and their interpretation may affect VWFSAG Group's financial conditions as well. Compliance and risk management systems may demonstrate an inadequate ability to prevent and discover breaches of regulations or may not be able to identify and take the countermeasures against all relevant risks. VWFSAG Group is exposed to different market risks as interest rate risk, foreign currency risk, fund and asset price risk. The VWFSAG Group business involves considerable funding and liquidity, so disturbance in funding sources or access to the capital markets can influence in liquidity, cash flows, financial condition and results of operations. Funding costs can be adversely affect by changes of Volkswagen AG's credit rating since credit ratings of VWFSAG are dependent of it.

Insurance coverage can also be insufficient due higher damages than expected or uninsured risks. VWFSAG Group also faces premium and reserve risks towards its insurance business and brokerage business. Changes in accounting standards and events that might cause reputational damage can also have a negative influence in the business of VWFSAG Group. At last, several risks as operational, legal and regulatory risks can arise from the reorganization of VWFS.

1.3 – Spin-off of VWFS AG

In November of 2016, the Supervisory board of Volkswagen Financial Services AG approved a reorganization measure of VWFS group regarding the separation of Volkswagen Bank GmbH (VWB) from VWFS AG. This corporate restructuration started in November of 2016 with the objective of bundle the credit and deposit business inside the European Economic Area (EEA) in Volkswagen Bank GmbH. **(Exhibit 2)** Volkswagen Financial Services AG would remain with all other activities as leasing, insurance, service and mobility business, but also the credit business outside EEA. This new step up was implemented in September 1, 2017 and VWB is from then on, a direct subsidiary of Volkswagen AG **(Exhibit 3)**. This process allowed European Central Bank (ECB) to supervise and regulate only the VWB entity. Thus, it was possible to free-up equity to fund some initiatives and reduce regulatory reporting requirements. Regarding bonds and ABS transactions, this realignment did not affect the repayment of the bonds and the only thing that has changed was the ownership structure of VWB, since the domination and profit and loss transfer agreement of VWFS with VWB was transferred to the Volkswagen AG. With this optimized structure for Financial Services Business, Volkswagen wanted to optimize capital requirements by reducing complexity and improving transparency, allowing a support to the future growth path.

As Dr. Michael Reinhart (Chairman of the Management Board of Volkswagen Bank GmbH) explained: *"With this strategic repositioning, we have created even more transparency and clarity for the supervisory authorities. We are already very successful with Volkswagen Bank GmbH today. We now want to expand it into an even stronger and even more successful European bank".*

1.4 - SPIN-OFF IMPLEMENTATION OF VWFS AG

The implementation of the spin-off was made in three different phases **(Exhibit 4)**. The first one had to be done until the first quarter of 2017 and was related to the definition of the Target Operating Model concept, which goal was to fully separate VWFS and VW Bank. In order to understand concretely what should be separated, ECB gave some guidance and keystones. Considering governance, supervisory and management boards should not have double mandates and VW Bank's and VWFS' management board and committees should have clear independence. Concerning sales, VWFS is a credit intermediary and supervisor of the distribution channels, while VW Bank takes credit decisions independently being responsible for sales guidelines, credit processes, pricing and conditions. Regarding Finance, VW Bank has complete control for business and capital planning process, managing controlling and accounting functions independently, being allowed cooperation. VWFS can perform tasks to consolidate VWFS results for Volkswagen AG. Treasury strategies and responsibilities are independent. About Compliance and Outsourcing, the core functions of VW Bank are risk management, internal audit, compliance, human resources, treasury and regulatory reporting. There is also a strong outsourcing management of VW Bank with clearly defined outsourcing contracts. This scheme is based on Head quarter's (HQ) entities (Bank HQ and VWFS HQ) since local branches have focus on credit decision-making, standard procedures defined by HQ being operational tasks outsourced, as will be further presented in the example of Portugal branch.

The second phase was regarding the Operating Model and was due to 31st of August 2017. There were three options concerning the separation of EU Bank from VWFS: For countries in wave 1, countries where the separation had to be completed by the end of 2017 **(Exhibit 5)**, a direct separation of VWFS could be done if the IT systems of the market could be separated. This would result in two entities, the EU Bank entity and the Volkswagen Financial Services entity. In this case, a clear separation of systems and data would happen, and VW Bank would be able to control its IT systems and data. Otherwise, VWFS would be divided into three entities: the EU Bank entity, VWFS and Digital Solutions.

For countries in wave 2, (countries where the operational separation will be after 2018), where the separation could not be before 31st of August 2017, the VWFS activities would be reassigned to the banking activities firstly **(Exhibit 6)**. At a later date, the two entities would be deconsolidated to implement the Target Operating Model. Interim solutions could be applied for specific branches. In the last phase, the business in priority markets would be stabilize in phase three with the separation of VWFS and VW Bank across all countries established and with the target operating model implemented.

1.5 – Impacts of the change in VWFS AG operation structure

In order to have a successful restructuration there are some significant changes in the operation structure of VWFS that were necessary and resulted in many impacts for the companies involved. First of all, VWFS loses shareholder responsibility for VWB. Then, the future market results from two independent units, and due to these separate sources, the earnings of VWFS may be volatile. Temporarily, because of the new operating structure, there are some countries completely in VW Bank as Norway and Czech Republic. Negative impacts on bank rating were also verified. According to Standard and Poor's, VWFS AG rating was revised after the spin-off, and since it is a core subsidiary of Volkswagen AG, its rating should reflect the rating of Volkswagen AG. This way, the outlook of Standard and Poor's on VWFS AG was stable, corresponding to a "BBB+/A-2" rating. However, a negative outlook regarding VW Bank was attributed, which reflects the risk of within the next two years the core business of VW Banks (that involves the credit business) attract a higher economic risk outside German markets than the expected. Thus, a rating of "A-/A-2" was attributed to VW Bank GmbH.

Not only impacts on results are observed, but also in the culture, since will be observed a development of different cultures in VWFS and VWB. This can generate emotional stress of the workforce that may lead to an inefficient work.

1.6 – Optimization of Equity Requirements

One of the biggest advantages of this restructuration is the reduction of equity requirements. Hence, it is very important to analyze the impact of this benefit in the firm. The minimum equity ratio is defined by the regulator, in this case, by ECB for companies with credit business within the European Economic Area.

In 2016, before the spin-off, the minimum equity ratio defined was 12% plus 0.75% as internal capital reserve. Thus, the equity needed in 31st of December, 2016 with 19 million contracts was 16.1 billion euros. However, in 1st of January, 2017 this ratio would increase to 14% plus 0.75% (as internal capital reserve) being then required 18.1 billion euros. Regarding the company strategy for 2025, the number of contracts expected for that year were 30 million contracts. Without the spin-off, the equity requirement in 2025 would be 30 billion euros.

After the restructuration, the two entities would have different minimum equity ratios, as only one of the entities would have an equity ratio defined by the ECB. The Bank entity would have 14% plus 0.75% (as internal capital reserve), making a total of 13 billion euros regarding the 2025 strategy, while the VWFS entity would not have the minimum equity ratio defined by the ECB, but would need to guarantee 8% of the balance sheet, making a total of 11 billion euros regarding the 2025 strategy. In total, with the restructuration, both entities would have an equity need of 24 billion euros.

Comparing the equity requirements without the spin-off (30 billion euros) and with the spin-off (24 billion euros) it is possible to conclude that this restructuration allowed a reduction of 6 billion euros in equity requirements, having then more resources to fund the VWFS growth goals.

1.7 - History and the spin-off of VWFS Portugal

Volkswagen Bank Portugal was founded in 2011 with 35 employees, but only in 2012 started its activity with the start of credit financing, car insurance and credit protection insurance with a total of 29 contracts. In 2013, ALD and Leasing products were launched, and the contracts number increased to 4.463. The company MAN Financial Services and a portfolio of 600 trucks were acquired in 2014, which allowed the company to grow and to have in the end of the year 9.564 contracts. This acquisition also permitted the company to introduce renting contracts (with a specific team dedicated to the corporate channel – Customers with an exposure higher than 500.000€).

From then on, these two firms in Portugal, VWB Portugal and MAN Financial Services which was later called Volkswagen Renting (VWR) were subsidiaries of VWFS AG. Hence, in 2015 a total of 18.115 contracts was reached. In 2016, the company launched the auto credit product, and was able to have 25.001 contracts. In the end of that year, VWFS AG decided to spin-off which impacted all the companies of the group. In Portugal, this restructuration process was easier since two companies were already established, but it was still necessary to separate both companies across all key dimensions as the structure organization, shared processes and employees' allocation. After the spin-off, VWB became a subsidiary of VWB AG, while VWR continued to be a subsidiary of VWFS AG. It is important to highlight that while VWB Portugal is a branch of VWB AG, VWR is a Portuguese company, having to comply with the Portuguese law.

The growth of the company was noteworthy, and in 2017 maintenance service was launched for financial products, having in the end of the year more than 130 employees and 28.000 contracts. Nowadays, since leasing contracts are included in VWB portfolio, the company is working in a second spin-off, in which a third company will be created – Volkswagen Financial Services (VWFS). This new entity will englobe a portfolio of operational leases and is also a Portuguese firm that needs to comply with Portuguese law, being a subsidiary of VWFS AG.

1.8 – Spin-off implementation in Portugal

As mentioned in chapter 1.4, the implementation of the spin-off was made in three different phases and the first phase was related to the target operating model concept. This concept was not defined in the same way for markets with branches and for other markets. Since VWB Portugal is a branch, this applies to the Portuguese market. Hence, the previous description of the target operating model is not applicable to Portuguese market. VWB Portugal as a local branch focuses on credit product management, credit decision making, core banking functions and outsourcing steering. On the other side, VWR as a local VWFS Company, and in the future also applicable to VWFS Portugal, focuses on Corporate development and strategy, legal and internal audit, sales management, product management, marketing and customer relationship management, brand management, controlling, accounting, purchasing, risk and credit management (ICS), Human Resources (HR) and organizational development, operational HR support, information technology (IT) and customer service. Considering the second phase, a direct separation between VWB Portugal from VWR Portugal could not been done, since IT systems could not be separated. Hence, this separation originated a third entity – Volkswagen Digital Solutions - that was created in 2018, being this a shared services company in the areas of IT, customer, processing and document management services. The last phase is related to the business stabilization of these entities and the target operating model implemented.

1.9 – Summary of local work package and central work package

This spin-off involved different work packages regarding the HQ and its subsidiaries, since this was a reorganization project combined with Europe-wide legal restructuration.

First of all, the work packages in the local level will be analyzed. In terms of reorganization, it was important to define and execute target operational model by defining roles and responsibilities of units. Considering internal contracts and outsourcing steering, there was a need to provide contractual templates and develop concept for Service level agreement (SLA) and Outsourcing. In order to separate entities, it is mandatory to identify the affected contracts to initiate the mitigation strategy. Finally, it is important to implement a communication strategy supporting the process of change management.

On the other side, observing the work package in the central level, there are also four key fields. Related to the legal target model, it is required to define and implement the legal target picture together with local lawyers in the markets. About the Target Operational Model and its execution, HQ needs to support subsidiaries with regulatory advice. Due to the new regulatory environment there is a new definition of the Internal Control system for VWFS. Lastly, in financial terms it is essential the preparation of business cases, equity planning and the integration of liquidity project.

1.10 – Learnings from the Spin-off

After the implementation of the project it is very important to analyze what went well and what must be improved in upcoming projects. This was one of the most challenging projects in VWFS history with a high degree of complexity and a tremendously little timeline with predefined implementation date. Thus, the learnings from the spin-off can be related to the Method, the People, the Culture and the Organization and Structure. Concerning the learnings from the Method, it is important to have a clear target vision, an analysis related to the viability of the project, a focused approach, since the guidance was provided centrally for local implementation and external deadlines are helpful to raise focus and attention during the project. A kickoff meeting can also be advantageous to introduce the project and identify first challenges and risks. Ensure that existing tools can be used and the existence of templates to cover the project plan, impact and the process analysis. The overall project status should also be reported to the HQ. Regarding the People, the first point of contact for each local team was the HQ Core team, that would manage any incoming request. In order to have faster communications and decision makings, HQ Core team members should be exempted from their routine tasks in order to ensure that this team would not be overloaded. Contemplating the Culture, it is important to point out the team spirit, the culture differences, the internal communication by providing project news associated with the progress to employees, since they can have some concerns and fears since some people are not involved in the process and thus, do not have the same access to information. A failure culture is very essential, accepting the errors without sanctions to be possible to improve with the mistakes made. Considering the Organization and Structure, responsibilities and representatives should be defined in order to have a better process of decision making, related with the stability of decision that leads to a better planning and implementation process. An easy access to experts and the involvement of management board for high level decisions are also important factors.

CHAPTER 2: TEACHING NOTES

This case study is related to a change in the legal structure of VWFS AG, which required the separation of VW Bank GmbH from VWFS AG, thus becoming VWB a wholly-owned subsidiary and with direct reporting line to VW AG. VW Bank GmbH contains all credit business within the European Economic Area, being the only entity regulated by the European Central Bank. The aim of this case is to understand the risks and the reasons behind this restructuration, analyzing the process that the company had to follow in order to be successful. Hence, this case is particularly appropriate for an Applied Corporate Finance or Mergers and Acquisitions course, with subjects related to Divestitures and Spin-off. A set of suggested questions will be presented as well as possible answers. Finally, a conclusion regarding the spin-off will be obtained in last section.

1. **Explain the designation of a spin-off and the type of the spin-off of VWFS AG?**

The literature regarding the spin-off definition is heterogeneous. According to Veld and VeldMerkoulova (2008), spin-off is considered a form of demerger. In order to comprehend the type of spin-off it is important to point out the environmental context from which the spin-off derived. Thus, in this case, it derived from a commercial environment being VWFS AG a profit corporation. This type of spin-off is known as Corporate spin-offs and is defined by Parhankangas and Arenius (2003) as the business ideas developed within the parent firm that form a new business, being these based on new technologies and findings developed in the parent firm.

2. **The main reason for the restructuration of VWFS AG was related to the non-fit of business capital structure. However, there are a lot of drivers for the creation of a corporate spin-off. Indicate three possible reasons that could also influence the motivation to spin-off.**

As Rosenfeld (1984) stated, the core objective of financial management is to maximize wealth, this way, the company will only create spin-off if it brings benefit to company's shareholders. The preparation for future changes in business environments can be a driver to create spin-off, being the restructuration the reaction to external forces as deregulation, globalization and strategic innovation by global competitors (Markides & Singh, 1997). An increase in operating performance can be a driver to restructure a firm, since due to the separation spin-off will not have extraordinary costs as it occurs when subsidiary is connected with a parent company business, having a reduction of agency and overhead costs (Cumming and Mallie, 1999). Moreover, sometimes parent company and its subsidiary have conflicts regarding their business, and spin-off gives them the possibility to follow different ways, solving the conflicts between them (Sullivan & Cromwell, 2010).

3. **This restructuration of entities generated some benefits, especially on the scope of regulatory supervision as mentioned. Could you please refer some benefits of this spin-off?**

The benefits of this restructuration are related to the reduction of equity requirements for VWFS AG (around 6 billion euros regarding the strategy for 2025) and the decrease of regulatory requirement for IT and processes of non-credit business and for business out of the European Economic Area. It allows to improve the liquidation ability of European banks due to the new regulatory requirements. This spin-off permits a capital efficient growth for non-credit business in Europe and for all entities in overseas, but also ensure the same competitive conditions for non-credit business, enabling progress possibilities. For regulated entities, a double-supervision no longer exists.

4. **The future spin-off success is directly related with the good choice of the leadership team. Since it requires planning and priorities it is essential to have the right people to prepare them to successfully deal with changes. This way, what are the impacts of the spin-off regarding the HR Department and employees?**

After the reorganization, new job profiles are identified, new responsibilities and areas of responsibility arises, and employees have to be trained in order to meet the new needs. Employees have to adapt to the new organizational structure and processes under time pressure. However, employees' know-how is not quickly transferred, so this process can create some dyssynergias regarding the distribution of personnel. The transfer of employees to other firms can also generate employee insecurity, which can influence their work quality. To conclude, the company will have less back-ups, which can be a significant risk if an employee leaves the company and no other employee has the know-how to assume their tasks.

5. **A successful transaction is not only made with the right people, but it is also vital to have the right processes. For IT, what are the challenges regarding this restructuration?**

A reorganization of a company creates a lot of challenges for IT. There are new persons responsible for approvals and it is needed to separate access options. Thus, new authorization concepts have to be developed and implemented. The test effort will also be bigger since a reorganization implies changes in systems, and employees will need to revise the performance of the systems. It is important to point out that employees are only able to do this task if they have the required knowledge, and this phase of tests is very important to guarantee that systems are working according to the expected. A weak performance of systems can impact negatively the work ability of the company.

6. **In which way can the spin-off lead to a change in customer behavior?**

Not only customers, but also investors may not be interested in preserving the current level of business with VWFS AG, because they can consider the structure of the new company critical. The normal business activities can also be disturbed at short notice triggered by difficulties during the adaptation phase regarding the operational implementation of new processes (not only related to employees working on operational tasks but also related with IT difficulties related to systems). It is impossible to be sure that the restructuration will not affect the relation with customers, and this can be a serious risk since it can affect business results.

7. **Although current investors may not be interested in preserving the existing level of business with VWFS AG due to spin-off, refer one motivation why new investors may be willing to invest?**

The asymmetric information hypothesis affirms that multidivisional companies are less clear and usually undervalued (Boreiko and Murgia, 2013). Restructuring one big company in smaller firms helps reducing information asymmetry, which in turn increases the information quality about each company on the market, attracting investors.

8. Comment the risks associated with legal and regulatory proceedings for VWFS AG entity.

In the period of the reorganization, VWFS AG Group can be subject to governmental investigations, legal disputes and other official proceedings in Germany and abroad. These can be initiated by employees, suppliers, investors and relevant authorities and can be related to information security policies and legal and regulatory requirements. Claims from tax authorities and rejection by regulators can be the origin of financial damages and for failures regarding transactions of companies. After the reorganization, the pertinent supervisory body may identify that some applicable regulations are not being complied, which can result in adverse publicity and negative perceptions for supervised entity. Not only the stated above, but also a meaningful regulatory action against a member of VWFS AG Group can have a negative effect on business results.

Case-study Exhibits

Exhibit 1 – VW AG structure from September 2017

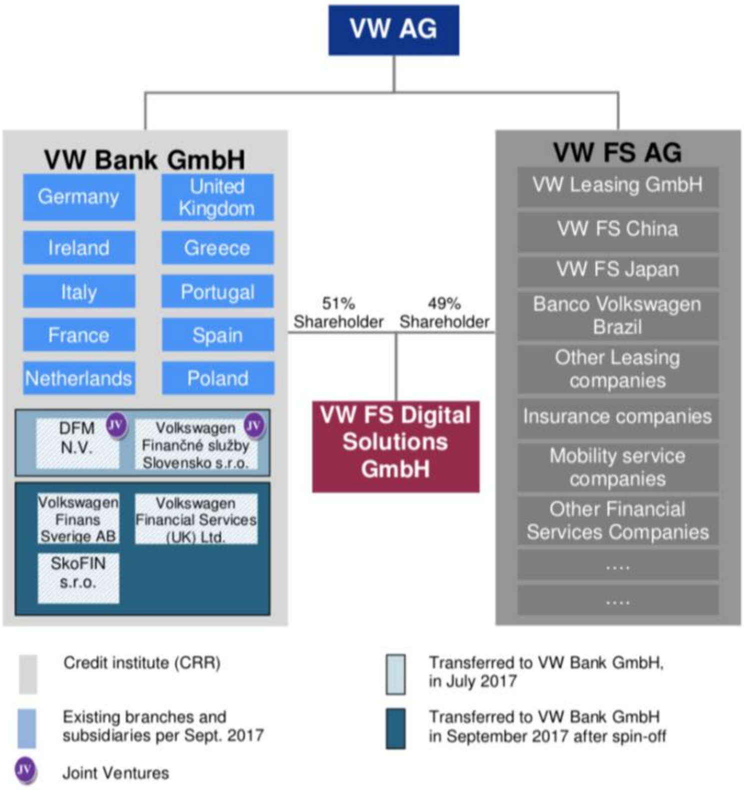


Exhibit 2 – Objective of the restructuration

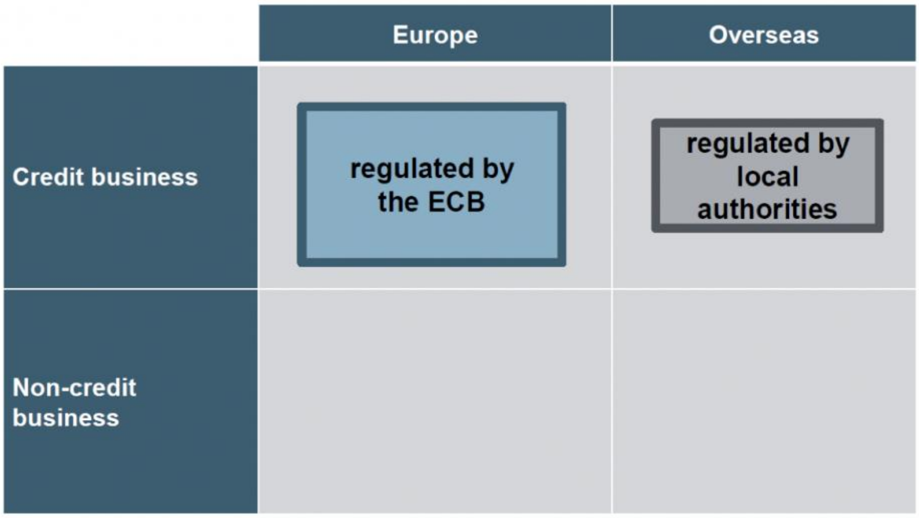


Exhibit 3 – VWB as direct subsidiary of VW AG

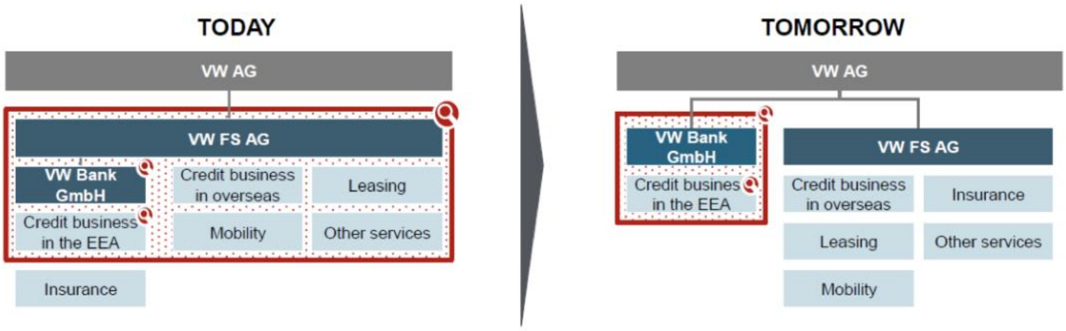


EXHIBIT 4 – IMPLEMENTATION PHASES OF THE SPIN-OFF

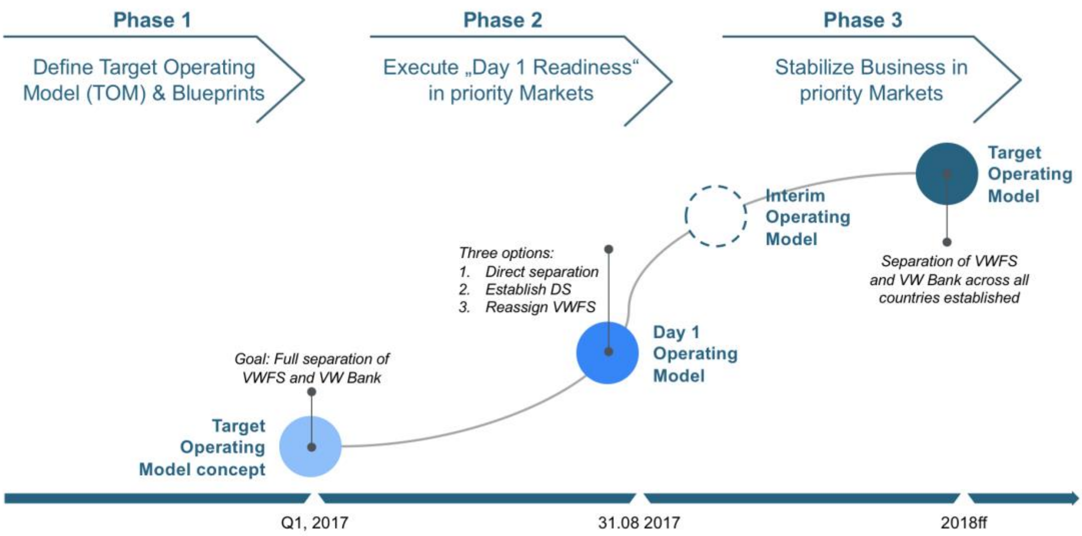


EXHIBIT 5 – WAVE OF COUNTRIES

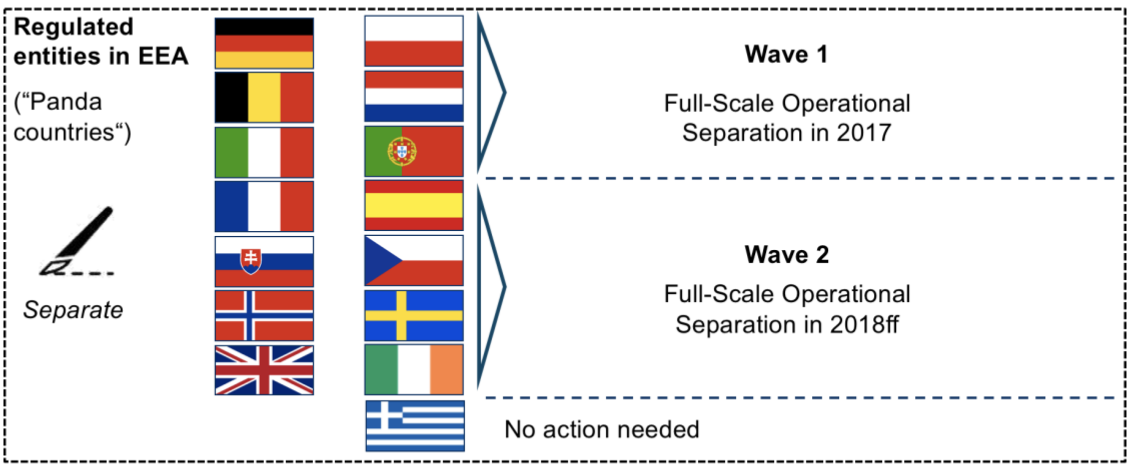
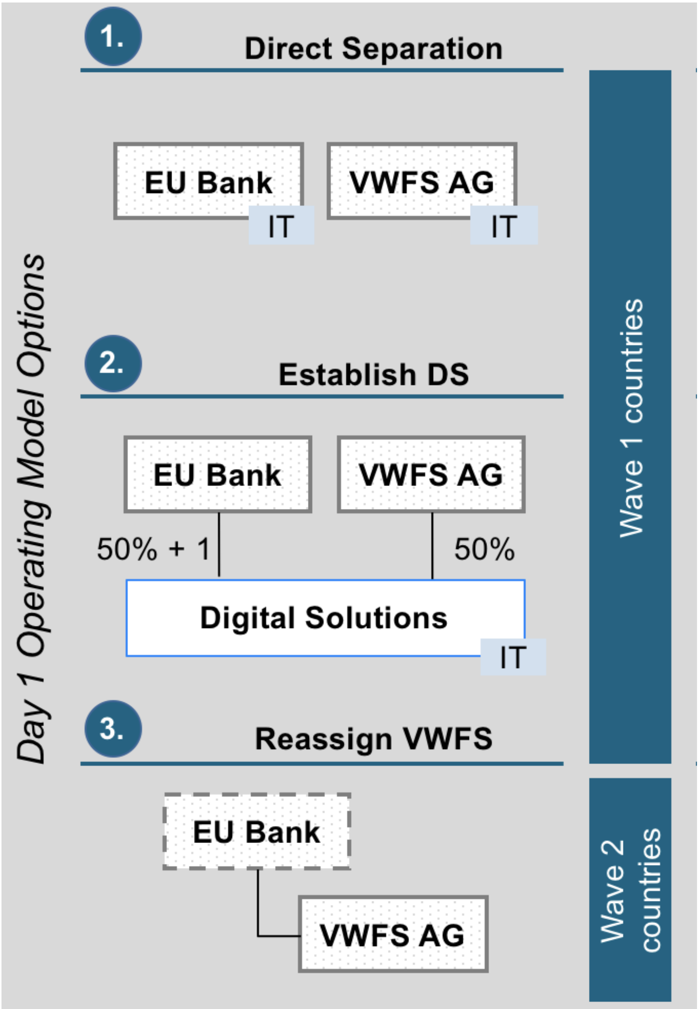


EXHIBIT 6 – PHASE 2 OF THE TARGET OPERATING MODEL



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