



OFFICE *of*
RAIL REGULATION

**Enforcement policy
and
penalties statement –
draft for consultation**

November 2005

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Summary

1. This document sets out the Office of Rail Regulation's (ORR) enforcement policy as economic regulator and contains the penalties statement required by section 57B of the Railways Act 1993 (as amended)(the Act). ORR recently consulted on a proposed health and safety enforcement policy in anticipation of the transfer to ORR of responsibility for safety regulation of the rail industry.
2. The purpose of this document is to describe how we use our licence enforcement powers to ensure that the public interest is protected, that the industry delivers a safe, high quality, and efficient service to passengers and freight customers which represents value for money, and to be transparent as to the approach we are likely to adopt in individual cases.
3. We are consulting on both the enforcement policy in Chapter 3 and the penalties statement in Chapter 4.

General approach

4. The purpose of enforcement is to ensure delivery and secure compliance with public interest obligations. Enforcement is one of ORR's key functions, and we shall use our powers firmly but fairly. ORR monitors the industry's compliance with obligations in licences to ensure that the public interest is protected. We aim to ensure that monitoring and enforcement is proportionate to the issue. As a matter of policy, we focus on systemic issues. Monitoring takes several forms, including analysis of regular reports on industry performance, including those from independent regulatory reporters, discussions with industry stakeholders on current issues, and investigation of complaints. Where there is an area for concern, we shall adopt a staged approach of investigation and escalation, leading ultimately to the consideration of enforcement action.

Licence enforcement and competition law enforcement

5. ORR has significant enforcement powers under the Act and under the Competition Act 1998. ORR's approach to competition law enforcement is set out in its recently updated guideline¹.
6. Where there is (or is likely to be) a contravention by an industry party of a licence obligation, we must first choose whether to act under the licence or under competition law. We shall generally seek to use the most effective remedy, taking into account a number of factors (for more details on these, see Chapter 3).

Licence enforcement

7. If we choose to use our licence enforcement powers, section 55 sets out what we may do and how we go about it. This is described in detail in Chapter 2.
8. Broadly, if we take enforcement action, we have the option of issuing a provisional order or a final order. A provisional order is, in effect, an interim measure for cases of urgency and may last no more than three months. The final order or provisional order will set out the steps the licence holder needs to take to remedy the breach within a given timescale.
9. In taking enforcement action, we may levy a financial penalty or include in the order a reasonable sum which will be payable if the licence holder fails to comply with the order. We may also levy a financial penalty for breach of a licence condition, even if no order has been made, or following failure to comply with an order, only if no sum was included in the order.

Enforcement principles

10. In considering the enforcement of licences, we shall act in accordance with section 55 and section 4 of the Act, which require us to balance a number of public interest duties. Our approach is informed by best regulatory practice and the following principles:
 - proportionality - we shall focus our monitoring and investigation of potential breaches on those aspects of compliance which are most

¹ ORR Competition Law Guideline: Application to Services Relating to Railways, Office of Fair Trading, October 2005 <http://www.rail-reg.gov.uk/upload/pdf/OFT430.pdf>

important for users and funders, where non-compliance would cause most harm and where there has been a sustained failure;

- consistency - consistency of approach does not mean uniformity. It means taking a similar approach in similar circumstances to achieve similar ends. Through the adoption of common principles, and consideration of the approach adopted by others, we shall try to ensure consistency in our approach to regulating the industry;
- targeting – our policy is generally to focus on using our regulatory powers to resolve systemic issues that are not effectively dealt with in contractual relationships;
- transparency – we shall help the industry to understand what is expected of it and what they in turn should expect from ORR. This means publishing our decisions and the reasons for them and ensuring that we are open about the action we are taking; and
- accountability - regulators are accountable to the public for their actions through the courts and through Parliament. We consult on and publish our policies and keep them under review to ensure they remain fit for purpose.

Penalties

11. We are consulting on our statement on penalties in accordance with section 57B of the Act.
12. The statement covers both the levying of a penalty for a breach or for failure to comply with an enforcement order and the inclusion of a “reasonable sum” in a final order to be paid in the event of failure to deliver.
13. In summary, our policy is that:
 - the penalty or sum should be proportionate to the nature and severity of the breach. In some cases, this may lead to no penalty or sum being required, but, in other cases, the potential penalty or sum may be substantial;
 - the size of the penalty or sum should be greater than the cost of compliance and should reflect the harm caused;

- there may be a number of mitigating or aggravating factors; and
- we shall consider imposing a penalty or sum on any licence holder, irrespective of its legal status.

1. Introduction

1. This document describes the Office of Rail Regulation's (ORR) general approach to the use of its enforcement powers and the levying of financial penalties in its role as economic regulator for rail. It includes the penalties statement required by section 57B of the Railways Act 1993 (as amended) ("the Act"). A separate document has been published² describing ORR's proposed health and safety enforcement policy following the transfer of responsibility for safety regulation from the Health and Safety Executive (HSE). We shall review our approach to enforcement of matters where there are both safety and economic considerations following the merger of safety and economic regulation next year.
2. ORR's principal powers as economic regulator lie in the Act, and, as a competition authority for rail, in the Competition Act 1998, the Enterprise Act 2002 and under Articles 81 and 82 of the European Treaty. This document concentrates on our licence enforcement powers and policy and their relationship with our competition powers and other remedies. It also sets out ORR's policy on financial penalties in accordance with section 57B of the Act. We have published, with the Office of Fair Trading (OFT), a revised guideline³ describing how we shall exercise our competition powers following the modernisation of EU competition law.
3. The aim of this policy statement is to ensure that the railway industry, funders, passengers and freight customers understand ORR's approach, and the circumstances in which we shall use our powers to ensure delivery and secure the public interest. A published policy also provides transparency about our approach to individual cases. The circumstances of each individual case are different, however, and we shall consider each case on its merits. In the case of licence enforcement action, we shall consider each case in accordance with our duties under section 4 of the Act (set out at Annex A) and with the requirements of section 55 of the Act (as set out in Chapter 2).

² ORR Health and safety enforcement policy statement, Office of Rail Regulation, October 2005. <http://www.rail-reg.gov.uk/upload/pdf/254.pdf>.

³ ORR Competition Law Guideline: Application to Services Relating to Railways, Office of Fair Trading, October 2005 <http://www.rail-reg.gov.uk/upload/pdf/OFT430.pdf>.

4. This document describes:
- the legal framework for licence enforcement and for competition law enforcement;
 - the purpose of monitoring and enforcement;
 - the factors we shall consider in deciding whether to use our licence enforcement or competition law enforcement powers, or whether to rely on the application of other remedies;
 - the principles we shall apply to its enforcement of licences generally; and
 - ORR's statement on financial penalties.
5. This is a consultation document. Technically, the consultation is in two parts: on ORR's enforcement policy and on ORR's penalties statement. The latter is a statutory requirement under section 57B(5) of the Act. We shall consider comments made before publishing the final version of this document, alongside the final version of our health and safety enforcement policy.
6. Comments on the draft enforcement policy and penalties statement should be sent, by 8 February 2006, and preferably by e-mail, to:
- Abigail Grenfell (abigail.grenfell@orr.gsi.gov.uk)
Manager, Network Regulation
Office of Rail Regulation
1 Waterhouse Square
138-142 Holborn
London
EC1N 2TQ
Tel: 020 7282 2093
7. Respondents should indicate clearly if they wish all or part of their responses to remain confidential to ORR. Otherwise, you should expect that your response will be placed in the ORR library and on our website and may be quoted from by us.
8. Where your response is made in confidence, it would be helpful if you could include a statement we can publish summarising the submission but excluding confidential information.

9. We may also publish your name in future documents or on our website, unless you indicate that you wish your name to be withheld.

2. The legal framework

The legal framework for licence enforcement

1. All operators of railway assets are required to hold an appropriate licence or licence exemption granted either by ORR or by the Secretary of State in accordance with sections 6 to 9 of the Act and associated regulations. Under regulations implementing the First Package of EU Rail Directives, ORR also has the power to grant European licences (valid throughout the EU) to “railway undertakings”, meaning most passenger and freight train operators⁴.
2. Licences contain a number of conditions or regulatory provisions with which the licence holder must comply. Where there is an apparent failure to comply with the terms of a licence condition, there is a legal framework for licence enforcement. This is summarised below.

Orders for securing compliance

Final order

3. Under section 55 of the Act, where ORR is satisfied that the licence holder is contravening, or is likely to contravene, a condition, it **must** take enforcement action by making a final order, unless:
 - (a) it considers it requisite that it should make a provisional order⁵ (see below); or
 - (b) one of the relevant statutory exceptions applies, namely:
 - (i) ORR’s section 4 duties preclude it from making the order⁶;

⁴ This will result, where necessary, in these train operators’ existing licences being replaced by a European licence and a statement of regulatory provisions, containing those requirements which are outside the standard European licence. The policy described in this document applies to the latter.

⁵ Section 55(2).

⁶ Section 55(5)(a).

- (ii) ORR is satisfied that the most appropriate way of proceeding is under the Competition Act 1998⁷; or
- (c) the section 55(5B) exception applies. This applies if ORR is satisfied that:
 - (i) the licence holder has agreed to take, and is taking, all such steps as it appears to ORR for the time being appropriate to take for the purpose of securing or facilitating compliance with a condition; or
 - (ii) the contravention or apprehended contravention will not adversely affect the interests of users of railway services or lead to any increase in public expenditure,
 in which case, it shall only make the final order if it considers it appropriate to do so.⁸

Provisional order

4. A provisional order is, in effect, an interim measure for cases of urgency and may last for no more than three months. ORR may make a provisional order without going through the procedural steps required for a final order where it appears to ORR that it is requisite that a provisional order be made. In considering what is requisite, ORR must have regard in particular to the extent to which someone is likely to sustain loss or damage from the breach *before a final order may be made*.
5. A provisional order will expire at the end of the period stated in the order (no more than three months) unless ORR “confirms” it by making a final order. The requirements for confirming a provisional order are substantially the same as for making a final order (see paragraph 3 above).⁹

Contents of final and provisional orders

6. A final or provisional order must make such provision as is requisite to secure compliance with the condition. In particular, it must specify:

⁷ Section 55(5A).

⁸ Section 55(5B).

⁹ Section 55(4).

- (a) what the licence holder is required to do, or not to do; and
 - (b) the time when it takes effect (being the earliest practicable time).
7. An order may include a reasonable sum to be paid by the licence holder for failure to comply with the order. ORR may also levy a financial penalty for breach of licence (see Annex B).

Substantive test to be satisfied to make final order

8. Thus, there is an **obligation** on ORR to make an enforcement order if it is “satisfied” that a condition is being contravened or is likely to be contravened¹⁰ **unless** one of the statutory exceptions applies. Whenever the statutory exceptions (except section 55(5B)) apply, ORR is **precluded** from making a final order. Under section 55(5B), ORR may still impose a final order even where the substantive elements of the exception are satisfied, “if it considers it appropriate to do so”.
9. If ORR decides not to make a final order, or not to make or confirm a provisional order in respect of a licence breach, because we consider that one of the statutory exceptions applies, ORR must, under section 55(6) of the Act, serve notice of that fact on the licence holder and publish the notice. Although the Act does not specifically require ORR to set out in the notice our reasons for making such a decision, we would, as a matter of policy expect to do so.

The legal framework for competition law enforcement

10. ORR’s approach to its competition law powers is set out in its revised guideline available on the ORR website¹¹.
11. In summary, ORR may:
- (a) consider complaints about possible infringements of Article 81 and/or Article 82 of the European Treaty or the Chapter I and/or Chapter II prohibitions of the Competition Act 1998;

¹⁰ Section 55(1).

¹¹ ORR Competition Law Guideline: Application to Services Relating to Railways, Office of Fair Trading, October 2005 <http://www.rail-reg.gov.uk/upload/pdf/OFT430.pdf>

- (b) impose interim measures to prevent serious and irreparable damage;
- (c) carry out investigations both on its own initiative and in response to complaints, including requiring the production of documents and information and searching premises;
- (d) impose financial penalties on an undertaking up to a maximum of 10% of its worldwide turnover in the business year preceding the date of the decision, taking into account the statutory guidance on penalties issued by the OFT;
- (e) issue and enforce directions to bring an infringement to an end;
- (f) apply Article 81(3) criteria to agreements which may breach Article 81, or section 9 criteria to agreements which may breach the Chapter I prohibition;
- (g) accept commitments that are binding on an undertaking in lieu of a decision;
- (h) publish written guidance, in the form of an Opinion, where a case raises novel or unresolved questions about the application of competition law in the rail sector and where ORR considers there is an interest in issuing clarification for the benefit of a wider audience; and
- (i) make a market investigation reference to the Competition Commission (CC) under part 4 of the Enterprise Act 2002.

3. ORR's enforcement policy

The purpose of monitoring and enforcement

1. The railway is a public service operated by the private sector. Regulation exists to ensure that the public interest is protected and that the industry delivers a safe, high quality and efficient service to passengers and freight customers which represents value for money.
2. ORR's general approach¹² to economic regulation of the rail industry is to:
 - ensure that the right incentives are in place for the industry to meet public interest objectives;
 - facilitate and encourage the industry to deliver safe and efficient services which meet the reasonable requirements of users and funders; but also
 - use our enforcement powers, where appropriate, to ensure that the industry works in the public interest.
3. Enforcement is one of ORR's key functions, and we shall use our powers firmly but fairly. **The purpose of enforcement is to ensure delivery and secure compliance with public interest obligations.** The possibility of enforcement provides an assurance to users and funders that the railway will be accountable for delivery, and acts as an incentive for the industry to deliver in accordance with the public interest.
4. ORR has substantial powers at its disposal. We have powers under the Act to enforce licences granted to Network Rail and other infrastructure operators, train operators, station operators and light maintenance depot operators, which contain a number of conditions reflecting public interest requirements. We are also a competition authority with powers to enforce UK and European competition law in relation to railways in Great Britain. ORR does not enforce *contracts* between industry parties, although in many cases we approve or direct the terms.

¹² This is described in ORR's corporate strategy. ORR will be consulting shortly on its corporate strategy for 2006-09.

5. There is a range of enforcement tools available. These include requiring (and ensuring delivery of) recovery plans, making provisional and final enforcement orders, and imposing financial penalties. Annex C lists, by way of background, the occasions on which we have taken licence enforcement action in the past.
6. ORR will consider each case on its merits and the statements in this document must be considered in that context. However, we recognise that the industry, its funders, and wider stakeholders wish to understand how we shall use our powers, and our general approach is therefore set out below.

Monitoring and investigation

7. ORR monitors the industry's performance to ensure that it acts in the public interest. Depending on the issue, monitoring takes several forms. These include analysis of regular reports on industry performance, discussions with industry stakeholders on current issues, and investigation of complaints. We publish regular reports on the industry's performance, including National Rail Trends, the Network Rail Monitor, and our annual assessment of Network Rail's performance. As a matter of policy, we focus on systemic issues. However, we also have a duty under section 68 of the Act to investigate any complaint about an alleged or apprehended contravention of a licence condition, unless it is frivolous or vexatious.
8. Where there is cause for concern, we shall adopt a staged approach of investigation and escalation, leading ultimately to consideration of enforcement action. This includes one or more of the following:
 - researching and analysing specific areas of potential under-performance;
 - considering the findings of independent regulatory reporters;
 - carrying out investigations, including formal investigations under competition law;
 - requiring an explanation from the undertaking responsible;
 - highlighting the issue publicly;
 - considering whether there has been a breach of a licence condition or competition law;
 - if appropriate, requiring a recovery plan; and

- taking steps to secure compliance.

Choices between licence enforcement, competition law, and other remedies

9. ORR will not generally, as a matter of policy and good practice, seek to use different enforcement mechanisms simultaneously. We may however decide to switch between enforcement mechanisms if the circumstances of the case indicate that an alternative mechanism would be more appropriate.
10. Where a problem is found to exist, we shall consider the most effective, efficient and expeditious solution, in the light of our legal obligations. Under the Act, ORR must decide whether to use competition law or licence enforcement. More generally, there may be remedies available:
 - at ORR's disposal, for example in the Act, the Competition Act 1998, the Enterprise Act 2000, health and safety legislation or legislation implementing European law;
 - in the hands of other public authorities, for example in health and safety legislation, rail franchises, legislation implementing EU railway law or environmental legislation or elsewhere; or
 - in the hands of the industry, for example in contracts.
11. Where there is a choice of remedy or enforcement mechanism available to ORR, we are likely to consider:
 - (a) the remedies at ORR's disposal;
 - (b) the ability of the industry to utilise contractual remedies;
 - (c) the effectiveness of each remedy;
 - (d) the speed of resolution;
 - (e) the need for ongoing regulation of the issue (using our powers under the Act, rather than other monitoring or enforcement mechanisms);
 - (f) cost;
 - (g) the ability of third parties to seek damages or compensation;

- (h) whether there may be benefit in establishing a precedent in competition law; and
- (i) any other factors relevant to the specific case.

The principles of enforcement

12. ORR's approach is one of firm but fair enforcement. In considering the enforcement of licences, we shall act in accordance with section 55 and section 4 of the Act (see Annex A), which require us to balance a number of public interest duties. Our approach is informed by best regulatory practice and the following principles¹³: *proportionality* in applying the law and securing compliance; *targeting* of enforcement action; *consistency* of approach; *transparency* about how we operate and what the industry may expect; and *accountability* for our actions in line with best practice in regulation. These principles apply both to enforcement in particular cases and to management of monitoring and enforcement activities as a whole.

Proportionality

13. ORR oversees the compliance of all licence holders with the conditions of their licences and has a duty under section 68 of the Act to investigate complaints about alleged or potential breaches.
14. We shall focus our monitoring and investigation of potential breaches on those aspects of compliance which are most important for users and funders and where non-compliance would cause most harm.
15. Some licence obligations are specific and absolute; others require judgement, or an assessment of the adequacy of the licence holder's performance. We shall apply the principle of proportionality to both types of licence obligation. The level of monitoring undertaken by ORR varies from condition to condition, depending on the nature of the obligation, the consequences of the licence holder breaching the condition for other industry parties, passengers, freight customers, funders and other stakeholders, and our section 4 duties. Methods of monitoring include use of independent regulatory reporters, analysis of regular reports and industry information, feedback from industry stakeholders,

¹³ These are the principles of the Better Regulation Task Force, and reflect those used by the Health and Safety Commission (HSC) in respect of safety enforcement policy.

and regular discussions with licence holders and other stakeholders. Where there has been a particular problem in compliance, we may monitor more closely. Where there are potential areas for concern, we shall consider what action is being taken by the licence holder to resolve them and whether any action by ORR is required.

16. We shall consider carefully the circumstances of individual cases when considering whether to take enforcement action. We are likely to take account of the following factors:
 - (a) the extent to which the licence holder has a robust, adequately resourced plan to achieve compliance within a reasonable period of time;
 - (b) whether it would encourage greater effort on the part of the licence holder to remedy the breach;
 - (c) any persistent non-compliance; and
 - (d) the effect on third parties and their potential right to compensation.

One-off failures

17. We shall generally focus our resources and priorities on sustained failure to deliver outputs or on individual events of material significance, rather than on one-off minor failures. This is because, in some cases, outputs may fluctuate over a short period of time. For example, train delays fluctuate from day to day and have to be considered over a reasonable period of time. In other cases, the significance of a licence holder missing a deadline or target will depend on the overall effect on users, funders and other relevant stakeholders. We shall, however, investigate complaints about one-off failures and consider enforcement action where it is in the public interest and in accordance with the requirements of section 55 of the Act.

Targeting

18. ORR's policy is to focus on using its regulatory powers to resolve systemic issues that are not effectively dealt with in contractual relationships. These relationships include access contracts, the Network Code, and in due course the Stations Code and Depots Code, as well as industry wide arrangements

on ticketing. We do not monitor compliance with contractual obligations and the ordinary rules of private law apply to them. We expect the industry to manage its contractual relationships effectively and to explore the mechanisms in those contracts to secure compliance.

19. ORR will give priority to enforcing obligations in licences where there is a detrimental effect on users, funders and other stakeholders. Subject to the specific requirements of individual licence conditions, we shall normally adopt the above approach in considering whether to take enforcement action.

Consistency

20. Consistency of approach does not mean uniformity. It means taking a similar approach in similar circumstances to achieve similar ends. We shall normally explain the reasons for any apparent differences in approach. Through the adoption of common principles, including those set out in this document, through consideration of the approach taken by other authorities, and by being transparent in our actions, we shall aim to ensure consistency in our approach to regulation of the industry.

Transparency

21. Transparency means helping the industry to understand what is expected of it and what it should expect from ORR. It means publishing our decisions and the reasons for them and ensuring that we are open about the action we are taking.
22. ORR publishes periodic information on the performance of the industry and of Network Rail in particular. When we are concerned about an aspect of industry performance, we shall make this clear.
23. When considering whether to take action under competition law or under the Railways Act 1993, we shall make it clear to interested parties which route we propose to adopt and shall notify them of any subsequent change in approach.
24. When taking or proposing enforcement action, we shall give our reasons.
25. We recognise that the industry we regulate must be able to understand why we are concerned about a particular issue, the options open to us, and any rights of appeal or complaint. Therefore:

- we shall always explain why we are concerned, whether we are taking formal action, and where we are, and the next steps; and
- where we require an undertaking to take steps to remedy the position, we shall seek its views before including any steps in formal action.

Accountability

26. Regulators are accountable to the public for their actions through Parliament¹⁴ and through the courts. We have an obligation to give written and oral evidence to the Committees of Parliament and to make an annual report to the Secretary of State for Transport and lay it before Parliament. We are subject to scrutiny by the National Audit Office and are answerable to the Parliamentary Commissioner for Administration in cases of alleged maladministration.
27. We also have an obligation to comply with the rules of administrative law and good public administration. We consult on, and publish, our policies and keep them under review to ensure that they remain fit for purpose. We also consult on our corporate strategy. As a matter of policy and good practice, we shall consider any representations made to us about our approach to monitoring, enforcement, or the levying of penalties and we shall respond to them. Ultimately, our decisions are subject to judicial review and scrutiny by the courts. A licence holder aggrieved by an enforcement order we have made also has a specific right of appeal to the court under section 57 of the Act.

Application of ORR's enforcement policy

28. Examples of our approach to enforcement of Network Rail's network licence and of train operators' licences are outlined below. Different licence conditions will require different approaches to ensuring compliance, depending on the nature of the condition and of the alleged or potential breach. We are happy to provide further details to interested parties of our likely approach to specific issues on a case-by-case basis.

Network Rail

29. One of the most important licence conditions is Condition 7 of Network Rail's network licence. Condition 7 requires (inter alia) the company to:

¹⁴ Both in Westminster and in Scotland.

“secure -

- (a) the operation and maintenance of the network;
- (b) the renewal and replacement of the network; and
- (c) the improvement, enhancement and development of the network,

in each case in accordance with best practice and in a timely, efficient and economical manner so as to satisfy the reasonable requirements of persons providing services relating to railways and funders in respect of:

- (i) the quality and capability of the network; and
- (ii) the facilitation of railway service performance in respect of services for the carriage of passengers and goods by railway operating on the network.

General duty

The licence holder shall take such steps as are necessary or expedient so as to achieve the purpose to the greatest extent reasonably practicable having regard to all relevant circumstances including the ability of the licence holder to finance its licensed activities.”

- 30. ORR considers that Condition 7 applies to Network Rail’s management of both the network as a whole and individual parts of it. So if Network Rail is meeting outputs at a network-wide level, but is failing on a significant part of the network, we shall investigate the reasons for this and shall consider enforcement action.
- 31. In monitoring and enforcing compliance with Network Rail’s network licence, we shall examine Network Rail’s efficient operation, maintenance, renewal and development of the network, and review whether Network Rail is meeting the reasonable requirements of its customers and funders under Condition 7. We consider that reasonable requirements are likely to include:
 - outputs established in a periodic review;

- disaggregated outputs established as a result of the transfer of responsibility for funding infrastructure in Scotland to Scottish Ministers;
 - firm commitments included in Network Rail's business plan (including route plans); and
 - effective communication with customers and funders about the delivery of these outputs and commitments.
32. If Network Rail is failing to deliver an output which ORR determines is a reasonable requirement, ORR will go on to consider whether, in the circumstances of the case, Network Rail is fulfilling the general duty.

Other operators

33. The monitoring and enforcement of other operators' licences has changed following the Railways Act 2005. This removed the distinction between consumer protection and other licence conditions created at the time of the establishment of the Strategic Rail Authority (SRA) in the Transport Act 2000. This is discussed in more detail in ORR's licensing review consultation document¹⁵.
34. ORR is now responsible for the imposition and enforcement of all licence conditions, as it was from 1994 to 2000. However, the Department for Transport (DfT)¹⁶ has assumed various approval roles under the terms of conditions dealing with disabled persons protection, through ticketing, impartial retailing, the National Rail Enquiry Service (NRES), complaints handling, and general liaison with the Rail Passengers Council. This reflects the synergies between those issues and franchising, fares policy and DfT's other statutory responsibilities. DfT will also be responsible for routine monitoring of compliance with the arrangements it approves, many of which also appear in franchise agreements. For these matters, consideration by ORR of enforcement action will normally take account of advice from the DfT. In addition, we have a duty under section 68 of the Act to investigate proactively any complaints about alleged or potential licence breaches, and

¹⁵ Licensing review: Consultation, Office of Rail Regulation, August 2005 <http://www.rail-reg.gov.uk/upload/pdf/246.pdf>.

¹⁶ And the Scottish Executive in Scotland.

we shall also take action on our own initiative where it is appropriate to protect the interests of users and funders.

35. ORR's routine monitoring will focus on those conditions in operator licences not being monitored by DfT. This will include, for example, monitoring to ensure that passenger train operators play their part in providing advance timetable information and that all operators hold appropriate insurance cover against third party liabilities. Under European legislation due to be implemented shortly in the UK, we shall also need to be satisfied that train operators are of good repute, comply with safety requirements and have the necessary financial resources to satisfy European licensing rules, without this becoming an undue barrier to entry to the market.

4. Penalties statement

1. Section 57B of the Act (introduced by section 225 of the Transport Act 2000) requires ORR to, “prepare and publish a statement of policy with respect to the imposition of penalties and the determination of their amount”. Turnover regulations made by the Secretary of State under by the Transport Act 2000¹⁷ (the turnover regulations) became law on 3 August 2005.
2. Under section 57B of the Act, ORR must undertake appropriate consultation in preparing the statement of policy. We must also have regard to the statement in deciding whether to impose penalties and reasonable sums and in determining their amount. Any penalties or sums are paid to the Secretary of State and/or Scottish Ministers as appropriate.
3. This penalties statement relates to licence enforcement under the Act and covers both the levying of a penalty (under section 57A(1)) and the inclusion of a reasonable financial sum (under section 55(7A)) in an individual enforcement order. Penalties under the Competition Act 1998 are governed by statutory guidance on penalties, issued by the Office of Fair Trading,¹⁸ and associated turnover regulations¹⁹.
4. Procedural requirements relating to the imposition of penalties are set out in Annex B of this document.

General approach

5. In deciding whether it would be appropriate to impose a penalty or include a reasonable sum in an order, we shall take full account of the particular facts and circumstances of the contravention, including any representations and objections made to us, and shall act in a manner best calculated to fulfil the duties placed upon us by section 4 of the Act. We shall take account of the

¹⁷ The Railways Act 1993 (Determination of Turnover) Order 2005, SI 2005/2185

¹⁸ OFT 423, Guidance as to the appropriate amount of a penalty, published 21 December 2004

¹⁹ The Competition Act 1998 (Determination of Turnover for Penalties) Order 2000 (SI 2000/309) (as amended by the Competition Act 1998 (Determination of Turnover for Penalties) (Amendment) Order 2004 (SI 2004/1259))

five principles of good regulation: proportionality, targeting, consistency, transparency, and accountability.

6. The penalty or sum should be proportionate to the nature and severity of the breach. In some cases, this may lead to no penalty or sum being required but, in other cases, the potential penalty or sum may be substantial.
7. We shall, in particular, consider:
 - (a) the seriousness of the breach;
 - (b) whether the breach or possibility of the breach would have been apparent to a diligent licence holder;
 - (c) culpability;
 - (d) the extent to which a penalty or reasonable sum would provide additional incentives on the licence holder to remedy the breach;
 - (e) the impact the breach has had on third parties;
 - (f) whether the licence holder has profited from the breach; and
 - (g) the licence holder's record of compliance or non-compliance with this and other obligations.
8. The legal status of the licence holder (for example, whether it is a publicly listed company, an unlisted company or a company limited by guarantee) and any dependency on public funds of itself will not influence a decision to impose a reasonable sum or levy a financial penalty.

Calculating the amount of a penalty or sum payable

9. When assessing the amount of a penalty or reasonable sum to be imposed, ORR is likely to consider a number of factors falling into three categories:
 - (a) proportionality;
 - (b) mitigating and aggravating factors; and
 - (c) financing issues.

Proportionality

10. Our principal objective in setting a penalty or imposing a reasonable sum would be to incentivise compliance with the relevant condition or requirement. Given this objective, we consider that any potential penalty or sum imposed should be greater than the cost of compliance, such that it will be more expensive for the licence holder to continue in breach of its licence condition rather than to comply.
11. In setting the level of the penalty, we shall have regard to the following factors:
 - (a) the cost of compliance;
 - (b) the costs incurred by third parties as a result of the breach (net of any compensation through contractual remedies or other settlements); and
 - (c) any benefit from non-compliance enjoyed by the licence holder.
12. The principle we intend to use would therefore result in a penalty or sum set at the minimum level required to incentivise compliance.

Adjustments for mitigating or aggravating factors

13. Additional factors may also be considered, depending on the particular facts and circumstances of a specific individual case. ORR may consider the following factors as mitigation, resulting in a decrease in the level of a penalty or sum:
 - (a) any remedial steps the licence holder may have taken to rectify the breach, including whether these were initiated by the licence holder or in response to ORR's actions;
 - (b) any steps taken to minimise the risk of the breach recurring;
 - (c) co-operation with ORR's investigation; and
 - (d) evidence that the breach was genuinely accidental or inadvertent.
14. Other mitigating or aggravating factors may arise in a specific case.

15. The following factors may be considered by ORR as aggravating the breach, resulting in an increase in the level of a penalty or sum²⁰:
- (a) whether any infringement is deliberate or reckless;
 - (b) repeated infringement of this or other obligations, particularly if subsequent breaches occur after the licence holder becomes aware of, or is made aware of, the initial infringement;
 - (c) the extent of involvement of directors or senior management in the action or inaction which caused the breach or their lack of involvement in action to remedy the breach;
 - (d) the absence of internal procedures intended to prevent infringements occurring and the extent to which organisational weakness may result in repeated infringements of the same type by the same licence holder; and
 - (e) evidence that the licence holder attempted to conceal the infringement from ORR.

Financing issues

16. Under section 4 of the Act, ORR is required to act in a manner that does not make it unduly difficult for a network licence holder to finance those activities relevant to ORR's functions. We also have a duty to enable others to plan their businesses with a reasonable degree of assurance. We shall take these requirements into consideration in setting the amount of a penalty or sum.
17. However, we consider that these duties do not require us to protect a firm from its own inefficiency. In the event that ORR concludes, having regard to the particular facts and circumstances, that it would be appropriate to impose a monetary penalty or sum, sufficient to incentivise compliance, it would, in our view, be inappropriate to refrain from doing so merely because this would make it difficult for an inefficient operator to finance its functions.
18. Having considered, to the extent appropriate, the factors listed above and the nature and severity of the breach, ORR will determine an appropriate amount

²⁰ Ibid

for a financial penalty or sum. In doing so, we shall ensure that the amount determined does not exceed 10 % of the turnover of the licence holder (as determined in accordance with the turnover regulations) and that it is consistent with our statutory duties in section 4 of the Act.

Revision of the statement of policy

19. ORR may, from time to time, revise this statement, in accordance with section 57B(4) and (5) of the Act.

Annex A – ORR’s statutory duties

The Office of Rail Regulation (ORR) must discharge the statutory duties placed upon it by section 4 of the Railways Act 1993 (as amended by the Transport Act 2000 and the Railways Act 2005²¹)²².

Section 4 of the Railways Act 1993 – General duties of the Secretary of State and the Office of Rail Regulation

- (1) The Office of Rail Regulation shall have a duty to exercise the functions assigned or transferred to it under or by virtue of this Part or the Railways Act 2005 that are not safety functions in the manner which it considers best calculated —
- (zb) to promote improvements in railway service performance;
 - (a) otherwise to protect the interests of users of railway services;
 - (b) to promote the use of the railway network in Great Britain for the carriage of passengers and goods, and the development of that railway network, to the greatest extent that it considers economically practicable;
 - (ba) to contribute to the development of an integrated system of transport of passengers and goods;
 - (bb) to contribute to the achievement of sustainable development;
 - (c) to promote efficiency and economy on the part of persons providing railway services;
 - (d) to promote competition in the provision of railway services for the benefit of users of railway services;

²¹ All the section 4 duties are included here, including those in the Railways Act 2005 which have not yet been implemented.

²² ORR also has an overriding duty in section 21 of the Channel Tunnel Rail Link Act 1996 to exercise its regulatory functions in such a manner as not to impede the performance of any development agreement.

- (e) to promote measures designed to facilitate the making by passengers of journeys which involve use of the services of more than one passenger service operator;
 - (f) to impose on the operators of railway services the minimum restrictions which are consistent with the performance of its functions under this Part or the Railways Act 2005 that are not safety functions;
 - (g) to enable persons providing railway services to plan the future of their businesses with a reasonable degree of assurance.
- (2) Without prejudice to the generality of subsection (1)(a) above, the Office of Rail Regulation shall have a duty, in particular, to exercise the functions assigned or transferred to it under or by virtue of this Part or the Railways Act 2005 that are not safety functions in the manner which it considers is best calculated to protect—
- (a) the interests of users and potential users of services for the carriage of passengers by railway provided by a private sector operator otherwise than under a franchise agreement, in respect of—
 - (i) the prices charged for travel by means of those services, and
 - (ii) the quality of the service provided, and
 - (b) the interests of persons providing services for the carriage of passengers or goods by railway in their use of any railway facilities which are for the time being vested in a private sector operator, in respect of—
 - (i) the prices charged for such use; and
 - (ii) the quality of the service provided.
- (3) The Office of Rail Regulation shall be under a duty in exercising the functions assigned or transferred to it under or by virtue of this Part or the Railways Act 2005 that are not safety functions—
- (a) to take into account the need to protect all persons from dangers arising from the operation of railways; and

- (b) to have regard to the effect on the environment of activities connected with the provision of railway services.
- (3A) Subsections (1) to (3) above shall have effect in relation to the Secretary of State as in relation to [the Office of Rail Regulation], except that in their application to the Secretary of State—
 - (a) ...
 - (b) the references in each of the subsections to the functions transferred or assigned to the Secretary of State under or by virtue of this Part include only the functions transferred or assigned to him under or by virtue of sections 6 to 22 and 37 to 50 below; and
 - (c) the references in each of the subsections to the functions transferred or assigned under or by virtue of the Railways Act 2005 include only the functions transferred or assigned to the Secretary of State under or by virtue of the provisions of Part 4 of that Act other than section 39.
- (3B) Subsections (1) to (3) above shall have effect in relation to the Scottish Ministers as in relation to the Office of Rail Regulation except that, in relation to those Ministers—
 - (a) the references in each of the subsections to functions transferred or assigned to those Ministers under or by virtue of Part 1 of this Act include only the functions transferred or assigned under or by virtue of sections 16A to 16G of this Act; and
 - (b) the references in each of the subsections to the functions transferred or assigned under or by virtue of the Railways Act 2005 include only the functions transferred or assigned to those Ministers under or by virtue of Part 4 of that Act.
- (3C) Subsections (1) to (3) above shall have effect in relation to the National Assembly for Wales as in relation to the Office of Rail Regulation except that, in relation to that Assembly, the references in each of the subsections to functions transferred or assigned under or by virtue of Part 1 of this Act or the Railways Act 2005 include only the functions transferred to assigned to the Assembly under or by virtue of the provisions of Part 4 of that Act of 2005 other than section 39.

- (4) The Secretary of State shall also be under a duty, in exercising the functions assigned or transferred to him under or by virtue of this Part or the Railways Act 2005, to promote the award of franchise agreements to companies in which qualifying railway employees have a substantial interest, “qualifying railway employees” meaning for this purpose persons who are or have been employed in an undertaking which provides or provided the services to which the franchise agreement in question relates at a time before those services begin to be provided under that franchise agreement.
- (5) The Office of Rail Regulation shall also be under a duty in exercising the functions assigned or transferred to it under this Part or the Railways Act 2005 that are not safety functions—
- (a) to have regard to any general guidance given to it by the Secretary of State about railway services or other matters relating to railways;
 - (aa) to have regard to any general guidance given to it by the Scottish Ministers about railway services wholly or partly in Scotland or about other matters in or as regards Scotland that relate to railways;
 - (ab) in having regard to any guidance falling within paragraph (aa), to give what appears to it to be appropriate weight to the extent (if any) to which the guidance relates to matters in respect of which expenditure is to be or has been incurred by the Scottish Ministers;
 - (b) to act in a manner which it considers will not render it unduly difficult for persons who are holders of network licences to finance any activities or proposed activities of theirs in relation to which the Office of Rail Regulation has functions under or by virtue of this Part or that Act (whether or not the activities in question are, or are to be, carried on by those persons in their capacity as holders of such licences);
 - (c) to have regard to the funds available to the Secretary of State for the purposes of his functions in relation to railways and railway services;
 - (ca) to have regard to any notified strategies and policies of the national Assembly for Wales, so far as they relate to Welsh services or to any other matter in or as regards Wales that concerns railways or railway services;

- (cb) to have regard to the ability of the National Assembly for Wales to carry out the functions conferred or imposed on it by or under any enactment;
- (d) to have regard to the ability of the Mayor of London, London Regional Transport and Transport for London to carry out the functions conferred or imposed on them by or under any enactment.
- (5A) Before giving any guidance for the purposes of subsection (5)(a) above the Secretary of State must consult the National Assembly for Wales.
- (5B) In exercising its safety functions, other than its functions as an enforcing authority for the purposes of the Health and Safety at Work etc Act 1974, the Office of Rail Regulation shall be under a duty to have regard to any general guidance given to it by the Secretary of State.
- (5C) In performing its duties under subsections (1) to (5A) above in relation to—
 - (a) any matter affecting the interests of users or potential users of railway services;
 - (b) any matter affecting the interests of persons providing railways services; or
 - (c) any matter not falling within paragraph (a) or (b) but falling within subsection (5D).

the Office of Rail Regulation must have regard, in particular, to the interests, in securing value for money, or the persons mentioned in paragraphs (a) and (b) above, of the persons who make available the resources and other funds mentioned in that subsection and of the general public.

- (5D) A matter falls within this subsection if the Office of Rail Regulation has been informed that—
 - (a) public financial resources (within the meaning of paragraph 1D of Schedule 4A to this Act); or
 - (b) funds that do not comprise such resources but are provided in whole or in part by Transport for London, the National Assembly for Wales, a

Passenger Transport Executive or any other body in receipt of such resources;

are or are likely to become available to be applied for purposes connected with that matter.

(6) In performing its duty under subsection (1)(a) above so far as relating to services for the carriage of passengers by railway or to station services, the Office of Rail Regulation shall have regard, in particular, to the interests of persons who are disabled.

(7) Without prejudice to the generality of paragraph (e) of subsection (1) above, any arrangements for the issue and use of through tickets shall be regarded as a measure falling within that paragraph.

(7ZA) Where any general guidance given to the Office of Rail Regulation for the purposes of subsection (5)(a) or (aa) or (5B)—

(a) it may be varied or revoked by the person giving it at any time; and

(b) the guidance, and any variation or revocation of the guidance, must be published by that person in such manner as he considers appropriate.

(7A) Subsections (1) to (6) above do not apply in relation to anything done by the Office of Rail Regulation in the exercise of functions assigned to it by section 67(3) below (“Competition Act functions”).

(7B) The Office of Rail Regulation may nevertheless, when exercising any Competition Act function, have regard to any matter in respect of which a duty is imposed by any of subsections (1) to (6) above, if it is a matter to which the Office of Fair Trading could have regard when exercising that function.

(8) . . .

(9) In this section—

“the environment” means all, or any, of the following media, namely, the air, water and land (and the medium of air includes the air within buildings and the air within other natural or man-made structures above or below ground);

“notified strategies and policies”, in relation to the national Assembly for Wales, means the strategies and policies of that Assembly that have been

notified by that Assembly for the purposes of this section to the Office of Rail Regulation;

“the passenger transport market” means the market for the supply of services for the carriage of passengers, whether by railway or any other means of transport;

“railway service performance” includes, in particular, performance in securing each of the following in relation to railway services –

- (a) reliability (including punctuality);
- (b) the avoidance or mitigation of passenger overcrowding; and
- (c) that journey times are as short as possible;

“safety functions” means functions assigned or transferred to the Office of Rail Regulation—

- (a) under this Part;
- (b) under or by virtue of the Railways Act 2005; or
- (c) under or by virtue of the Health and Safety at Work etc Act 1974;

so far as they are being exercised for the railways safety purposes (within the meaning of Schedule 3 to the Railways Act 2005) or for purposes connected with those purposes.

Annex B – Penalties: procedural requirements

1. ORR is empowered:
 - (a) under section 55(7A) of the Act, to impose a payment of a “reasonable sum” on the licence holder as part of the making of a final or provisional order to secure compliance with a licence condition in the event of contravention of such order; or
 - (b) under section 57A(1) of the Act, to impose payment of a penalty on the licence holder directly for infringement of a licence condition or a final or provisional order.
2. The reasonable sums and penalties are payable to the Secretary of State and/or Scottish Ministers as appropriate.

Section 55

3. ORR is specifically empowered under section 55(7A) to include in a final or provisional order a provision requiring the licence holder to pay a “reasonable sum” in the event of any specified contravention of an enforcement order.
4. The “reasonable sum” is to be specified in the section 55 order or determined in accordance with it. However, the sum imposed may not exceed 10% of the turnover of the licence holder - determined in accordance with the turnover regulations.²³
5. There are a number of procedural requirements that must be followed by ORR prior to the imposition of the “reasonable sum” on a licence holder. These are set out in section 56 of the Act. In particular, prior to making a final order or confirming a provisional order, ORR must give notice that it intends to make or confirm the order and, amongst other things, set out the grounds on which the order is made. ORR is obliged to consider any representations or objections made to it. ORR may not then modify a final order or confirm a provisional order unless the licence holder consents or ORR has complied

²³ The Railways Act 1993 (Determination of Turnover) Order 2005, SI2185

with certain additional requirements, specifically the giving of further notice and the consideration of any further representations or objections made.

6. Section 57 provides an aggrieved licence holder with the right, in certain circumstances, to make an application to the court to question the validity of an order made by ORR.

Section 57A

7. If ORR is satisfied that a licence holder has contravened or is contravening:
 - (a) any condition of its licence; or
 - (b) a final or provisional order made by ORR,

ORR may impose on the licence holder a penalty of such amount as is reasonable.

8. A penalty may not be imposed under section 57A if payment of a reasonable sum has already been imposed under section 55(7A) (see above) in respect of the same contravention.
9. The amount of the penalty imposed may not exceed 10% of the turnover of the licence holder (this is determined in accordance with the turnover regulations).
10. ORR may not impose a penalty under section 55(7A) if it is satisfied that the most appropriate way of proceeding is under the Competition Act 1998. Financial penalties may also be payable for infringements of the competition law prohibitions in the Competition Act 1998.
11. There are a number of procedural requirements that must be followed by ORR prior to imposing a penalty on a licence holder under section 57A. These are set out in section 57C of the Act. In particular, before imposing a penalty on a licence holder, ORR must give notice that it proposes to impose a penalty setting out, amongst other things, the amount and the grounds on which the penalty is being imposed. ORR is obliged to consider any representations or objections made to it. ORR may not modify a proposal to impose a penalty without the licence holder's consent, unless the modifications consist of a reduction of the amount of the penalty or a deferral of the date by which it is to be paid, or ORR has complied with certain

additional requirements (specifically the giving of further notice and the consideration of any further representations or objections made).

12. ORR must then give a final notice stating that it has imposed the penalty on the licence holder and its amount. In addition, it must set out the grounds on which the penalty is imposed and must specify the manner, the place and the date on which the penalty is to be paid.
13. A penalty under section 57A must be imposed within the time limits set out in section 57D of the Act. A copy of the notice relating to the penalty must be served on the relevant licence holder within two years of the time of the licence condition being contravened. Alternatively, if a final or provisional order has been made by ORR in relation to the contravention, a copy of the notice relating to the penalty must be served on the licence holder within three months of the confirmation of the provisional order or the making of the final order or, where the provisional order is not confirmed, within six months of the making of the provisional order.
14. Section 57F provides an aggrieved licence holder with the right, in certain circumstances, to make an application to the court to question the validity of a penalty order made by ORR.

ORR's statutory duties

15. ORR must exercise its functions in the manner that it considers best calculated to achieve the duties in section 4 of the Act (set out in Annex A of this document). The duties placed on ORR under section 4 rank equally with each other.

Annex C – Enforcement action

Licence enforcement action taken to date

Enforcement orders have been made in the following instances:

- answering targets for the National Rail Enquiry Service (NRES) (against all franchised passenger train operators, under Condition 7 of passenger train operator licences in 1997-1998);
- delivery of performance targets (against Railtrack PLC, under Condition 7 of the Network Licence in 1999-2001);
- West Coast modernisation delivery (against Railtrack PLC, under Condition 7 of the Network Licence in 1999-2000); and
- post Hatfield rail recovery (against Railtrack PLC, under Condition 7 of the Network Licence in 2001).

Monetary penalties

ORR has imposed penalties in the following instances:

- penalties totalling £350,000 on all franchised passenger train operators in respect of answering targets for NRES (Condition 7 of passenger train operator licences, 1997); and
- a penalty of £7.9 million on Railtrack PLC in respect of failure to deliver performance targets, (Condition 7 of the Network Licence, 2001).

Notices in lieu of enforcement action

ORR has issued notices under section 55(6) of the Act in lieu of enforcement action in the following instances:

- failure to comply with the Telephone Enquiry Bureau scheme (against West Anglia Great Northern Railway Limited, under Condition 7 of its passenger train operator licence, 1996);
- failure to comply with the Ticketing and Settlement Agreement and Travelcard agreement (against LTS Rail Limited, under Condition 7 of its passenger train operator licence, 1997);
- failure to maintain station ticket office opening hours (against Northern Spirit Limited, under Condition 7 of its passenger train operator licence, 1997);

- failure to plan renewal, maintenance and enhancement of the network in a timely and efficient manner (against Railtrack Plc, under Condition 8 of the Network Licence, on a number of occasions, 1999-2000);
- non-compliance with answering targets for the NRES, pending investigation of the achievability of the targets (against all franchised passenger train operators, Condition 7 of passenger train operator licences, 1999-2000);
- failure to plan renewal, maintenance and enhancement of the network in a timely and efficient manner (against Railtrack Plc, under Condition 9 of the Network Licence, on a number of occasions in 2001-02);
- failure to provide information to enable Railtrack to comply with Condition 9 of the Network Licence (T-12) (against South West Trains Limited, under Condition 14 of its passenger train operator licence, 2002);
- omission from Network Rail's 2003 business plan of long term expenditure projections (against Network Rail, under Condition 7 of the Network Licence, 2003);
- failure to plan renewal, maintenance and enhancement of the network in a timely and efficient manner (T-12) (against Network Rail, under Condition 9 of the Network Licence, 2004); and
- failure to plan renewal, maintenance and enhancement of the network in a timely and efficient manner (T-12) (against Network Rail, under Condition 9 of the Network Licence, 2005).