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9 December 2015

Dear stakeholder

Review of ORR's economic enforcement policy and penalties statement

I am writing to let you know that we have now published ORR's updated economic enforcement and penalties statement which sets out how we will approach monitoring, intervention and enforcement action for railway licence holders.

We launched a consultation exercise in December 2014 and we received a number of helpful responses to the areas we proposed to revise to improve our policy. A summary of the comments we received can be found attached to this letter.

Following your feedback we have made a number of changes to the policy. In summary some of the key updates to the policy are:

- **Clarity on the pre investigation work and our process:** We have responded to feedback from the consultation and included a new chapter in the policy document which provides greater clarity on our monitoring work and the staged approach we adopt when looking at taking potential enforcement action;
- **Reparations:** We have included more detail in the policy on reparations, setting out our approach and criteria for the consideration of offers of redress;
- **General updates:** We have updated the policy to better reflect that it is applicable to all licence holders.

The policy and penalties statement is available on our website¹. Please feel free to contact Gary Taylor, senior executive, operations and network regulation at gary.taylor@orr.gsi.gov.uk if you have any queries.

Yours sincerely



Alan Price

¹ http://orr.gov.uk/data/assets/pdf_file/0018/4716/economic-enforcement-policy.pdf

Review of ORR's economic enforcement policy and penalties statement – summary of consultation responses

December 2015

Summary

ORR reviewed its enforcement policy and penalties statement. As part of this review we undertook a consultation exercise which ran from December 2014 through to March 2015. Below is a summary of the responses we received and how we considered these points in developing the final policy which was published on 9 December 2015.

In December 2014 we began a consultation period and invited stakeholders to provide their comments on a revised policy for ORR's economic enforcement policy and penalties statement.

We published a consultation document which set out the areas we had identified (through a period of research) as aspects of the policy which could be improved or better defined. In summary these areas were:

- One policy for all licence holders;
- Early intervention and engagement;
- Consideration of penalties;
- Application of reparations;
- Use of enforcement orders; and
- General updates to the presentation of the policy.

As part of this consultation we held a stakeholder workshop on 12 January 2015. This session was well attended and provided some useful feedback on the areas highlighted above.

By the close of the consultation period we received responses from the following:

Associated Society of Locomotive Engineers and Firemen (ASLEF)	North Yorkshire Moors Railway
Civil Aviation Authority	Rail Delivery Group
Chiltern Railway	Rail Freight Group
DB Schenker	National Union of Rail, Maritime and Transport workers (RMT)
Department for Transport	Transport Focus [Passenger Focus at the time of response]
Govia	Transport for London
London TravelWatch	Transport Scotland
Network Rail	

We thank all those who took the time to respond to the consultation questions and who attended the workshop.

Below we provide a summary of the responses received and how we considered these points when producing our finalised policy document.

An enforcement policy for all licence holders

What our consultation said

We assert that one policy for all licence holders is still the most appropriate approach, despite the fact that some licence holders are publically funded. We do however propose to ensure the policy document is drafted to better reflect the range of licence holders covered by our economic enforcement functions.

Questions we asked our stakeholders

- Do you agree with our view that we should continue to have one economic licence enforcement policy and penalties statement which covers all licence holders?

Summary of responses to our consultation

The vast majority of responses agreed that we should continue to have one policy for all licence holders. The main driver for this was to ensure that there was consistency and clarity in ORR's approach to economic enforcement.

A number of responses agreed with our proposal to ensure that the policy should be drafted to better reflect that the policy applies to all licence holders. There was a suggestion that creating separate policies could create an unhelpful disparity in how ORR seeks to regulate, influence and incentivise licence holders. Other responses stressed that the policy should be flexible to take account of changing circumstances.

Consideration of responses

We considered these responses and recognised that the majority agreed with our proposal to maintain a flexible single policy for all licence holders. We recognise that there is an argument that having a separate policy for publically funded bodies was an option; however we believe that having a flexible policy enables us to hold all licence holders to account in a fair and consistent way – a key consideration when reviewing our policy.

Given this point we have drafted the policy to better reflect and inform all licence holders. We have attempted to make the policy clearer and easier to follow.

Intervention and industry engagement

What our consultation said

We see real value in regulatory intervention at early stages of an issue to bring parties together and resolve issues. This can mean formal enforcement may not be required. We monitor licence compliance and use a range of information, data and regulatory influence to hold licence holders to account. We think there are better ways in bringing transparency in our approach to early intervention and industry engagement. We also consider how we can apply reputational levers more effectively as well as bringing greater clarity and efficiency to our internal processes for intervention and enforcement;

Questions we asked our stakeholders

- Do you agree ORR should be more transparent in highlighting issues and its activities in taking early intervention; for example publishing more of our intervention correspondence and associated documents? Including more information on which we make our judgement?
- What kinds of activities, such as those discussed in this chapter, would better incentivise the industry and licence holder to raise issues and resolve these before formal enforcement was needed?

Summary of responses to our consultation

The majority of responses supported the approach of early intervention set out in the consultation document and believed and recognised the value in having greater discussion of issues at the earliest opportunity. Many felt that having earlier engagement could lead to less formal enforcement action being taken and this should be seen as a positive outcome.

A number of responses supported greater dialogue with the industry. One suggestion was for the introduction of a “task and finish” group (joint board) to provide oversight, review and governance to issues with the confidence to approach ORR with its findings and to demonstrate how it has raised and resolved issues. Another response felt that early engagement with licence holders is important but doubted whether ORR is sufficiently resourced to engage proactively with a large number of licence holders on an individual basis.

Nearly all responses welcomed the potential for greater clarity in ORR’s enforcement process. There was support for publication of data that demonstrated where early intervention made a difference. Other responses also felt that it would be beneficial to have more clarity on ORR’s process for dealing with early intervention and the subsequent steps for enforcement actions.

A number of responses stressed that purely publishing higher volumes of data and correspondence would not necessarily be a productive or useful resource for the industry. One response recognised the importance of having greater transparency but feel that publishing a greater number of correspondences may not be the best use of time and resources.

Consideration of responses

Feedback from our consultation told us that stakeholders would like to understand ORR’s process for taking enforcement action. To address this in our policy we have created a new chapter (chapter 2 Monitoring and Investigation) which sets out in detail the activities we undertake during our typical investigation staged process along with what types of

information we produce and when we would normally publish such information on our website.

As requested by a number of consultation responses we have also included further information on what actions take place pre formal enforcement action – highlighting the monitoring work we undertake.

We agree with those who suggested that publishing more information is not necessarily effective or adding value to the process. However we have looked at what we currently produce and, in the interest of transparency, intend to publish our CP5 Monitoring handbook for Network Rail which sets out the CP5 outputs and the activities we undertake to monitor delivery. We will publish this on our website in 2016. Our monitor document will also continue to highlight any formal enforcement activity which takes place during the year.

Penalties

What our consultation said

Financial penalties are an important part of a regulator's enforcement toolkit – although in many cases a penalty will likely be ORR's last resort for enforcement. We see benefit in exploring the use of other tools, such as more effective use of reparations and enforcement orders to create a package of effective measures. However, we also recognise that the seriousness of a breach, or the particular circumstances of a case, might require a financial penalty as the most suitable sanction (rather than offers of reparations or a mix of both).

We raise questions about how best to use financial penalties and at what levels to act as an incentive for future compliance of financial penalties. We set out how we think we could improve our current penalties statement to ensure it reflects more effectively the implications of financial penalties on all licence

Questions we asked our stakeholders

- Is the seriousness of breach table in the policy statement helpful to licence holders and wider stakeholders?
- Do you think the seriousness categories in the penalties statement remain appropriate?
- Would raising ORR's percentage of turnover (beyond the percentages shown in the table above) starting point for determining penalty amounts under its seriousness levels act as a stronger deterrent to future non-compliance?

- Do you support the general revisions proposed to the penalties statement to ensure it covers all licence holders?
- Do you have any other general comments on the penalties statement?

Summary of responses to our consultation

Responses agreed that the penalties table included in the policy is a useful tool for stakeholder and licence holders. There was also agreement that the levels of potential fine remain appropriate and the clarity is important for licence holders.

Responses generally recognised that penalties should be part of ORR's enforcement toolkit and should be used at the extreme end of failure (or where other forms of intervention have proven to be demonstrably unsuccessful).

Some responses questioned the effectiveness of imposing penalties on a publically funded body. Views were expressed that the current approach to enforcement on public sector organisations can lead to the ORR compounding problems on the network through cost cutting.

There was recognition of the benefits of a predict and prevent approach. Whilst recognising the incentive an aspect of a potential penalty it was suggested that it was vital that the ORR works with the industry to better understand the underlying problems, particularly around areas of sustained poor performance, and develops an appropriate and effective response to these.

There was also support for ORR to use its regulatory levers in a more effective way. It was suggested that the ORR should examine its current statutory powers to see if it can make the correlation between breach and individual senior accountability much clearer. One avenue for this in relation to Network Rail may be through the Management Incentive Plan.

Linked to this, some respondents suggested that fining public bodies such as Network Rail was not appropriate; instead ORR should look to address any licence breach through the remuneration of executives.

Consideration of responses

We recognise the points questioning the effectiveness of penalties on publically funded bodies. At the same time we believe that we should maintain penalties as part of our regulatory toolkit. To this extent we have stated in our policy that we consider penalties as a likely last resort in terms of taking enforcement action. Whilst recognising that the use of enforcement tools such as reparations and orders can often be highly effective, the particular circumstances of a case might nonetheless mean that a financial penalty is the most suitable sanction.

We asked for views on the table which sets out our indicative levels of penalties based of the seriousness of a licence breach. Feedback from stakeholders suggests that the table is useful in highlighting the five levels of seriousness and the likely level of a penalty. Our revised penalty table has been amended to include ‘up to’ monetary levels for each seriousness category and we have included more generic examples of action we would take within each level.

We have considered points raised in relation to linking executive remuneration and enforcement action. Whilst recognising that we do not have specific legislative powers to direct a licence holder to use senior level remuneration to fund any sanction in relation to breach we do see the benefit of being explicit in our policy in stating that we would expect a licence holder to consider the impact of enforcement action sanctioned by ORR when considering the performance of senior management and executive remuneration.

Reparations

What our consultation said

We have found that our current policy does not provide the flexibility in considering reparation offers which other regulators have and have used effectively. We propose to incentivise early admission and offers of redress by establishing in our policy that the absence of such offers will be a factor in our consideration of the appropriateness and size of any financial penalty. We think there is scope to improve our reparations process and add a stage into the current process which would enable consideration of reparations after a breach has been identified (either by ORR or by way of early admission by the licensee) but before we decide that a penalty is appropriate. We think that our three component parts of reparations – genuinely additional, appropriately targeted and proportionate to the harm done and deliverable – remain appropriate and we do not intend to make major changes to these. However, we think that ‘appropriately targeted and proportionate to the harm done’ is a desirable element of any offer of reparations, but should be flexibly applied.

Questions we asked our stakeholders

- Do you agree that licensees should be encouraged to make early admissions and to provide public apologies?
- Do you agree ORR should revise its enforcement processes to enable offers of reparations to be considered in each of the following circumstances on a flexible basis depending on the circumstances of the case?

Early in the investigation process where a licence holder provides an admission, apology and suitable offers of reparations;

Before considering a penalty; and,

As a mitigating factor once it has been decided that a penalty is appropriate and the level of penalty is being set?

- Do you agree that ORR's enforcement policy and penalties statement should incentivise non-compliant licence holders to offer early admission and offers of reparations by stating that the absence of such offers will be considered when:
 - a) deciding whether a financial penalty is appropriate; and
 - b) identifying factors informing the level of any penalty.

Summary of responses to our consultation

Responses support the use of reparations at any point of the enforcement process. One response stressed that reparations should be used to remedy harm caused and there should be transparency around where the reparations are funded.

Respondents generally agreed that licensees should be encouraged to make early admissions where appropriate as this will reduce the overall burden of a regulatory investigation and enable both ORR and the licence holder to deal with a possible breach situation quickly and decisively.

There was support for licence holders to be encouraged to make early admissions and to provide public apologies. One licence holder supported this action as early admission is likely to lead to early action to remedy issues for the benefit of passengers. Properly planned and executed reparations, where the rail user can see and enjoy the tangible benefits, was thought to be a far better outcome than a fine and the ORR must be more proactive in encouraging this approach from the rail industry.

Consideration of responses

We have updated the policy to be more explicit on the approach to reparations and where they fit within our enforcement policy. Our previous policy did not provide any detail on how we would consider an offer of reparations from a licence holder and the criteria for our consideration of these offers. These are:

- **Genuinely additional** (for example, to the franchise agreement or all the commitments already made to us, funders, operators etc.). In order to confirm that reparations are not already part of an existing franchise commitment ORR will consult the relevant franchising authority, for example DfT, Transport Scotland, Transport for London (TfL) or London Underground Ltd. (LUL). We will also check to ensure that the offer is additional to existing commitments made through periodic reviews or other obligations;

- **Provides value for money:** The licence holders need to show that offer is value for money and has regard to ORR's section 4 duties. Value for money in this context means the benefits of the reparations exceeds the costs using a standard cost/benefit methodology.
- **Appropriately targeted and proportionate** to the harm done. That is, the reparations being offered are sufficient to compensate for the harm done to a meaningful degree and are targeted at those that suffered, as far as is practicable. We will consult with the appropriate passenger organisations when considering this.
- **Deliverable** that is, the licence holder needs to set out clearly how it proposes to deliver the reparations proposed.

We have also said that we will consider offers of reparations at the earliest possible stage. Previously we could only consider an offer once a breach had been found and as a mitigation of a penalty.

Enforcement orders

What our consultation said

We would like to use enforcement orders more innovatively to get licence holders to remedy issues as quickly as possible – utilising a range of activities which engage the industry, where appropriate; these could include taskforces, recovery boards, joint recovery plans. We consider that provisional orders offer a real opportunity to take targeted and swift actions in circumstances where it is clear that the required process for making a final order will impact on the loss and damage suffered by any person as a result of the licence breach

Questions we asked our stakeholders

- Do you agree ORR should revise its enforcement policy and processes to reflect a more effective use of provisional and final orders, in particular, to enable ORR to be more proactive and forward looking?

Summary of responses to our consultation

There was general support for the use of more enforcement orders – final and provisional.

Responses said that enforcement orders can be an appropriate way of holding a licence holder to account and requiring that it takes the necessary steps to remedy its failings. ORR's approach to the use of enforcement orders was seen to be appropriate.

There was support for more use of provisional orders however it was suggested that it is important that ORR sets out the criteria for these types of orders. There was also a number of responses which recognised that provisional orders should be used in matters where a licence holder is imminently about to undertake an action that has not been approved by ordinary contractual process, and therefore promoting the right behaviour.

It was suggested that any actions which result from provisional and final orders have to be tangible. It is not enough to simply produce a 'plan'- the outcomes, benefits to rail users and timescales have to be clear and focused and the ORR must ensure that they are delivered in full.

Consideration of responses

The policy has been updated to reflect our approach to final and provisional orders. We will continue to consider the option of provisional orders when weighing up the best form of action where we have concerns.