Regulatory Justice:
Sanctioning in a post-Hampton World

Consultation Document
May 2006
Cover page
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Annexes with more information on the following topics are available in downloadable form from http://www.cabinetoffice.gov.uk/regulation/penalties.

- Annex A: Sample Enforcement Pyramid
- Annex B: The Review’s Work
- Annex C: The Regulators
- Annex D: Strict Liability Analysis – Professor R. Macrory
- Annex E: Strict Liability in UK Regulation
- Annex F: The Availability and Use of Statutory Enforcement Notices

Acknowledgements
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Acronyms and Abbreviations
Executive Summary

In September 2005, I was asked by the Chancellor of the Duchy of Lancaster to examine the system of regulatory sanctions to ensure that these were consistent and appropriate for the risk based approach to regulation set out in the Hampton Review. This consultation document contains my initial findings on the penalties system and outlines my vision for a modernised system of regulatory sanctions, which I invite all stakeholders to consider and comment on. I intend to publish my final recommendations in autumn 2006.

Sanctions are an important part of any regulatory system. They provide a deterrent and can act as a catalyst to ensure that regulations are complied with. A system of effective penalties can signal that behaviour which jeopardises citizens’ health and safety, pollutes the environment, violates the rights of consumers or distorts a free and competitive market is not acceptable and will not be tolerated.

Over the past few years, the Government has introduced a series of reforms that have aimed to improve the efficiency of the sanctioning system. Many of the more recently created economic and financial regulators have very modern sanctioning toolkits which include flexible and proportionate responses to address regulatory non-compliance, including monetary administrative penalties (administrative fines). The tribunal system is also looking to undergo a radical overhaul and this work is being led by the Department for Constitutional Affairs (DCA). The Department for Environment Food and Rural Affairs (Defra) is currently consulting on the introduction of administrative sanctions for regulatory non-compliance in the fisheries industry. I recognise the good work done in these areas, and have built on these ideas when setting out my own vision for a modern regulatory penalties system.

The challenge for Government and regulators set out in my review is to build on these initial steps. This will mean a shift in the way regulators approach regulatory sanctioning. A more flexible toolkit will require some additional safeguards for the rights of victims and offenders. It will also mean a lesser reliance on criminal prosecutions as a regulatory sanction with greater reliance on other types of sanctions such as administrative penalties or statutory notices. Modernising the sanctioning toolkits should enable the Hampton vision to be realised more readily with a renewed focus on advice and education and less emphasis on inspections.

My vision for the penalties system is a step change from where we are today. It allows for a flexible and proportionate approach with a broad range of sanctioning options, where regulators can respond to the needs of individual cases and the nature of the underlying offence. It recognises that effective sanctions can also aim to restore the harm caused by regulatory non-compliance and take into consideration the needs of victims, offenders and communities affected by regulatory non-compliance.

The changes needed to realise this vision will not happen overnight. Some will require legislation; others will require a shift of long-established culture and practice in regulators and business. I think, however, that both Government and regulators have already taken some initial steps towards a more flexible sanctioning toolkit. I believe the vision set out in this document is achievable and in tune with the latest thinking on regulation in the UK and abroad.

Professor Richard Macrory
Introduction

1. The final report of the Hampton Review, published in March 2005, recommended that the Government establish a comprehensive review of regulators’ penalty regimes. Following this recommendation, the Penalties Review was established under my leadership. As part of this review, I have looked at sanctioning regimes and penalty powers in detail over the last eight months. My work and thinking has been informed by the evidence submitted to me and by the work of Government departments, academics and practitioners. I have also studied the administrative penalties and regulatory sanctions available in other countries, including Australia, Canada and the United States to obtain an understanding of the policy and practice in these leading developed nations.

2. The Hampton Review found that regulatory penalty regimes can be cumbersome and ineffective. Although the Hampton Review envisaged the introduction of tougher and quicker penalties for more serious offences, the principal purpose of my review is not a blanket strengthening of penalty regimes. Rather, I want to consider options that could add to regulators’ enforcement toolbox, broadening the flexibility available to both regulators and the judiciary to better meet regulatory objectives and improve compliance. These options would also benefit business, by providing a transparent system with appropriate sanctions that would aim to get firms back into compliance, ensure future compliance, provide a level playing field for business and enable regulators to pursue offenders that flout the law.

3. I published a discussion paper, Regulatory Justice: Sanctioning in a post-Hampton World in December 2005 to promote thinking on how regulatory sanctions and penalties could be reformed or improved. It invited anyone with an interest in or experience of regulatory justice to submit evidence to the review team. The discussion paper set out the key issues previously identified in the Hampton Review and identified areas of interest for my review when considering reform, such as the use of criminal prosecutions as a regulatory sanction, administrative penalties, restorative justice, re-categorising or decriminalising regulatory offences and venues for hearing cases and appeals related to regulatory non-compliance. The purpose of the paper was to promote discussion and stimulate thinking around the area of regulatory sanctioning and penalty regimes.

4. It is important that regulators have a sanctioning toolkit that lets them ensure the protection of workers, consumers and the environment. Such a toolkit needs to provide appropriate options to handle the regulatory needs of legitimate business as well as those businesses that intentionally and knowingly fail to comply with regulatory obligations. Evidence submitted to me suggests that many regulators are over-reliant on one tool, namely the criminal prosecution, as it is the main sanction should business or individuals be unwilling or unable to follow advice and comply with legal obligations. This option may not be the most appropriate in all circumstances to ensure that non-compliance is addressed and that any damage caused is remedied or behaviour is changed; the availability of other tools may result in better regulatory outcomes.

1 Reducing administrative burdens: Effective inspection and enforcement, Hampton P., HM Treasury, March 2005, Recommendation 8
5. The reforms I propose are designed to modernise sanctioning toolkits across the regulatory system, reflecting the risk-based approach to regulation and the broader regulatory reform agenda and addressing the needs identified above. In this document, I set out the vision for what this modern, fit-for-purpose sanctioning regime could look like. My aim is not to be prescriptive, but to offer options for Government departments and regulators to consider which will be unique and specific to particular areas but will share common principles, features and characteristics.

6. Many of my suggested recommendations are a continuation of current Government proposals and reforms. For example the Home Office is exploring the role of Restorative Justice in areas such as corporate homicide and youth offending; the Department for Constitutional Affairs (DCA) is looking to undertake a radical overhaul of the tribunal system; and the Department for Environment, Food and Rural Affairs (Defra) is currently consulting on the introduction of administrative penalties in the area of fishing and marine activities.

7. Whilst the UK has a leading position in the area of regulatory reform, little has been done to modernise the sanctioning toolkit in recent times. In this area, we have not kept pace with the innovations being introduced in other leading OECD nations such as Australia and Canada, countries which share some of our legal tradition. Although some work towards this has begun, I believe that the UK must address this area in order to ensure that the Government’s better regulation agenda, including the recommendations of the Hampton Review and the Better Regulation Task Force’s report “Regulation – Less is More”, is realised.³

Policy Proposals

8. I have considered a broad spectrum of sanctioning tools, ranging from influencing methods such as warning letters or the use of informal, pragmatic means like advice and persuasion, to criminal prosecution at the top end of the enforcement pyramid (see annex A). I have also considered the major motivations for non-compliance. My aim is to identify a range of suitable sanctioning options that should be available to allow regulators to deal appropriately with each type of offender, including the ‘rogue’ element present in all areas of business.

9. The reformed sanctioning system I propose will increase public confidence, give greater awareness to the needs of victims and ensure that business non-compliance is met with a proportionate response. It will do this by providing a transparent system with sanctions that encourage and assist firms to comply with their regulatory obligations.

10. The proposed areas of policy reform I suggest are set out for consultation in chapter seven and summarised in Box E1 below. They include proposals around the following areas:

   - A list of ‘Penalties Principles’ and a framework for regulatory sanctioning;
   - The role of the criminal prosecution as a regulatory sanction;
   - The role of Monetary Administrative Penalties (administrative fines);

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Enforcement Notices and other innovations in a similar vein such as Enforceable Undertakings;
- The role of Restorative Justice in regulatory non-compliance; and
- Alternative sentencing options that could be available in criminal courts.

11. The reforms I suggest are not intended to transform sanctioning systems overnight. Rather, they are to bring into them the flexibility, efficiencies and responsiveness that can facilitate the full implementation of the Hampton agenda, resulting in better deterrence options for regulators, better compliance for business and better outcomes for society as a whole.

### Box E1 Proposed elements for reform of the penalties system

<table>
<thead>
<tr>
<th><strong>Criminal Proceedings</strong></th>
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<tr>
<td>• The use of criminal prosecution should be maintained to sanction serious regulatory non-compliance where there is evidence of intentional or reckless behaviour or where the actual or potential consequences are so serious that public interest demands a criminal prosecution.</td>
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<th><strong>Administrative Penalties</strong></th>
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<td>• There should be greater use of administrative sanctions and I propose three different models for consideration. My preferred model proposes that the regulator has discretion to apply Fixed or Variable Monetary Administrative Penalties (administrative fines) but, if contested, the recipient firm can appeal the matter to an independent administrative tribunal.</td>
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<th><strong>Statutory Notices</strong></th>
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<td>• The use of Enforcement and Improvement Notices should be strengthened by ensuring that regulators have mechanisms in place to follow them up.</td>
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<tr>
<td>• Regulators and firms should be able to agree an Enforceable Undertaking for the firm as an alternative to the imposition of a penalty (such as bringing a prosecution). Enforceable Undertakings could also be combined with a Monetary Administrative Penalty.</td>
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<th><strong>Restorative Justice</strong></th>
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<tr>
<td>• Restorative Justice could be a useful process to ensure that the needs of victims of regulatory crimes are addressed and proposes two options to consider: I believe both options should become part of the regulatory toolkit.</td>
</tr>
<tr>
<td>• Option one – RJ as a pre-court diversion. The regulator could suggest a Restorative Justice process to the firm after gathering all the facts of the case, but before initiating criminal proceedings.</td>
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<tr>
<td>• Option two – RJ in lieu of an administrative fine. The regulator could suggest an RJ process before imposing an administrative fine.</td>
</tr>
<tr>
<td>• Option three – RJ as part of criminal proceedings, Magistrates or Crown Court judges could recommend a Restorative Justice process to the firm at various stages of the criminal proceedings such as pre-sentencing or as part of a sentence.</td>
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EXECUTIVE SUMMARY

Proposals to increase effectiveness of criminal courts
- I suggest some proposals for consultation which could increase the effectiveness of sanctioning regulatory non-compliance through criminal proceedings. These include initiatives to develop guidelines for sentencing and to concentrate prosecutions in certain areas to particular courts.
- I also suggest for consultation that, when appropriate, the maximum level of penalties available should be reviewed and that fines handed down by courts should aim to eliminate the financial gain made as a result of the regulatory non-compliance.

Powers available to the criminal courts
- I suggest that in addition to the tools that could be made available to regulators, Magistrates and Crown Court judges may also benefit from having an extended toolkit in addressing regulatory offences, which could include options beyond financial penalties or imprisonment. This could include options such as conditional cautions or publicity orders.

12. I have also set out a framework within which these new sanctions would fit. The revised sanctioning tools must adhere to the ‘Hampton Principles’ and regulators must ensure that they are consistent with a publicly available enforcement policy to ensure transparency, fairness, proportionality and accountability when applying a sanction for regulatory non-compliance. This framework is set out in Box E2 below.

Box E2 Proposed key principles and framework for applying penalties

The Macrory Penalties Principles
I have identified the following ‘Penalties Principles’ that I believe should be the basis for any sanctioning regime:
1. Sanctions should change the behaviour of the offender.
2. Sanctions should ensure that there is no financial benefit obtained by non-compliance.
3. Sanctions should be responsive and consider what is appropriate for the particular offender and the particular regulatory issue.
4. Sanctions should be proportionate to the nature of the offence and harm caused.
5. Sanctions should aim to restore the harm caused by regulatory non-compliance.
6. Sanctions should aim to deter future non-compliance.

Framework for applying penalties
I suggest that, in order for these Penalties Principles to be applied effectively and consistently, regulators should operate within a framework with the following six characteristics:
1. Regulators should publish an enforcement policy.
2. Regulators should measure the outcomes of their enforcement activities and tailor their enforcement effort to improving these outcomes.
3. Regulators should always be able to justify the choice of enforcement actions and explain why these actions are appropriate.
4. Regulators should always follow up enforcement actions and ensure that their sanctions are credible to offenders.
5. Regulators should be transparent in what formal enforcement activity has been taken in order to safeguard all stakeholders.
6. Regulators should be transparent in the methodology for calculating administrative penalties.
Consultation

13. The proposed solutions set out in this interim report are not final recommendations. Rather, at this stage of the review process, I am seeking views on a number of key options. I am interested in hearing from regulators, business, non-governmental organisations and any other interested parties on all areas discussed in this report.

14. Chapter seven details the questions for consultation and how responses can be submitted to me. The closing date for the consultation period is August 18, 2006. I will publish my final report and recommendations in autumn 2006.
Chapter one
My Vision For Contemporary Sanctioning Regimes

This chapter sets out the importance of regulatory sanctions and outlines my vision for what a regulatory sanction regime should look like. Chapter two reports on the evidence that was submitted to me in response to the call for evidence, while chapter three explores the role of Monetary Administrative Penalties (administrative fines). Chapter four explores the use of statutory notices such as Enforcement Notices and Enforceable Undertakings and chapter five considers the role for Restorative Justice in cases of regulatory non-compliance. Chapter six sets out some alternative sanctions that could be made available to the judiciary. Lastly, chapter seven identifies my proposed reforms and brings together all of the questions for consultation.

Introduction

1.1 Although the Hampton Review envisaged the introduction of tougher, quicker penalties for more serious offences, the principal purpose of my review is not a blanket strengthening of penalty regimes. Rather, I want to present options for consultation that could add to regulators’ enforcement toolbox, broadening the flexibility available to regulators, the judiciary and business to better meet regulatory objectives, improve compliance and ensure a level-playing field for all.

1.2 The Macrory Penalties Review was commissioned as part of the implementation of the Hampton Report by the Chancellor of the Duchy of Lancaster in September 2005, and its terms of reference are set out in the discussion paper Regulatory Justice: Sanctioning in a post-Hampton World. Annex B contains more details. The aim of my review is to bring the sanctioning regimes of the 60 national regulators (listed at the start of Annex C) and 468 local authority regulators into line with the risk-based, proportionate model of regulation set out in the Hampton Review.

1.3 In this report, references to ‘the regulators’ refer only to those regulators that are within the scope of this review. My review did not examine regulators that are the responsibility of the devolved administrations in Scotland, Wales and Northern Ireland, but did consider the operation of England-based regulators in those countries. Many of the underlying principles, though, are likely to be applicable within the devolved jurisdictions. The penalties available to the economic regulators listed (also in Annex C) are considered solely for the purposes of comparison.

1.4 In my review I have concentrated on the sanctioning tools available to regulators. The processes by which regulations are made and enforced is not strictly within the scope of the review and therefore does not feature in my recommendations, although they have been commented on in various places within this report. Nor was it within my remit to consider the actual substance of the regulatory legislation, though it is axiomatic that sensibly drafted and appropriate substantive law is vital to the effectiveness of any regulatory system.

1.5 Following the publication of this interim report, my team and I will consult extensively with key stakeholders and experts and with interested members of the public with a focus on the preparation of a final report to be published in the autumn.
Sanctions are an essential feature of a regulatory enforcement toolkit

1.6 Sanctions are an important part of achieving compliance in supporting the enforcement activities of regulators. In some instances, the threat of a punishment can act as a catalyst towards improved outcomes and greater compliance. It can do this by providing a signal to the firm that has offended (and others who are contemplating offending) that the offence will not be tolerated and that there will be a reprimand or consequence. Other times, the imposition of a sanction can provide a non-compliant firm with an opportunity to better understand what is required of it under the law and improve the firm’s competence and performance, as well as ensuring better compliance with regulatory obligations.

1.7 The scheme below outlines the relationship between sanctions and other elements of enforcement and inspection. Most regulators will operate with a blend of the activities illustrated on the diagram below in order to ensure that firms comply with the relevant regulations and uphold the safety and protection of workers, the environment and consumers.

**Figure 1.1 Sanctions as part of the enforcement toolkit**
Context of the Macrory Review

1.8 The Hampton Review, which looked at effective inspection and enforcement, commented on the balance that should exist between each of the different strands in Figure 1.1. The Hampton Review concluded that regulators should focus on advice and education. Inspections, that review concluded, should only take place for a reason, not just for the sake of an inspection. For instance, reasons for inspection would include if a firm is identified as high risk or high hazard or if the inspection is part of a random sample to ensure that the risk assessment framework of a regulator is working as it is intentioned.

1.9 The Hampton Review also suggested a set of enforcement principles for business regulation to establish a formalised framework for the balance between the various strands of enforcement activities. The Government has accepted these Hampton Principles and is currently in the process of legislating to require regulators to have regard to them when exercising their regulatory functions.

1.10 The Hampton enforcement principles are being expanded into a new ‘Compliance Code’ for regulators.1 The Legislative and Regulatory Reform Bill is currently going through Parliament. Part two of that Bill, at the time of writing, contains a power to issue a statutory code of practice and it is envisaged that the draft Compliance Code, currently out for informal consultation, may well form the basis for that code. However, the Bill provides that any draft code to be issued using the power in the Bill will be subject to full statutory consultation. This code will replace its predecessor – ‘The Enforcement Concordat’ - which was a voluntary code of practice.2

1.11 It is within this context that reform of sanctioning regimes must take place. An important caveat that I want to ensure is that regulators do not stray from the path laid out in the Hampton Review regarding advice and education. Sanctions should not become a more dominant feature of the enforcement strategy. Sanctions should be effective and assist regulators in achieving better compliance, but should not be used at the expense of giving those that they regulate advice and education in order to encourage compliance.

The criminal prosecution as a regulatory sanction

1.12 In nearly every area of regulation in the UK examined by the review, the core sanctioning tools are the formal notices and prosecutions provided by the criminal law. The term ‘regulatory offence’ is neither a clearly defined term nor a distinct category of the criminal law as such, but instead breaches of regulatory obligations are defined in the relevant legislation as criminal offences of different degrees of seriousness. Legislation also provides that the failure to comply with the various types of Improvement and Enforcement Notices available to regulators is a criminal offence. This means that such offences are handled by the criminal courts – with the vast majority of offences concerning regulatory non-compliance in England and Wales being heard in the Magistrates’ Courts. Criminal procedural requirements apply to the prosecution of such offences.

2 Enforcement Concordat, Cabinet Office 1998.
1.13 This reliance on criminal prosecution in the regulatory field can be contrasted with countries such as Germany, the US, Canada and Australia. In many countries, prosecution is reserved for the most serious offences, and greater use is made of other forms of sanctions to deal with regulatory non-compliance and minor offences. In England and Wales, modern regulatory systems such as those found in the field of competition law and economic regulation (such as the system set up by the Financial Services and Markets Act 2000) and the legislation relating to the utility regulators such as water and sewerage providers makes greater use of monetary administrative penalties rather than criminal prosecutions. There is detailed discussion of these types of penalties in chapter three.

1.14 Figure 1.2 below captures the current system of regulatory sanctioning in England and Wales and its focus on criminal prosecutions.

![Figure 1.2 Typical existing regulatory enforcement toolkit](image-url)
The criminal offence – casting a wide net

1.15 Much of the evidence submitted to me has indicated that in most areas of regulation there are, at one end of the spectrum, what can truly be described as criminal or rogue operators intentionally avoiding compliance with regulatory requirements for economic gain. Between this and the other end of fully compliant businesses lie a whole host of others that are striving to comply to varying degrees and with varying success. Under the current system, a single regulatory offence often in effect has to do a great deal of work - acting as a deterrent and sanction both for the “truly criminal” and the legitimate business that fails to comply with regulatory requirements for a range of reasons.

“We agree with the comments in the report that criminal prosecution is a heavy handed approach, focusing as it does on punishment rather than prevention, and that it can undermine regulatory efficiency. This severe treatment, coupled with the fact that the fines available to the magistrates are relatively limited, means that the system fails on all levels: we spend a lot of money preparing cases, get little if any recompense and, often, the other party comes away feeling resentful, making it difficult to rebuild constructive relationships.”

British Potato Council

Source: Response from British Potato Council to the Macrory Review, February 2006

1.16 I believe that the current reliance on the criminal prosecution as one of the only regulatory sanctions is perhaps not the best arrangement. This is because the criminal sanction may not be the most appropriate sanction in order to deter non-compliance and change the behaviour of the firm. The particular facts of a case must be reflected both in the regulator’s enforcement policy and the sentencing practices of the courts. However, the lack of appropriate tools for regulatory sanctioning has resulted in a number of concerns from stakeholders which I describe in the next section.

Concerns expressed to the review

1.17 Businesses are concerned that the current regulatory sanctioning system prevents effective action from being taken against rogue businesses which undercut honest operators. Current tools are not sufficient to deter the ‘truly’ criminal or rogue operators, and equally when cases do reach the courts, sentences imposed are not considered by industry to be a sufficient deterrent or punishment for the offences in question.

“Our members occasionally complain that the regulatory authorities could do more to concentrate their efforts on rogue traders and other disreputable businesses who deliberately flout the law. They will be encouraged to see that the present review recognises the importance of cracking down hard on these “cowboy” operators.”

IoD

Source: Response from Institute of Directors (IoD) to the Macrory Review, February 2006
1.18 A further concern from the business community is that some regulatory non-compliance is not sanctioned at all. Many regulators, for certain offences, do not have access to any other sanctions outside of criminal prosecutions. This lack of flexibility constrains their ability to respond effectively to regulatory non-compliance. A heavy reliance on formal criminal sanctions makes the resolution of cases a costly and time-consuming exercise for both businesses and regulators. In many instances, given the limited resources within regulators, although regulatory non-compliance has occurred, the cost or expense of bringing criminal proceedings deter the regulator from taking any action, creating what has come to be known as a compliance deficit.

1.19 Evidence submitted to me has suggested that criminal convictions have lost the stigma that they once had, as criminal convictions in some industries are often regarded as part of the business cycle. This may be because criminal sanctions are applied to legitimate businesses that may be prosecuted for a strict liability offence (see Annex D for a discussion of strict liability offences), where no fault or intent was present, as well as rogues who are deliberately flouting the law. The current system does not differentiate between these two types of offenders other than through sentencing.

1.20 In instances where there has been no intent or wilfulness relating to regulatory non-compliance, a criminal prosecution may be a disproportionate response. However, regulators may not have any other sanctions available within their toolkits. If the actual or potential consequences of the regulatory non-compliance are serious, regulators may want to take some action, and the public may expect the regulator to take some enforcement action, but the only option available is a criminal prosecution.

1.21 Since the focus in criminal proceedings is on the offence and the offender, the wider impact of the offence on the victim may not be fully explored. There has been limited evolution in the rights and needs of victims in the area of regulatory non-compliance and I explore this area more in chapter five.

The criminal courts

1.22 In the call for evidence last December, I asked whether respondents felt that the current criminal system was adequate for addressing regulatory non-compliance and for suggestions for improvement. There was no compelling evidence advocating the wholesale transfer of criminal prosecutions for regulatory offences out of the ordinary criminal courts to an alternative venue or system. Yet there was a consistent view from both regulators and the regulated that the current system is not as effective as it could be.

1.23 Whilst I believe that reliance on criminal prosecution as the only formal sanction is not ideal, it does not follow that the failure to comply with regulatory requirements, whether that non-compliance is non-intentional or negligent, should not have a legal consequence. In cases where non-compliance has given rise to significant external damage or given a significant financial advantage to a business (the non-intentional failure to register for a licence, for
example) a substantial financial sanction may well be appropriate. Under the current system, most regulators only have the option of a criminal prosecution in such cases, even where the business concerned was at the most, careless. But it is questionable as to whether the criminal courts and the imposition of a criminal conviction are the most effective way to ensure that in such cases, a non-compliant business makes recompense for any economic gain made or damage caused.

1.24 For this reason, I have considered the potential for administrative penalties and other additional forms of sanctions that avoid the use of the criminal courts. If such sanctions were made available for those types of cases, one would be in a stronger position to attach a ‘stigma’ to a criminal conviction for regulatory non-compliance. I consider that individuals or firms who, say, deliberately and consciously put adulterated food into the consumer market, dump waste into rivers, or expose workers and others to risks to their health and safety through unsafe practices should be treated as committing ‘real’ crime, and treated with the same degree of seriousness as any other criminal. Clearly Parliament shared this view when these offences were categorised in the relevant legislation as criminal offences.

1.25 I do outline some proposals for increasing the effectiveness of the criminal courts in dealing with regulatory offences, and endorse the use of the formal procedures provided by the criminal law in appropriate cases. But reliance on the sanctions currently provided under the criminal law as effectively the only sanctions available appears to me to be no longer appropriate in a contemporary regulatory system. Criminal prosecution and the criminal courts, in my opinion, should largely be preserved for the truly egregious offenders or for cases where a regulatory breach leads to very serious actual or potential external consequences such as a death or serious injury caused by a failure to comply with health and safety requirements.

Using mainstream criminal law

1.26 Serious instances of regulatory non-compliance involving intention or recklessness may also involve conduct that amounts to a mainstream criminal offence. Conspiracy charges, for example, have been successfully brought in the food industry, by local authorities and the police working in partnership, where organised crime was involved in selling condemned food to hospitals, schools, and national supermarkets (see Box 1.1 below). Illegal dumping of waste on land, for example, could be an offence under s 1(1) Criminal Damage Act 1971 (damaging property belonging to another with intention or recklessness) as well as a breach of s 33 (1) Environmental Protection Act 1990 (depositing waste on land without a licence). Bringing such prosecutions is likely to be more resource intensive than a more “straightforward” regulatory offence couched in strict liability terms, and may require close cooperation between the police and regulatory authorities. Nevertheless, I consider that intentional or reckless breaches of regulatory law imposing significant damage or risk should be considered as criminal as any other “mainstream” crime. Where the facts of the case could give rise to such a mainstream offence, then it appears entirely appropriate to charge accordingly.
Evidence supplied to the review by the Food Standards Agency suggests that for certain types of offences, penalties provided in relation to regulatory offences in the field of food regulation are too low to be an effective deterrent. In these cases Local Authorities sometimes seek charges of conspiracy to defraud as a route to higher penalties.

This strategy has been successful in certain cases. For instance charges of conspiracy were brought against a gang in Derbyshire who had recycled 450 tonnes of unfit chicken and turkey back into the food chain. The convictions of the gang resulted in five people being jailed for a total of over 15 years and the imposition of Confiscation Orders totalling over £500,000. However, conspiracy can be very difficult to prove and, as a result, cases are very resource intensive and, due to the nature of the crime, normally require a significant police involvement.

Source: Response submitted to the Macrory Review by the Food Standards Agency, February 2006

A Vision for the future

1.27 I recommend for consultation that a richer range of sanctioning tools be made available to regulators, which would permit a range of regulatory offences to be handled other than by means of a criminal prosecution, leaving the most egregious to be dealt with by the criminal courts. Making such options available would itself reinforce a more appropriate role for the criminal courts, where in turn I propose exploring the scope for improving the effectiveness of the criminal prosecution for regulatory non-compliance.

1.28 My vision of sanctioning options within a modern regulatory system, based upon risk-based enforcement, is portrayed in Figure 1.3 below. Regulators would, against the background of their enforcement policy and the proposed Compliance Code, continue to exercise discretion as to when it is appropriate to apply a sanction, and the choice of the sanction would be determined by the nature and circumstances of the breach. But if other sanctioning tools such as fixed or variable administrative fines were available as additional tools, I would expect to see a shift in the current use of sanctions.

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3 Those sentenced to Compensation Orders were subject to default jail sentences totalling six and a half years were these not paid within the specified time.
Criminal prosecutions for serious breaches

1.29 As part of this vision, the use of criminal prosecutions would, of course, remain appropriate for serious breaches where there was evidence of intentional or reckless flouting of the law, whether by an individual or a business. Similarly, an intentional or reckless flouting of an Enforcement Notice would also be appropriate for criminal proceedings. Regulators may also decide within their discretion that criminal proceedings are justified where there is evidence of gross negligence, and where the actual or potential consequences of the breach are so serious (such as the death or serious injury of an employee) that public interest demands a criminal prosecution.

1.30 Minor breaches of regulatory requirements would I believe, be more effectively dealt with by the use of fixed or variable administrative fines (but giving the offender the option to have the case heard before an independent tribunal). The knowledge that an administrative fine, even of a fairly small amount, is a likely consequence for minor breaches will act as an inducement to comply for many businesses. But in instances of continual breaches, even of a minor nature, where administrative fines were clearly having no deterrent effect, a regulator should retain the option of bringing criminal proceedings or imposing another type of administrative penalty.
1.31 Many core ‘regulatory offences’ have been drafted in strict liability terms, meaning that to secure a conviction the prosecution simply has to present the facts of the offence without needing to prove the ‘mental’ element of the crime (*mens rea*), including intention, recklessness, or even negligence on the part of the offender. I commissioned Professor Simester of Nottingham University to examine the nature of current offences across a broad spectrum of regulation and his research confirmed that the majority of core offences surveyed impose strict liability. (see Annex E)

1.32 Serious regulatory breaches (such as those giving rise to significant damage or significant economic gain from non-compliance) which are strict liability offences, but where there is no evidence of a deliberate or reckless flouting of the law or gross negligence by the business concerned would, in my view, be more appropriately dealt with by the imposition of an administrative penalty. The business would still be financially penalised for the breach, but without the need for the imposition of a criminal conviction, and in a process that more fairly reflects the nature of the breach.

The Macrory Penalties Principles - Principles for effective sanctions

1.33 In order for this vision to be realised, I have arrived at a set of ‘Penalties Principles’ that I believe should be the basis for any sanctioning regime.

1.34 Fundamental to these ‘Penalties Principles’ is the notion that the underlying regulation is fit for purpose and provides for a greater social purpose such as the protection of consumers, workers, or the environment. When regulatory non-compliance occurs, these protections are compromised. The overriding purpose of sanctions is therefore to ensure that these protections are maintained and safeguarded.

- **Principle #1 – Changing behaviour**
  
  A sanction should aim to change the behaviour of the offender. This means that a sanction is not focused solely on punishment but also ensures that the offender is less likely to break the law in the future. Changing behaviour could involve culture change within an organisation or a change in the production or manufacturing process to ensure that regulatory non-compliance is minimised.

- **Principle #2 – No financial benefit**
  
  A sanction should aim to eliminate any financial gain or benefit from non-compliance. Firms may calculate that by not complying with a regulation, they can make or save money. They may also take a chance and hope that they are not caught for failing to comply with their regulatory obligations or deliberately breaking the law. Some firms may even believe that if they are caught, the financial penalties handed down by the courts will usually be relatively low and they will probably still retain some level of financial gain.

  If, however, firms know that making money by breaking the law will not be allowed, with sanctions specifically targeting the financial benefits gained through non-compliance, then this can reduce the financial incentive for firms to engage in this type of behaviour. For firms that persist in operating this way, the removal of any financial benefits will ensure that, in future, the financial gains are not enough of an incentive to break the law. There
are many who will argue that determining the financial benefit is a difficult and inaccurate process. I am aware of these challenges, but I believe that every attempt should be made to make these determinations.

- **Principle #3 – Responsive sanctioning**
  A sanction should be responsive and take into account what is appropriate for the particular offender and the particular regulatory issue. The regulator must have the ability to use its discretion and if appropriate base its decision on whether the firm would be more likely to benefit from a non-punitive sanction, such as an administrative penalty and some advice. The regulator should also consider the needs of victims and the public when deciding which types of sanctions would be appropriate to pursue in each particular case. This type of approach could come under some scrutiny as it may be argued that this is an example of inconsistency in the approach of regulators towards certain firms. However, I believe that the true consistency is that the regulator is seeking out the best route to get the firm to comply with its legal obligations. The way in which the regulator chooses to do this can vary depending on the needs of the business or offender, as well as the nature of the offence.

- **Principle #4 – Proportionate sanctioning**
  A sanction should be proportionate to the nature of the offence and the harm caused. While the previous principle is concerned with the reasons for the failure to comply, this principle takes into account the nature of the non-compliance and its consequences. Including these factors, will ensure that firms are held accountable for the impact of the actual or potential consequences of their actions and that these are properly reflected in any sanction imposed.

- **Principle #5 – Restore the harm caused**
  A sanction should include an element of restoration. This principle encompasses the needs of victims and ensures that corporate offenders take responsibility for their actions and any consequences of these actions. We talk more about this concept in chapter five on Restorative Justice.

- **Principle #6 – Deterrence**
  A sanction should aim to deter future non-compliance. Sanctions should signal to others within the regulatory community that non-compliance will not be tolerated and that there will be consequences. Whether this is a criminal prosecution or some other sanction would remain at the discretion of the regulator, within the scope of the powers available to it in relevant legislation, but firms should never think that non-compliance will be ignored or that they will ‘get away with it’.

1.35 Of course, regulators would be bound to operate within the framework of their own enforcement policies and also within the ‘Hampton Principles’ and the ‘Penalties Principles’ set out above, should the Government choose to accept these. We discuss this framework in more detail in the next section.
Framework within which the ‘Penalties Principles’ must operate

1.36 In order for these ‘Penalties Principles’ to be applied across regulators and for business to have some consistency in the approaches taken, I have proposed a framework within which I recommend that regulators should operate and describe some characteristics which I believe should be present in order for these principles to be applied. The framework I have set out is consistent with the Five Principles of Good Regulation.4

- **Characteristic # 1 – Enforcement policy**
  *Regulators should publish an enforcement policy.* Having a published enforcement policy would signal to business and society more generally what kind of behaviour to expect from the regulator when regulatory non-compliance has been identified, thus ensuring transparency and accountability in the exercise of its regulatory functions. A public enforcement policy also helps ensure that regulators use their sanction powers in a proportionate and risk based way.

  Internal research on the access and availability of enforcement policies within national regulators and government departments has found that of the 60 regulators in scope, 17 had an enforcement policy that was readily and publicly available.

  Source: Internal research undertaken by the Macrory Review, spring 2006

- **Characteristic # 2 – Measure outcomes**
  *Regulators should measure outcomes.* I have found that most regulators, when talking about enforcement activity or compliance, report on the number of prosecutions or the number of enforcement notices that they have issued. However, there is very little evidence of what the actual outcomes of these enforcement actions are. I therefore propose that regulators should measure outcomes and not just outputs. I appreciate that this is not an easy exercise and there may be difficulties in determining these measures, but I consider that real efforts should be made in this regard. By measuring outcomes, regulators and the public will know what impact the enforcement actions are having, whether these have improved compliance and whether there needs to be any modification to the balance between different types of enforcement actions to get better results.

- **Characteristic # 3 – Justify choice of enforcement actions**
  *Regulators should justify their choice of enforcement actions year on year.* To increase confidence in the way that regulatory non-compliance is dealt with, the public and private sector should be able to understand why regulators use the sanctions they do. For instance, if a regulator does not bring any criminal prosecutions in a year, then this might be a very good outcome because it may mean that there is no criminal activity in the area of regulation with most breaches being addressed through other means. However, it could also mean that criminal behaviour is occurring but not being addressed because the regulator is only focusing on administrative penalties where there may be a lower burden of proof. As a protection for legitimate business, regulators should be required to justify overall what their general enforcement strategy is and why they have chosen the enforcement actions that make up their strategy in any given year.

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Characteristic # 4 – Follow-up enforcement actions

Regulators should follow up their enforcement actions properly. At present, there is no substantial evidence which I have seen which suggests that regulators follow up on low-level enforcement actions such as warning letters or Enforcement/Improvement notices. This means that firms may or may not actually do what is required of them by those written notices. I believe that in order for these low level enforcement actions to be taken seriously and credibly by firms, regulators must follow them up proportionally.

Characteristic # 5 – Be transparent in what enforcement actions have been taken

Regulators should enforce in a transparent manner. Ensuring that key stakeholders and the wider public have an opportunity to be kept abreast of enforcement actions is an important element of a sanctioning system. I believe it is important for regulators to disclose when and against whom enforcement action has been taken. I believe that this should not be isolated to criminal prosecutions, but should also be used for other enforcement action such as administrative penalties, enforcement or improvement notices or any other formal sanction. This information should be easily accessible and serves as a safeguard for firms, the regulator and the public interest.

Characteristic # 6 – Be transparent in the methodology for calculating administrative financial penalties

Regulators should be transparent in the way in which they apply administrative sanctions. Regulators should disclose the methodology for calculating variable administrative fines and publish a schedule of fixed administrative fines so that firms will have an awareness of what mitigating and aggravating factors are relevant. I discuss these administrative sanctions in more detail later in chapter three.

Options for reform

1.37 Within the framework and consistent with the ‘Penalties Principles’ laid out in the discussion above, I have investigated a number of areas for potential reform outlined in Figure 1.3. I would like to consult upon these options. The areas for reform cover administrative sanctions, Restorative Justice and the venues for hearing cases dealing with regulatory non-compliance and appeals.

Monetary Administrative Penalties (MAPs)

1.38 As I describe in more detail in chapter three, I have developed a series of options regarding the role and introduction of administrative penalties. The calculation of any penalty can give due credit to businesses which clearly acknowledge the consequences of their regulatory non-compliance (such as providing recompense to any victims). A right to an independent appeal against the imposition of such a penalty would be required but as discussed in chapter three, I consider that this would be best handled by a dedicated regulatory appeals tribunal rather than the criminal courts since an administrative penalty system I believe should be clearly detached from the criminal justice system.
Model # 1 - Applied Monetary Penalties (AMP) model

1.39 A first model to consider is one where the regulator would gather the relevant evidence required for criminal proceedings. However, the regulator would give the firm the option of paying an administrative penalty as an alternative to a criminal prosecution. If the firm accepted the administrative penalty, then the matter would be concluded upon payment. If, however, the firm disagreed, the regulator would proceed to take the case to court as per the present system.

1.40 This model, while relatively simple to introduce into the current regulatory landscape, would not be my preferred option based upon the evidence I have seen, because it is punitive in nature and could be seen as giving offenders an opportunity to buy their way out of a prosecution.

Model # 2 - FMAP + VMAP with appeals to the courts

1.41 A second model which can be considered is a hybrid model, where regulators have the power to apply Fixed or Variable Monetary Administrative Penalties but, if the decision is contested, the recipient business can appeal the decision to the courts. The regulator decides if an offence should be subject to an administrative penalty or prosecution, however since the business can always appeal to the courts, it is effectively the choice of the business to either accept the administrative penalty or go through a full criminal prosecution process.

1.42 This model is attractive in its simplicity and it does not necessitate the development of distinct appeals routes as the offender can always opt for criminal prosecution. However, this is also the disadvantage of the model. There is a risk that it would replicate the current penalties system, and that there would still be too much reliance on criminal prosecution for dealing with regulatory offences, leading to an enforcement system which is at times disproportionate, inflexible and slow.

Model # 3 - FMAP + VMAP with appeals to regulatory tribunal

1.43 In my third model of administrative penalties, the regulator can apply a Fixed or Variable Monetary Penalty as an alternative to criminal prosecution or the available sanction. The appeals mechanism is to an independent administrative tribunal that deals exclusively with regulatory offences. The criminal courts are not involved in sanctioning regulatory offences except in the most serious cases, where the regulator considers criminal prosecution as the most appropriate response.

1.44 This model clearly decouples the administrative penalty system from the criminal system. A tribunal would enable the presentation of the case to be put before an expert panel and the tribunal might be able to make more precise assessments of the merits of the case and also on the appropriate levels of financial sanctions.

1.45 I discuss each of these specific options regarding administrative penalties in more detail in chapter three. I believe the best option is for administrative penalties with an appeals mechanism to a regulatory tribunal (Model #3). This is because a tribunal is a specialist body that can better address cases of regulatory breach as I discuss more in chapter three.
**Statutory Notices**

1.47 In addition to criminal prosecutions and administrative fines, I believe regulators should have access to options that would encourage and facilitate businesses to move into regulatory compliance. I believe that statutory notices could serve this purpose. These are discussed in more detail in chapter four.

1.48 I have commissioned some research on the role and use of statutory notices such as Enforcement Notices. This work is presented in more detail in Annex F. I conclude that Enforcement Notices, which are currently available in some regulatory regimes, are a good sanction because they are forward looking and are focused on bringing the firm into compliance. The one area of improvement I suggest is that these statutory notices should be followed up by regulators on a risk adjusted basis.

1.49 In addition to Enforcement Notices, I am interested in suggesting a further sanction should be available to UK regulators where appropriate. These are known as Enforceable Undertakings (EU), which are voluntary, but legally binding agreements between a firm and a regulator in cases of more serious offences where prosecution may not lead to the best outcomes. EUs usually require the offender to undertake specific actions to mitigate the damage done by the regulatory non-compliance. In these instances, regulators could prosecute, or could offer firms the opportunity to enter into an EU which typically includes provisions for compensation, reimbursement or redress to affected parties and also some measure to ensure the non-compliance is not repeated. EUs can also include a restorative element. A growing number of Australian regulators have Enforceable Undertakings available to them as an alternative to criminal prosecution or Monetary Administrative Penalties.

1.50 Enforceable Undertakings could also be combined with Monetary Administrative Penalties and these could be known as an ‘Undertaking Plus’. This sanction would combine the restorative and preventative measure of an Enforceable Undertaking with the removal of the financial gain resulting from non-compliance through a MAP. Similar safeguards would exist for this sanction including clear policy from the regulator on when it would be applied as well as fairness, proportionality, transparency and accountability in its use and conditions.

**Restorative Justice**

1.51 I have considered the role of Restorative Justice (RJ) with regard to regulatory non-compliance. It has been suggested that the current criminal justice system does not take account of victims to the extent that it could and that the adversarial style of this system also limits the extent to which those not in compliance with regulatory requirements take responsibility for their actions. Restorative Justice could be a useful process to consider as a means to change the way firms behave and ensure that the needs of victims of regulatory crimes are addressed.

1.52 Restorative Justice in this instance is a process whereby victims and offenders meet to resolve their conflict or restore the harm done by a corporate actor. Such a process has been found to be more meaningful for both victims and offenders including corporations. I discuss these ideas more fully in chapter five.
1.53 There are three options I would like to hear views on in this area:

- **Option # 1 – RJ as a pre-court diversion**
  This option is where the regulator, after gathering all the facts of the case would present the option of an RJ process to the offender before initiating any other formal proceedings, such as a prosecution. It could also be used as an alternative to an administrative fine, where appropriate.

- **Option # 2 – RJ as an alternative to an administrative fine**
  This option is where the regulator would offer the option of an RJ process as an alternative to an administrative fine, where appropriate.

- **Option # 3 – RJ within the criminal justice system**
  Where a regulator pursues a criminal prosecution, Magistrates or Crown Court judges could recommend an RJ process at various stages of the criminal proceeding – either before or as part of a sentence.

**Proposals for improving the effectiveness of criminal courts for regulatory offences**

1.54 Most cases involving regulatory offences (in England and Wales) are heard before the Magistrates Courts, but they represent a very small proportion of the total offences heard by magistrates, with the result that individual magistrates may rarely deal with a regulatory offence and, as a result, may be unfamiliar with the area of law concerned. Of the more than two million cases Magistrates and Crown Courts process each year, less than one percent deal with regulatory offences. A magistrate will typically see a health and safety offence every 14 years and an environmental case every seven years.

1.55 This is an area that has previously been acknowledged and there is some work being done to provide greater clarity on the sentencing of regulatory offences. The Magistrates Association and the Environmental Law Foundation prepared a sentencing guidance document for magistrates entitled ‘Costing the Earth: Guidance for Sentencers’. I believe that this type of initiative can be beneficial although the impact can also be constrained due to the infrequency of hearing cases dealing with regulatory non-compliance. Regulators could also investigate the training they could offer to Justice’s Clerks in order to address this issue.

1.56 I have also heard evidence that in some areas of regulation, prosecutions are concentrated on certain courts. For example, in Greater London, health and safety prosecutions are initiated in the City of London Magistrates Court. The British Potato Council, because of its location, concentrates prosecutions in the Oxford Magistrates Court. For similar reasons, prosecutions for many regulatory offences under company law are heard before Cardiff magistrates.

1.57 Focussing offences in this way gives greater opportunity for both magistrates and court officials to gain expertise and familiarity in the area of regulation concerned. It would appear sensible if further moves in this direction were taken. There must be limits – not least because of human rights implications for offenders – to the extent this can be taken, but within the

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8 Statistics provided by the DCA for England and Wales, 2004 for Magistrates and Crown Courts. Out of over two million cases, an estimated 15,445 cases are regulatory offences (or breaches) committed by companies or businesses.

jurisdictional areas of magistrates, there may be further opportunities for particular Magistrates Courts to take the lead in handling different types of regulatory offences.

1.58 In addition to powers of imprisonment (where provided for in the relevant legislation) and fines, the criminal courts now possess a range of sentencing options, which I discuss more in chapter six. Some of these may be appropriate in dealing with particular regulatory offences.

1.59 Criminal court judges can see cases in so many differing areas, so in order for the court service to work effectively, the Sentencing Advisory Panel and the Sentencing Guidelines Council formulate guidance on sentencing for particular offences, categories of offences and other sentencing issues. These bodies work closely with the Home Office. To date, they have issued limited guidance in the area of regulatory non-compliance. I believe that more work should be done to prepare sentencing guidance in the area of regulatory non-compliance for criminal court judges.

1.60 Where offences are heard before Crown Courts, the level of fine the court may impose is generally unlimited, while magistrates are subject to statutory maxima when deciding what an appropriate fine would be for a particular offence. Although it will be rare for a court to impose the specified maximum, this maximum can send a signal as to the seriousness which the legislature attributes to a particular offence. In certain areas (such as waste offences) the maximum fines have been increased significantly in recent years and it is important for the integrity of the system that, when appropriate, maximum penalties are reviewed, and that there is consistency across different regulatory regimes so that non-compliance in one area is not seen to be less important simply because of inconsistent fine maxima.

1.61 It remains the case that offenders before the courts can range across a spectrum from individuals and small traders with limited means, to larger businesses and multi-national corporations, where even the maximum specified financial penalties would have little economic deterrent effect. I would therefore welcome views on whether in fact the fine maxima should be abolished completely across the board, or whether some other form of cap should be introduced where one option may be to adopt the approach under the Competition Act 1998, which provides that administrative penalties may not exceed ten percent of the relevant turn-over of the business concerned.\(^{10}\) I accept that there can be difficulties in defining turn-over, but would welcome views on whether this sanctioning option would be desirable, feasible or appropriate in criminal cases.

1.62 I believe that any economic profits gained from non-compliance should, as a matter of sentencing practice, be reflected in levels of fine imposed. But both the Hampton Review and this review have been given examples of cases where fine levels do not appear to reflect the gains from non-compliance with regulatory requirements.\(^{11}\) There are, of course, many other factors that come into play in setting sentences, and it is important not to over-generalize from particular cases. But it is a concern, I believe, that should be addressed.

\(^{10}\) s. 36(8) Competition Act 1998.

1.63 I accept that in many cases of regulatory non-compliance it may simply not be possible to identify the profits gained from non-compliance, but equally there are instances where the economic gain is clearly apparent. My thinking in this area is at a relatively early stage and I would welcome views.

1.64 One approach may be to detach the fine from the profits element. In such cases, a court could be empowered to impose a ‘profits order’ which is intended simply to remove any clear economic gains over legitimate competitors from the non-compliance (such as failing to obtain a licence and avoiding registration fees) with the fine element representing the level of condemnation and deterrence which the court considers appropriate in the particular case.

1.65 This in itself will not necessarily resolve the cases of rogue operators, or indeed even legitimate businesses, who may have made substantial gains but can produce evidence of impecuniosity by the time the case reaches court, since the total sum would still then be subject to the need of the court to take into account the financial means of the offender, as well as any other mitigating factors. But it could be a valuable additional sanctioning tool available to the courts and one that would help meet the concerns of regulators and compliant businesses that undue economic gains are not being made by those who fail to comply with regulations and who warrant prosecution.

Powers available to Magistrates or Crown Court judges

1.66 In addition to the tools that could be made available to regulators, I am mindful that Magistrates or Crown Court judges may also benefit from having an extended toolkit, which could include options beyond financial penalties or imprisonment, both of which are good deterrents in many instances, but some cases may require other types of interventions. In this vein, I will discuss options such as reputational sanctions, clean-up orders, and corporate probation. These are discussed in more detail in chapter six.

Questions for consultation

1. Do you agree that criminal prosecution and the criminal courts should be reserved for the truly egregious offenders or where regulatory breach has lead to severe actual or potential external consequences?

2. Do you agree with the vision that is laid out in Figure 1.3 of a contemporary regulatory enforcement toolkit?

3. Do you agree or disagree with the ‘Penalties Principles’ proposed in chapter one? If you disagree with one or all of the Principles listed below, please elaborate?

   a. Principle # 1 - Sanctions should change the behaviour of the offender to prevent regulatory non-compliance
   b. Principle # 2 – Sanctions should eliminate any financial benefit or benefit which was the result of regulatory non-compliance.
   c. Principle # 3 – Sanctions should be responsive and take into account what is appropriate for the particular offender and the particular regulatory issue.
   d. Principle # 4 - Sanctions should be proportionate to the nature of the offence and the harm caused
e. Principle # 5 - Sanctions should include an element of ensuring that the harm caused by regulatory non-compliance is put right.

f. Principle # 6 – Sanctions should aim to deter future non-compliance.

4. Are there any principles that should be added to this list? If yes, please provide details including supporting comments and evidence.

5. Do you agree that a regulator must ensure the following characteristics to be present in order for a sanctioning regime to be most effective?
   a. The regulator should have a published enforcement policy
   b. The regulator should attempt to measure regulatory outcomes (such as compliance rates) as well as outputs (such as the number of enforcement actions taken).
   c. The regulator should be able to justify the enforcement actions they take
   d. The regulator should follow up enforcement actions
   e. The regulator should be transparent in the enforcement actions it takes
   f. The regulator should be transparent in the methodology it uses for setting and calculating monetary administrative penalties.

6. How should regulators be required to report their performance and progress against their enforcement strategies?

7. Should regulators make a more focused effort to communicate their strategy for targeting businesses that are deliberately non-compliant? If yes, how should they approach this?

8. What can be done to capture the rogue elements within industries?

9. Is there a need for increased investigative powers to be afforded to regulators to better deal with rogue businesses?

10. Should due diligence defences be included in all areas of criminal offences involving regulatory breach?

11. Would more training be appropriate for judges in the area of regulatory non-compliance and appropriate sentencing?

12. Should sentencing guidance be prepared for areas of regulatory non-compliance?

13. Should the fine maxima in criminal courts be abolished? Should a cap be set?

14. Should the cap follow the principles laid out in the Competition Act 1998 which provides that financial penalties may not exceed ten percent of the relevant turnover of the undertaking concerned?

15. Should profits gained from non-compliance be subject to a separate profits order which is intended to remove any economic gains from non-compliance as well as a separate fine element?
Chapter two
The penalty system today

The previous chapter discussed the role of the criminal law as a regulatory sanction. It also set out my vision for a modern sanctioning regime. This chapter discusses the evidence submitted to the review as part of the call for evidence.

The Hampton Review’s conclusion on sanctions

2.1 The Hampton Review and my discussion paper identified some shortcomings in the regulatory penalty system, which should be addressed in order to deliver a simpler, more effective and coherent sanctioning regime.

2.2 The shortcomings identified by the Hampton Review can be summarised as follows:
   - Penalties handed down by courts are not seen as an adequate deterrent to regulatory non-compliance as the level of financial penalty can often fail to reflect the economic benefit of non-compliance with regulatory obligations.
   - The range of enforcement tools available to many regulators is limited, giving rise to disproportionate use of criminal sanctions which can be a costly, time-consuming and slow process.

2.3 In December 2005, the Macrory Review called for evidence from regulators, businesses, special interest groups, magistrates, and interested members of the public to further examine these claims. This chapter summarises the experience of stakeholders in the regulatory process with the current penalty system.

2.4 The responses to my call for evidence indicate that the majority of respondents see the current penalty system as requiring some updating. Businesses and trade associations are concerned that the complexity, difficulty and expense of bringing criminal prosecution prevent effective action being taken against rogue businesses. Regulators are concerned that financial penalties in some cases do not exceed, or even approach, the financial benefit of non-compliance, creating perverse incentives for businesses to evade the law. Magistrates have pointed out that in some cases the quality of information given to courts may lead to different outcomes for cases that appear to be similar.

2.5 The responses indicate that there is a lack of enforcement tools available to regulators. This constraint does not allow for flexibility in the enforcement process and regulators are unable to be responsive to the needs of the business in order to achieve compliance. Regulators are reliant on criminal sanctions, and have limited access to a range of other formal sanctions to ensure that businesses comply with regulations.
Low Financial Penalties do not send a strong deterrence signal

2.6 There is a perception within regulators that the financial penalties handed down in Magistrates and Crown Courts do not serve as an adequate deterrent in addressing regulatory non-compliance. The evidence presented to me has demonstrated that, in some instances, the fines handed down in court do not reflect the financial gain a firm may have made by failing to comply with an obligation, thereby not acting as a deterrent and, in effect, giving businesses an incentive to continue to fail to comply in return for profit. In some cases fines do not fully reflect the harm done to society.

<table>
<thead>
<tr>
<th>Box 2.1 Examples of fines that do not reflect the economic benefit or seriousness of the offence (environmental regulation)</th>
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<tbody>
<tr>
<td>● An Oxfordshire man was fined £30,000 for abandoning 184 drums of toxic waste. The man received £58,000 for disposing of the material, and the Waste Authorities had costs of £167,000 to properly incinerate the waste.</td>
</tr>
<tr>
<td>● A fine of £25,000 was handed down to a small waste disposal company which was operating without a licence. The company saved £250,000 by operating illegally over a 2 year period.</td>
</tr>
</tbody>
</table>

Source: Examples submitted to the Macrory Review by the Environment Agency, March 2006

2.7 The apparently low financial penalties could be seen as an acceptable risk by a business, which has already chosen to be deliberately non-compliant. In these instances, it might be assumed that financial penalties fail to achieve even the most basic of the objectives in an effective penalties system. If regulators are pursuing, as they should, a risk based compliance oriented enforcement strategy, prosecution will be used as a last resort. It is reasonable to conclude that the prosecutions that do take place are for the most serious offences and offenders and the sentences should reflect this level of seriousness and be a strong deterrence signal for other firms in the regulated community.

2.8 The lack of an effective deterrence signal compromises the effectiveness of the regulatory relationship. Without credible and meaningful sanctions, regulators are forced to pursue more burdensome and bureaucratic enforcement policies. If criminal prosecutions sent out a strong deterrence signal, then regulators would be able to impose less onerous burdens on legitimate business by conducting fewer inspections. Legitimate businesses, instead see their unscrupulous competitors cut corners, and gain competitive advantage, without facing serious financial consequences.
A construction company was prosecuted following an incident that resulted in two employees being trapped in an unsupported excavation whilst laying pipes. Despite the site engineer being aware of the risks, no attempts were made to stop the work. There was a potential for a double fatality. The court fined the company £8,500.

A hospital trust was prosecuted under section 3 of the Health and Safety at Work etc. Act 1974, after a patient fell from a second floor window to their death. Despite recent publicity and prosecutions following a number of fatalities, the trust failed to ensure that the window had sufficient restrictions in place to prevent such an incident and were fined £10,000.

2.9 Information from the 28 regulators who submitted evidence to me suggests that the average fines handed down by magistrates are relatively low, when compared to the fine maxima available. As set out in Table 2.1 below, average fines for businesses ranged from as little as £488 to £6,855. In environmental and health and safety cases, the average fines are in the range of £5,000 to £7,000. This does indicate that the deterrent effect of fines is likely to be limited for all but the smallest businesses.

### Table 2.1: Level of financial penalties 2004/2005

<table>
<thead>
<tr>
<th></th>
<th>Prosecutions</th>
<th>Convictions</th>
<th>Average financial penalty</th>
</tr>
</thead>
<tbody>
<tr>
<td>Health and Safety Executive*</td>
<td>1,267</td>
<td>999</td>
<td>£6,855*</td>
</tr>
<tr>
<td>Environment Agency*</td>
<td>887</td>
<td>876</td>
<td>£5,007</td>
</tr>
<tr>
<td>British Potato Council**</td>
<td>246</td>
<td>28</td>
<td>£488</td>
</tr>
<tr>
<td>Pesticides Safety Directorate</td>
<td>3</td>
<td>1</td>
<td>£1,800</td>
</tr>
<tr>
<td>Food Standards Agency</td>
<td>570</td>
<td>458</td>
<td>N/A</td>
</tr>
</tbody>
</table>

* Figures for 2005.

Source: Data submitted by regulators to the Penalties Review, February-April 2006

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2 This figure excludes the convictions with fines of over £100,000. Of those excluded, there was one fine of £2,000,000; three fines at £300,000 or above; and thirteen fines of between £100,000 and £300,000. If these seventeen convictions were included, the average for 2004/05 rises to £12,642. Reference HSE Offences and Penalties Report 2004-05, available at www.hse.gov.uk/enforce/off0405/figures.htm.
2.10 There is also evidence that for some offences the average fines are considerably below the maximum fine. For example, the average fine for non-compliance with the Trade Descriptions Act 1968 was £1,524 against a maximum fine available in the legislation of £5,000. Offences under the Health and Safety at Work etc. Act 1974 led to fines of £6,014 on average, against a maximum fine up to £20,000 depending on the offence. These are only two examples and are not meant to suggest that courts should always aim for the maximum penalty available. I do believe, though, that these examples can be indicative of the level of fines currently handed down under the criminal courts for particular offences.

2.11 The Government has previously recognised that in the area of health and safety, courts are in need of greater sentencing power and that there is scope for extending maximum fines available in the health and safety legislation.

2.12 In 2004, the House of Commons Environmental Audit Committee found, in its sixth report, that the level of sentences given in courts for environmental crimes is too low and recommended the introduction of alternative sentencing powers such as adverse publicity orders and environmental service orders.

2.13 The academic literature on penalties often reaches similar conclusions. For example, a study of penalties for environmental offences found that, with the exception of the Netherlands, fines were generally low in the European Union, and included judicial lack of familiarity with environmental law and low judicial and public awareness of the harmful consequences of pollution among the reasons.

2.14 I acknowledge that each firm will have its own financial circumstances and context such as the ability or means to pay a fine, which must be taken into account by a court when determining the appropriate fine. However, the low level of average financial penalties indicates that the deterrent effect of these penalties will be less meaningful for all but the smallest of businesses.

Regional Variation

2.15 I believe that it is right for individual cases to have differing outcomes depending upon the needs of the offender, the nature and seriousness of the offence and all of the other factors taken into consideration when determining a sentence.

2.16 I present data on regional variation which can raise some questions as to whether the regional variation is all due to the different nature of the offences and circumstances of the offender or whether it indicates a difference in other factors such as the courts’ view of the seriousness or importance of certain types of offences.

2.17 A typical example comes from the Food Standards Agency, who cited the case of a company prosecuted for very similar offences in two different parts of the country. In the one instance, the business was fined £20,000 and in the other £5,000.
2.18 The Environment Agency has noted that average fines handed down by magistrates for environmental offences vary considerably across regions. In 2004, average fines given for environmental offences in South West England reached a level of £2,000 while average fines given for similar offences in the Anglia region reached £7,000. Of course, there are numerous offences which the agency is prosecuting and these will all vary depending on what part of the country is being looked at. However, these factors are, in themselves, unlikely to explain the significant regional variations in average fines that the Environment Agency has discovered.

Figure 2.1 Regional average fines 2004 (Environment Agency)

Source: Data submitted to the Macrory Review by the Environment Agency, March 2006

Regulatory non-compliance in contrast to ‘mainstream’ crime

2.19 There are approximately 30,000 magistrates in the UK and these magistrates see approximately two million cases covering all areas of criminal law, on an annual basis.⁸ Excluding summary traffic offences, the majority of these cases relate to what is generally perceived as ‘mainstream’ crimes, i.e. assault, burglary, drugs offences or other behaviour that is criminal in its own right.

2.20 Non-compliance with regulatory obligations, on the other hand, can be perceived as the result of an economically productive act. There is a perception that with the day-to-day workload of magistrates, dominated by ‘mainstream’ crimes, the courts tend to look upon regulatory offenders as having committed “lesser” offences. This argument is explored in more detail in Annex D. The consequences for society of regulatory non-compliance can as a whole be as serious as those of ‘mainstream’ crime.

Resolution of criminal cases takes time and money

2.21 Criminal prosecutions by their nature are a slow and time consuming process. This may seem like an inappropriate use of resources for a company that is being prosecuted for a strict liability offence. In these instances, businesses and regulators may prefer to resolve cases of regulatory non-compliance in a more timely manner. The Environment Agency reports that in its experience cases on the whole take an average of seven months from discovery of an incident of non-compliance to when proceedings are commenced. This constitutes approximately five months for investigation and two months for legal review of the evidence and commencement of proceedings. The Health and Safety Executive (HSE) estimates that from an offence to approval of prosecution about 20 percent of cases are approved for prosecution within three months of the offence date, and more than 50 percent within six months. Four out of five cases are approved for prosecution within 12 months.

2.22 Although the time spent on preparing for a court case is necessary, and is spent investigating, considering the evidence, taking legal advice, and so on, for a business, this means that a regulatory non-compliance which was rectified can still be an issue that management has to deal with several months on. Industry may prefer a more timely resolution to appropriate cases of regulatory compliance as the delay and the uncertainty of the outcome can be an additional burden for the firm. The resource implications that prosecutions demand from regulators can also be significant.

“… in many cases even where a building control officer recommends prosecution, the authority’s solicitor will not proceed because of the costs of legal and technical staff time needed to prepare and prosecute a successful case…” Local Authority Building Control (LABC)

Source: Response from LABC to the Macrory Review, February 2006

Limited range of enforcement tools

2.23 I have suggested that regulators do not have an appropriate range of enforcement tools to work with. Stakeholders have supported this view.

“Defra supports the widely held view, espoused also in Hampton, that the current system is not sufficiently responsive, targeted and sensitive to ensure that appropriate penalties are applied in all cases. To this end, the department accepts that there is room for improvement but restates its basic tenet that a robust penalties framework should encompass different types and levels of sanctions depending on the nature, frequency and seriousness of non-compliance.” Defra

Source: Response from Defra to the Macrory Review, February 2006
2.24 Today, as discussed in chapter one, regulators are heavily reliant on criminal prosecutions, which remain the primary formal sanction available to them. While criminal prosecution is appropriate for some cases, it is an expensive and slow process for both regulators and businesses. It attaches a severe moral condemnation and a criminal record to a business or individual, which may not be appropriate for all regulatory offences, especially where no intention or recklessness is involved. Whilst criminal proceedings may be appropriate for the most serious cases, a criminal prosecution may not be the most effective tool in achieving a change in behaviour and improving outcomes for a large number of businesses where the non-compliance is not criminal in its intention.

Table 2.2: Mapping of regulators’ enforcement tools

<table>
<thead>
<tr>
<th></th>
<th>Financial Services Authority</th>
<th>Health Safety Exec.</th>
<th>Food Standards Agency</th>
<th>Environment Agency</th>
<th>Comp. House</th>
<th>Charity Comm.</th>
<th>Defra Core dept. regulators</th>
</tr>
</thead>
<tbody>
<tr>
<td>Criminal prosecution</td>
<td>●</td>
<td>●</td>
<td>●</td>
<td>●</td>
<td>●</td>
<td>N/A</td>
<td>●</td>
</tr>
<tr>
<td>Licence revocation</td>
<td>●</td>
<td>●</td>
<td>●</td>
<td>●</td>
<td>N/A</td>
<td>N/A</td>
<td>●</td>
</tr>
<tr>
<td>Licence suspension</td>
<td>●</td>
<td>●</td>
<td>●</td>
<td>●</td>
<td>N/A</td>
<td>N/A</td>
<td>●</td>
</tr>
<tr>
<td>Admin financial penalty</td>
<td>●</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>●</td>
</tr>
<tr>
<td>Fixed admin financial penalty</td>
<td></td>
<td>●</td>
<td>●</td>
<td></td>
<td></td>
<td></td>
<td>●</td>
</tr>
<tr>
<td>Statutory Notices</td>
<td>●</td>
<td>●</td>
<td>●</td>
<td>●</td>
<td>●</td>
<td>●</td>
<td>●</td>
</tr>
<tr>
<td>Warning letter</td>
<td>●</td>
<td>●</td>
<td>●</td>
<td>●</td>
<td>●</td>
<td>●</td>
<td>●</td>
</tr>
<tr>
<td>Persuasion</td>
<td>●</td>
<td>●</td>
<td>●</td>
<td>●</td>
<td>●</td>
<td>●</td>
<td>●</td>
</tr>
</tbody>
</table>

Source: Responses from regulators to the Macrory Review, February 2006

2.25 Regulators are relying on criminal prosecution for a number of reasons, the most important being a lack of effective intermediate options. As set out in Table 2.2 above, the sanctions to which the majority of regulators have access are either a warning letter at the informal end of the spectrum or a criminal prosecution at the other. Most regulators have limited access to administrative penalties and other sanctions as an intermediate step as indicated in the table.

9 The FSA have access to other enforcement options, which are not in the table, and can for example seek injunctions, make restitution orders and make prohibition orders against persons who are not fit and proper.

10 The Environment Agency also has access to issue cautions. These are formal written admissions of guilt which obviate the need for a prosecution. They are used against individuals as opposed to corporate offenders.

11 Companies House does not operate a licence regime. Therefore the licence suspension and licence revocation sanctions are not applicable. Criminal sanctions are not available to the charity commissioner.

12 The Charity Commission does not operate a licence regime. Therefore the licence suspension and licence revocation sanctions are not applicable. Criminal sanctions are not available to the Charity Commission.

13 Defra core departmental regulators include regulators operating in the areas of Environmental Impact Assessment (uncultivated land), Cattle Identification Scheme, Horticulture (classification of imported fruit and vegetables, Pesticides Safety, Waste Management, Fisheries and Ozone. Regulators can also confiscate assets, set up restorative conferences with offenders and can in some cases enter into voluntary and enforceable undertakings.
Is there a compliance deficit?

2.26 I believe that compliance levels in the UK are high. This is reflected in the good standards that are generally apparent and the lack of incidents related to regulatory non-compliance that occur. However, it can be frustrating for both regulators and businesses, when regulatory non-compliance is not addressed because the regulator lacks the appropriate enforcement mechanism.

2.27 I conclude that this problem creates what is known as a compliance deficit. This is the case where non-compliance exists and is identified but no enforcement action is taken because the regulator lacks the appropriate tool to effectively sanction. As noted by Local Authority Building Control above, there are also instances when, due to a lack of appropriate tools, a case of non-compliance is simply not addressed by regulators.

2.28 It is difficult to assess the general level of compliance because not every firm is inspected and not every incidence of regulatory non-compliance is identified. Tangible data is absent in this area. However, I have attempted to get some indication from regulators on the overall effectiveness of enforcement strategies on compliance levels. This has been a difficult process and most regulators are able to comment on their numbers of prosecutions or number of enforcement notices imposed, but are unable to draw any conclusions on what this means to overall compliance.

Responses to the penalties review

2.29 I invited all interested parties, including regulators, business, the courts and other relevant stakeholders in the enforcement process to consider a range of questions and proposals in the call for evidence in December 2005. The responses to the call for evidence indicate that across the board there is support for the key aims and ideas that the penalties review outlined.

<table>
<thead>
<tr>
<th>Box 2.3</th>
<th>The Macrory Review’s call for evidence, December 2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>In December 2005, the Macrory Review invited all stakeholders to comment on the issues raised in the report, <em>Regulatory Justice: Sanctioning in a post-Hampton World.</em></td>
<td></td>
</tr>
<tr>
<td>I received 51 responses; of which 28 came from regulators, nine from businesses or business organisations and six from specific interest groups. I also had comments from individuals and local authorities.</td>
<td></td>
</tr>
<tr>
<td>The statistical figures were compiled using data from the responses, and exclude those who chose not to respond to a particular question. The statistics are based on a limited number of responses from regulators, businesses and special interest groups, and should be considered as indicative only of the views within such groups.</td>
<td></td>
</tr>
<tr>
<td>The statistical figures include a Yes, No and Neutral category, whereby a ‘Yes’ corresponds to a positive agreement to a question, and a ‘No’ corresponds to a negative one. The ‘Neutral’ category corresponds to answers which were neither giving positive agreement nor expressing disagreement with an issue or suggestion.</td>
<td></td>
</tr>
</tbody>
</table>
Is criminal prosecution effective?

2.30 A key question that I has set out to address is whether criminal prosecution is an effective tool in dealing with regulatory non-compliance?

2.31 Overall, the responses we have received are nuanced. On the one hand, regulators and business consider prosecution to be effective, particularly in dealing with serious criminal offences. On the other hand, there is also a widespread belief that the current system is not adequate.

2.32 Of those who responded, 43 percent answered ‘Yes’ to the question ‘Is criminal prosecution an effective tool in dealing with regulatory offences’, with only eight percent saying it was not. But 60 percent of the respondents answered ‘No’ when asked if ‘In general, do you think the current system is adequate’.

43 percent say criminal prosecutions are effective for regulatory offences

60 percent think the current system is inadequate

“The difficulty which the GOC sees in the sole use of criminal prosecution is that, with the sanctions available, the financial implications of non-compliance are not inclined towards encouraging future compliance. While some courts have made use of conditional discharges, the ultimate sanction for a breach remains a financial penalty.”

General Optical Council

Source: Response from General Optical Council to the Macrory Review, February 2006

2.33 I believe that this statistical evidence is not necessarily contradictory. Rather, there is consensus that criminal prosecution is effective when dealing with the most serious types of offences, and that it would not be appropriate to dismiss the criminal route altogether. The responses also support the notion that currently there is too much reliance on criminal prosecution, and that for less serious offences alternatives are needed.

Figure 2.2 Criminal Prosecutions for Regulatory Offences
2.34 The responses are less ambiguous when it comes to the question of re-categorising or even de-criminalising some offences. Respondents are generally reluctant to go down the decriminalisation route. However, many respondents, particularly the trade organisations, stress the importance of maintaining criminal prosecutions for only the most serious offences.

“It is effective in certain circumstances where the public interest is served from the publicity, or knock on effects, a prosecution might attract. However in general fines do not exceed the financial gain to those prosecuted or represent the costs of taking the prosecutions to court. SCOTSS believes strongly that any penalties must be of sufficient scale to deter non compliance. One of the difficulties with criminal prosecution is that it seldom brings direct restoration or benefit to the victims of any crime.”

**Society of Chief Officers of Trading Standards in Scotland**

Source: Response from SCOTSS to the Macrory Review, February 2006

**Greater use of administrative penalties**

2.35 Responses indicate that there is support for greater use of administrative sanctions among regulators and special interest groups and, though to a lesser degree, also among some business organisations.

**Figure 2.3 Administrative Penalties**

Should the review look to the greater use of administrative penalties as an option for intermediate sanctioning?

<table>
<thead>
<tr>
<th></th>
<th>Regulators</th>
<th>Businesses</th>
<th>Specific Interest Groups</th>
</tr>
</thead>
<tbody>
<tr>
<td>Neutral</td>
<td>18%</td>
<td>43%</td>
<td>29%</td>
</tr>
<tr>
<td>Yes</td>
<td>76%</td>
<td>29%</td>
<td>67%</td>
</tr>
<tr>
<td>No</td>
<td>6%</td>
<td>43%</td>
<td>33%</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
2.36 Overall, two-thirds of respondents supported the extension of administrative penalties. Only 14 percent were against.

“Administrative sanctions are attractive because they can be speedy and have an immediate impact giving the enforcer a tool which has some bite.” [DTI]

Source: Response from DTI to the Macrory Review, February 2006

2.37 Regulators are the most enthusiastic supporters of expanding the use of administrative penalties. It is a commonly held view that administrative penalties would be an appropriate alternative to criminal sanctions. Regulators believe that it would allow for more flexibility and swifter action, in particular in less serious cases where criminal prosecution is considered a heavy handed approach. I would caution that the use of administrative penalties is not meant to replace the pursuit of serious cases into the criminal courts. Administrative penalties are also not meant to replace other enforcement actions such as the use of Enforcement Notices or advice and education. Administrative penalties should only be used in the appropriate circumstances and within a transparent, proportionate and accountable framework as set out in chapter one. We discuss administrative penalties in more detail in chapter three.

“It is accepted that administratively imposed penalties are now part of our way of life and indeed, given the vast number of ways in which individuals and organisations can now transgress the law, it would probably be impossible for courts to deal with all such offences as well as their more traditional business.” Justices’ Clerks’ Society

Source: Response from Justices’ Clerks’ Society to the Macrory Review, February 2006

2.38 Businesses also emphasise the need for more flexibility, and are in some cases supportive of greater use of administrative penalties. In particular small business representatives have stressed the need for a swifter and less costly enforcement processes, and consider administrative penalties as a possible route to achieve this.

2.39 However, business also expressed a concern that greater use of administrative penalties could lead to more frequent use of penalties and possibly more fines imposed on individual businesses. In particular, the introduction of fixed administrative penalties is a concern for business, which fears that it might damage the trust between a regulator and the regulated business. We comment on this in more detail in chapter three.

Enforcement Notices

2.40 In the current regime, a number of regulators have the power to issue an Enforcement Notice requiring compliance in the future from a regulated business. A majority of respondents feel that the current system of Enforcement Notices achieves its goal. However, respondents also believe that there is room for improving the effectiveness of the current system.
2.41 Today, most regulators use the threat of a possible criminal prosecution to encourage businesses to follow the instructions set out in an Enforcement Notice. The call for evidence shows that 22 percent of the respondents believe that coupling Enforcement Notices with an administrative penalty for non-compliance would be more effective than the threat of criminal prosecution. Fifteen percent disagree with this approach.

Figure 2.4 Enforcement Notices

Do you feel the current system of enforcement notices requiring compliance in the future achieves their goal?

- Yes: 52%
- Neutral: 37%
- No: 11%

Figure 2.5 Enforcement Notices + Administrative Fines

Would coupling enforcement notices with an administrative penalty for non-compliance be more effective in securing compliance than the threat of a criminal prosecution?

- Yes: 22%
- Neutral: 63%
- No: 15%
2.42 Regulators are generally more enthusiastic about coupling Enforcement Notices with an administrative penalty than business organisations. Many feel that Enforcement Notices are effective, but that there might be circumstances where Enforcement Notices coupled with an administrative fine would work better.

Financial penalties

2.43 Respondents generally agree that the financial penalties that are currently being handed down by Magistrates and Crown Courts are not a significant deterrent for cases of regulatory non-compliance. Across the board, regulators and businesses agree that there is need for fines to reflect the seriousness of an offence more accurately than is currently the case.

2.44 Only five percent of the respondents believe that in the current system, “financial penalties handed down in the Magistrates and Crown Courts are appropriate and effective for regulatory offences”, and 50 percent answered that they do not think the financial penalties handed down for regulatory offences are appropriate.

Figure 2.6 Financial Penalties in Magistrates Courts

2.45 I have asked respondents if the financial penalty should reflect the economic gain derived from non-compliance. Responses are generally supportive of this view, with 69 percent in favour and 14 percent against such a proposal.
2.46 There is also support for a system where the financial penalty, in the case of regulatory breaches, reflects the level of harm or potential harm caused. Sixty-one percent of responses support this idea with only six percent being against it. However, businesses tend to view this question more negatively. While most are neutral, 33 percent of businesses said ‘No’.

![Figure 2.7 Economic Gain](image)

Should the financial penalty in the case of regulatory breaches reflect the economic gain derived from the non-compliance?

- Yes: 69%
- Neutral: 17%
- No: 14%

![Figure 2.8 Level of Harm Caused](image)

Should the financial penalty in the case of regulatory breaches reflect the level of harm or potential harm caused?

- Yes: 61%
- Neutral: 32%
- No: 6%
Responses are supportive to the question of whether the level of financial penalty should take account of other factors such as previous compliance record, the ability to pay and the seriousness of the offence. Eighty-four percent of the responses were generally favourable towards such proposals, although there was mixed support for the listed examples.

Alternative sanctions

There is support for introducing alternative sanctions for regulatory non-compliance. However, specific proposals, for example that reputational sanctions should be used more by regulators, got a more mixed reception, depending on respondents. Our discussion of the type of sanctions that fall within the category of ‘alternative sanctions’ is set out in chapters five and six.

Almost 90 percent of respondents agree to the general introduction of alternative sanctions. Only a small percentage of respondents are specific about whether such sanctions should be introduced by regulators or the courts.

In sum, the responses indicate that regulators and business agree to the need for alternatives but there are various views on what these alternatives should be and at which institutional level they should be introduced.

What do respondents want?

There is consensus that a sanctioning system should be more flexible, proportionate and coherent and that exploring a wider range of tools for regulators would be a necessary step in achieving this objective.

A majority of respondents think that the current system is generally inadequate, that there should be greater use of administrative penalties and that ‘alternative’ sanction options should be available to regulators.

Respondents have different views on the merits of the current system and the prospects of the changes that might arise from my review. Some are concerned that there is too much reliance on criminal prosecution, leaving regulators unable to address appropriately less serious offences. Others consider criminal prosecution to be effective when dealing with serious or repeated regulatory offences, and are concerned that greater use of administrative penalties means that more businesses would be fined on a more regular basis.
Chapter three

Monetary Administrative Penalties

The previous chapter considered evidence submitted to the review. This chapter looks at an additional sanction that could be applied by a regulator: the potential role of Monetary Administrative Penalties (MAPs).

Administrative sanctions for regulators

3.1 The discussion in chapter one and the evidence presented in chapter two demonstrated that regulators are in need of a broader toolkit of flexible, quick and inexpensive sanctioning options. As previously discussed, the current sanctioning regimes are reliant on criminal proceedings, which may be a disproportionate response to the circumstances of non-compliance in any particular case, and which are costly to both the business and the regulator without necessarily resulting in the best outcome.

3.2 This chapter discusses the potential role for Monetary Administrative Penalties (MAPs) as a tool providing regulators and business with a more proportionate response, where appropriate, in addressing non-compliance with regulatory requirements.

3.3 The discussion in this chapter draws upon the evidence submitted to me, the academic literature in the area of administrative monetary sanctions as well as the experience of other OECD nations where administrative penalties have been introduced.

3.4 I am aware of the wider regulatory reform agenda which is focused on reducing administrative burdens of regulations, whilst maintaining or improving regulatory outcomes. I have looked to make suggestions that will modernise the sanctioning systems across regulatory regimes to be fit for purpose and consistent with the overall Better Regulation and Hampton agendas.

3.5 It is important to emphasise that the application of a MAP is not a revenue generating exercise designed to punish business with no recourse for an appeal or operating at the whim of a regulator without appropriate safeguards. MAPs, if introduced would operate with the appropriate safeguards and appeal mechanisms. Nor do I envisage that administrative sanctions will replace the need for criminal prosecutions in appropriate cases.

3.6 I present three monetary administrative penalty models for consideration in sections 3.40 – 3.51 below, but first I explain what I mean by MAPs.

Monetary Administrative Penalties (MAPs)

3.7 Administrative penalties, in general, consist of monetary penalties that are applied directly by a regulator. Criminal courts do not play a part in the process, and are generally not involved in their application. The recipient of a MAP has a right of appeal through an administrative appeals mechanism which usually takes the form of an administrative, specialist tribunal. For example, a recipient of an administrative penalty under the Financial Services and Markets Act 2000 is entitled to a complete rehearing of their case before the Financial Services and Markets Tribunal.

3.8 Administrative penalties as currently used in the UK can either be in the form of a fixed penalty, or a variable penalty – both of which are discussed and explained in more detail in paragraph 3.32 – 3.40 below.
3.9 I believe that the UK has lagged behind other nations in the introduction of administrative penalties. While some regulators do use administrative sanctions, it is not a tool that is widely available or utilised. The introduction of administrative sanctions in more regulatory regimes would fill a gap that exists in the current enforcement pyramid of many regulators (see Annex A). Administrative penalties can provide an intermediate step between the formal, costly and stigmatic action of criminal prosecution and the more informal means of advice and persuasion to get firms into compliance.

3.10 Well designed administrative schemes can also be flexible and take a more customised approach in dealing with regulatory non-compliance. For instance, the frequency of non-compliance can be factored into the level of an administrative sanction. This would enable some level of differentiation between a first time offender and a repeat offender. Compliance history of the firm is just one example of an aggravating or mitigating factor that can be taken into account by a regulator when utilising administrative penalties. I discuss this and other factors later in the chapter in paragraph 3.55 – 3.59.

3.11 In order for administrative sanctions to work best, it is important that they operate within a system that is transparent, in order to maintain the confidence of the public and the regulated community. Regulators must be transparent in the way in which administrative sanctions are applied, the way in which the level of the financial penalty is determined and upon whom any such sanction has been imposed. These considerations should be set out in the regulators enforcement policy.

3.12 Overall, if introduced with the appropriate safeguards, I believe that administrative penalties would promote the goals of deterrence, fair and equitable treatment of the regulated community, a swift resolution of regulatory problems, and improved regulatory outcomes.

**Administrative penalties abroad**

3.13 Administrative penalties are becoming the norm in countries such as the US, Australia and Canada. Many European countries, including Germany and Sweden, also rely heavily on administrative sanctions in their regulatory enforcement activities. Administrative penalties in these countries are common in the area of environmental regulation, health and safety, financial services as well as within other regulatory regimes, such as the regulation of utilities and water.

3.14 In the United States, administrative penalties have been in place for more than 30 years and are used extensively. For example, at the federal level, in the area of environmental regulation, more than 90 percent of the enforcement activity is done through administrative routes.1

3.15 Australia is also using administrative penalties in a number of policy areas. Most state environmental regulators have a range of administrative notices and penalties available to them. Health and safety regulators across Australia also utilise administrative sanctions. For example, inspectors at the New South Wales health and safety regulator, WorkCover, may issue penalty notices (on-the-spot-fines), which can be imposed at the discretion of the regulator for a number of breaches identified by the legislation and set out in a publicly available schedule.2

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3.16 In Canada, administrative penalties schemes differ across the provinces but are in operation in a broad range of regulatory areas. British Columbia has been using administrative sanctions against offenders, in the environmental areas, whilst in Ontario, a scheme of administrative penalties is currently being consulted upon with a view to introduce administrative sanctions in 2007. Ontario is aiming to fill a gap in its enforcement pyramid and to respond more effectively to environmental violations. At the federal level, the Canadian Centre for Occupational Health and Safety has administrative penalties in its enforcement toolkit. Administrative sanctions in Canada are also part of the enforcement toolkit in the area of financial services, forestry management and food safety.

Box 3.1 Introducing Environmental Penalties – Ministry of the Environment, Ontario, Canada

Ontario is in the process of revising its environmental penalties regime. Key changes include the introduction of Environmental Penalties, which gives the Ministry of the Environment the authority to directly impose financial penalties on violators.

Ontario is looking to introduce Environmental Penalties (EPs) in order to fill a gap in its compliance toolkit. In 2004 Ontario experienced a number of industrial spills that had negative environmental impacts. Environmental Penalties will allow the Ministry to respond more quickly to such environmental violations, and therefore will encourage violators to take swift corrective action.

The introduction of Environmental Penalties means that the Ministry will have the authority to issue orders to an owner or a person having control of a pollutant to pay for all reasonable costs and expenses incurred by the province or any municipality to address adverse effects related to a spill. The department has acknowledged that the determination of an Environmental Penalty must take into account the seriousness of the offence. The Ministry will have a maximum Environmental Penalty Order of $100,000 per day. The funds collected will be deposited in a separate account for a special purpose, and could be made accessible to Ontario communities that are affected by environmental contraventions and pollution or are undertaking projects which improve the environment.

The Ontario scheme sets out a possibility for the Director and the violator to enter into a settlement agreement which can lead to the reduction or cancellation of the Environmental Penalty Order. The violator can also agree to undertake an environmentally beneficial project in respect of the negotiated settlement agreement, but which the violator is not otherwise legally required to perform.

Source: Stakeholder Consultation Paper Developing Environmental Penalties for Ontario, Ministry of the Environment, 2005

3.17 In the European Union, the use of administrative penalties is widespread and countries such as Belgium, Finland, Germany, Greece, Italy, Portugal, Spain and Sweden all use administrative penalties to address regulatory non-compliance. As evidenced in Box 3.2 below, the use of administrative penalties is not limited to OECD countries and they are used on a widespread basis, for example in the area of fisheries regulation. The UK Government is currently consulting upon the introduction of administrative penalties in the area of fishing. This consultation is being led by Defra.4

Box 3.2 Administrative Penalties in Fisheries Law – International Experiences

A 2003 study by the UN’s Food and Agriculture Organization revealed that administrative sanctions are commonplace among many OECD and non-OECD countries, for example in fisheries legislation.

Countries like Spain, Portugal, Equatorial Guinea, Peru and Mexico, all have a predominantly administrative sanctioning system, with a range of powers to warn and fine offenders. These countries also have additional powers for more serious infringements, such as the ability to suspend or withdraw fishing licences.

In other countries where fishing offences are primarily considered criminal offences, such as France, South Africa and Kenya, amended legislation provides for administrative sanctioning to complement the existing measures. These measures include the imposition of monetary fines or provisions to settle out-of-court.

The report suggests that fundamental to the decision to use administrative enforcement systems is a recognition that it could prove more effective than traditional criminal ones.

Source: Administrative Sanctions in Fisheries Law, United Nation’s Food and Agriculture Organization (FAO), 2003

Administrative penalties in the UK

3.18 The Hampton report identified that 43 regulators had criminal penalties available to them in tackling cases of non-compliance. Twenty-six were able to seek prison sentences for some offences and 15 regulators within the scope of the Hampton Review were able to impose administrative penalties.5 The UK experience with administrative penalties is largely limited to the financial regulators. The Financial Services and Markets Act 2000 secures the Financial Services Authority ("FSA") a broad range of civil, administrative and criminal sanctioning powers, including the power to issue monetary administrative penalties. The majority of FSA cases are dealt with by using administrative routes. Since 2000 more than 70 cases were concluded with an administrative penalty. Only six cases went through the criminal court system.

4 Consultation on a system of Administrative Penalties for Fisheries Offences, Defra, February 2006.
CHAPTER THREE: MONETARY ADMINISTRATIVE PENALTIES

3.19 The Competition Commission can impose financial penalties under the Enterprise Act 2002 (in relation to the powers set out in sections 109-111). The penalties can either be a fixed amount, not exceeding £20,000 or calculated as a daily rate, not exceeding £5,000 per day.\(^6\)

The Competition Commission has responded to the Penalties Review that it believes that the financial penalties are a more appropriate sanction than criminal prosecution in many instances. The Commission has never utilised powers to bring criminal proceedings for contempt of court under provisions in the Fair Trading Act 1973 (section 85), as these were viewed as cumbersome and potentially disproportionate.\(^7\)

3.20 In dealing with competition enforcement issues, the Office of Fair Trading has access to a broad range of enforcement tools, including financial penalties for non-compliance with competition law. The Office of Fair Trading has discretion to impose financial penalties that can be severe, but may not exceed ten percent of a firm’s relevant turnover.\(^8\) This power is one of many set out in sections 25-44 of the Competition Act 1998 and in the Enterprise Act 2002.

Effectiveness of administrative penalties

3.21 I have investigated the evidence that supports the view that administrative penalties are a more effective way of ensuring compliance whilst reserving criminal prosecution for the most serious cases.

3.22 Administrative penalties have been found in both the UK and in other OECD nations to be an efficient and effective way of achieving deterrence against contravening the law. They have the ability to remove or reduce the profit-making motive of regulatory non-compliance. Administrative penalties are applied by the regulator, who, as a competent and expert agency in the particular area of regulation, can take all of the relevant information into account when determining whether an administrative penalty is appropriate and, if so, at what level it should be applied. This can be of value in complex and technical areas where courts, for instance, may not have a similar level of specialist expertise.

3.23 The use of administrative penalties can maintain respect for and achieve the purpose of individual legislative provisions while keeping the legal cost of sanctioning for both government and industry at a minimum. Criminal prosecutions are a resource intensive enforcement option for both government and industry. Generally, if the cost of enforcement is very high, it leads to lower outcomes because regulators will only be able to pursue a small number of cases. In addition, some cases of regulatory non-compliance will not be sanctioned at all because prosecution may not be appropriate or in the public interest. If regulators can have access to lower cost enforcement options, this can result in better outcomes such as improved compliance as more firms that are not in compliance can be sanctioned and brought into compliance.

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\(^6\) As provided for in the Competition Commission (Penalties) Order 2003 [SI 2003/1371].

\(^7\) These powers were repealed by the Enterprise Act 2002 and Media Mergers (Consequential Amendments) Order 2003 [SI 2003/3180].

\(^8\) As defined in the Competition Act 1998 (Determination of Turnover for Penalties) (amendment) Order 2004 [SI 2004/1259].
3.24 In comparative studies of administrative and criminal enforcement processes in the US and Canada, Brown and Rankin (1990) and Brown (1992) demonstrate that, in a system with administrative sanctions, offenders are more likely to be identified and penalised than in a system relying solely on criminal prosecutions. As a consequence, compliance is expected to be significantly higher in systems with administrative penalties than in systems which rely exclusively on the criminal courts.

3.25 The two studies referred to above identified a number of reasons why administrative sanctions have proven more effective in bringing offenders into compliance:

- **Administrative sanctions are more effective when operating within a risk-based regulatory environment.** Regulatory non-compliance in a risk-based system is focused on preventing harm rather than on the need for actual harm to occur. An administrative system is suitable for a risk-based system since it is not dependent on an actual event to occur. For instance, a firm can be in regulatory non-compliance and the non-compliance may not have actually resulted in a serious consequence. However, if the non-compliance persisted, it could lead to a serious incident. It is these occasions when non-compliance exists but has not yet caused any real damage that administrative penalties could be appropriate. Criminal courts are normally more appropriate for handling cases when there has been actual harm caused by regulatory non-compliance.

- **Administrative penalties are less stigmatising.** Regulators may be deterred from initiating prosecutions because it would be a disproportionate response to the circumstances of the failure to comply with regulatory obligations. Regulators consider administrative penalties as less draconian and a more appropriate response for certain types of non-compliance. I have heard about examples where criminal prosecutions are taken against legitimate industry for strict liability offences because this is the only formal sanctioning power available to a regulator under the relevant legislation, leading to a feeling of unfairness from industry and, in my opinion, a devaluing of the criminal process.

- **Administrative procedures are less cumbersome.** Regulators might also be deterred from bringing a prosecution to avoid the labour intensive criminal process. The pursuit of criminal prosecutions may absorb a large portion of a regulator’s enforcement budget. Regulators may choose to pursue lower cost enforcement options which will have more of an impact across a larger number of firms rather than pursue the high cost prosecution in a case where it may provide a satisfactory outcome in any event but at a greater cost.

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“A regime of administratively imposed sanctions is particularly suited to defaults that are highly technical or where the resultant offences are ones of strict liability. Courts on the other hand are best suited to making judgements on the basis of fault, particularly where intention or recklessness are necessary ingredients. It is suggested that courts should remain as the final arbiters of penalty for such offences.” **Justices’ Clerks’ Society**

Source: Response from Justices’ Clerks’ Society to the Macrory Review, February 2006

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• Administrative penalties can be more proportionate. There is evidence to suggest that in an administrative penalty system the level of penalties may be able to match the financial gain made by not complying with regulatory obligations and capture this financial benefit.

3.26 Dr. Carolyn Abbot, a lecturer in the School of Law at the University of Manchester, found that Australian environmental regulators generally have a broader enforcement toolkit than their English counterparts, and argued that if administrative penalties were introduced in the UK it would generally strengthen regulators’ hands in securing compliance.\(^\text{10}\)

3.27 In a UK context, my previous research has demonstrated that administrative penalties would provide a more cost-effective means of dealing with less serious environmental offences than the criminal law.\(^\text{11}\) We also found that there is increasing recognition of the benefits of employing administrative penalties as part of any effective system of regulation, and recommended that administrative penalties should play a significant role in delivering a proportionate, risk based approach that will improve compliance with environmental regulation.

3.28 Support from stakeholders suggests that a greater use of administrative penalties could be as effective in the UK as it has proven to be in countries with comparable judicial systems such as Australia and Canada. I have found that UK regulators, and to some extent also trade associations and businesses, generally believe that administrative financial penalties would be an effective and appropriate additional enforcement option alongside criminal prosecution.

3.29 As set out in chapter two of this report, of the 51 respondents to the call for evidence more than half answered favourably to the question of introducing administrative penalties as an additional tool for the regulatory toolkit, of course with the appropriate safeguards and guidance. A total of 66 percent supported the extension of administrative penalties. Less than 15 percent were against.

Models of administrative penalties for consultation

3.30 I have examined the evidence submitted to me and also studied the literature and the experience of other countries with administrative sanctions and identified three models of Monetary Administrative Penalties which I would like to consult upon. These are discussed in more detail below. The models share a number of common elements but also differ in a few of their major features such as the relationship with the criminal courts.

3.31 It is important for me to define a series of terms before I engage in the discussion of the models in order to clarify what the various terms mean and avoid confusion.

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Fixed Monetary Administrative Penalties (FMAPs)

3.32 Firstly, I will refer to the term “Fixed Monetary Administrative Penalty” (“FMAP”). FMAPs are generally found to be for small amounts and are applied in respect of low-level, minor, high-volume instances of non-compliance. Legislation specifies both the nature of the offence as well as the fixed amount of the fine. The regulator does not have discretion as to the level of the financial penalty, but does have discretion in whether or not to apply a penalty in the first instance.

3.33 Examples of fixed penalties in the areas of regulation covered by the review exist in other OECD nations visited by the review. These include on-the-spot fines from the Environment Protection Agency of New South Wales, WorkCover in New South Wales, the Ministry of Labour in the Canadian province of Ontario as well as the Occupational Safety and Health Agency (OSHA) in the US. Fixed penalties also exist in the UK. For example, tax forms submitted after the published deadline can result in a fixed penalty of £100 by HM Revenue and Customs. Also, in the area of vehicle operating, inspectors can give on-the-spot fines to lorry drivers who are not compliant with regulations.

3.34 Fixed MAPs are generally appropriate for low level breaches and the amount of the fines is quite low. However, international practise suggests that they can still be meaningful and significant as a sanctioning tool. As set out in the textbox below, in the area of health and safety in New South Wales, Australia, the on-the-spot fine scheme in operation by WorkCover, ranges in level of fine from A$80 to A$1,200. The average fine is A$550. The schedule for the penalties is set out in the relevant legislation (Occupational Health and Safety Act 2002). In some regimes legislation provides for a scaling up of penalties relative to the size of the company.

3.35 Evidence from Canada and the US suggests that fixed penalty offences can provide an effective deterrent to improve regulatory compliance. For example, the Canadian Food Inspection Agency introduced fixed penalties in their cattle identification regime. Anecdotal evidence presented to this review by the agency suggested that before the fixed penalties were introduced, compliance in the regime was approximately 60-70 percent, whereas once fixed penalties were introduced, compliance rates improved to greater than 90 percent.¹²

3.36 Individuals and companies are both liable for these fines and in order to reflect the differing means to pay and ability to absorb these costs, many administrative sanction regimes reflect these differences through a scaling up of the financial penalties through a published and agreed upon multiple for corporations. WorkCover and the Environment Protection Authority in New South Wales are both examples of this approach.¹³

¹² Notes from meeting with SMART Regulation officials, Ottawa, Canada, March 15 2006
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The health and safety regulator, WorkCover, in New South Wales, Australia, uses fixed penalty notices as an enforcement tool against employers. The options include penalty notices, an on-the-spot-fine handed down to businesses where the inspector is of the opinion that advice or direction is not sufficient. WorkCover considers penalty notices as an effective method of dealing with less serious breaches of the legislation.

Inspectors will consider various factors when determining whether to issue a penalty notice. These factors include:

- if the breach can be remedied quickly
- if the issuing of a penalty notice is likely to have the desired deterrent effect
- if the breach is a one-off situation or part of an ongoing pattern of non-compliance

The Occupational Health and Safety Act 2002 identifies a range of offences and determines a corresponding penalty. Fines range from A$80 to A$1,200. The average fine is A$550. The schedule of breaches with corresponding fixed financial penalties secures that there is transparency when the decision is taken to impose an on-the-spot-fine on a business.

A person served with a penalty notice may elect not to pay the penalty and to have the matter dealt with by the court. The procedure for making an election is set out on the back of the penalty notice.

Source: WorkCover compliance policy and prosecution guidelines, WorkCover, New South Wales, March 2004

Variable Monetary Administrative Penalties (VMAPs)

3.37 “Variable Monetary Administrative Penalties” (“VMAPs”) are sanctions applied by the regulator without the intervention of a court or a tribunal. Instead of being for a small fixed amount pre-determined by legislation (as with FMAPs above), a variable penalty can be for a more significant amount determined at the discretion of the regulator in accordance with a published scheme and with an upper limit specified in the relevant legislation. Many significant factors can be taken into consideration by the regulator when determining the amount of the penalty such as mitigating or aggravating factors which we discuss in more detail in paragraph 3.55 – 3.59 below.

3.38 VMAPs can be larger and more representative of the level of financial gain as well as the seriousness of the impact of the non-compliance. In practise, these types of sanctions already exist in the UK and currently range in levels from unlimited financial penalties administered by the Financial Services Authority to ten percent of the relevant annual turnover in the area of competition law available to the Office of Fair Trading.

3.39 Alongside my recommendation for maximum fines in the criminal courts, I would welcome views on whether a fine maxima should exist for administrative penalties, or whether some form of a cap should be introduced. One option may be to adopt the principles under the Competition Act 1998 which provides the administrative penalties may not exceed ten

Box 3.3 Fixed Penalties Notices – WorkCover, New South Wales, Australia

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A person served with a penalty notice may elect not to pay the penalty and to have the matter dealt with by the court. The procedure for making an election is set out on the back of the penalty notice.

Source: WorkCover compliance policy and prosecution guidelines, WorkCover, New South Wales, March 2004
percent of the relevant turnover of the undertaking concerned. Where the financial benefit gained by non-compliance exceeds the fine maxima, I believe that provisions should be made to supersede these levels in order to capture the financial benefits. German administrative penalties attach such a condition.

**Box 3.4 Administrative penalties – USA and Australia**

USA and Australia are characterised by slightly different approaches to imposing administrative penalties on non-compliant businesses.

In the US regulators can levy monetary penalties without involving the courts, except in rare cases of judicial review of regulators’ actions. If a penalty is contested, the recipient of the penalty has a right of appeal to a second administrative agency. In the US a parallel criminal process does exist but prosecutions are extremely rare compared with administrative penalties.

In the Australian “hybrid” model the offending party can either discharge a regulatory breach through the payment of a monetary penalty, or elect to have the matter dealt with by the court. In practice, not many businesses choose the criminal route, since it includes the risk of a more severe penalty being handed down by the court. For example, in New South Wales out of the thousands of penalty notices served in 2003 only approximately 50 offenders elected to appear before the courts.

Source: Brown (1992) and Abbot (2005)

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**Model #1 – Applied Monetary Penalties (AMPs)**

3.40 Using this model the regulator would gather the evidence required for a criminal prosecution. However before proceeding to court the regulator would be able to propose the alternative of an administrative penalty to the business.

3.41 If the firm accepted this administrative penalty, then the matter would be concluded upon payment. This payment would go to either the consolidated fund or to a special dedicated fund independent of the regulator. The matter would be resolved by a payment and the firm would avoid the inconvenience and uncertainty connected with criminal proceedings.

3.42 If, however, the firm disagreed and did not want to make the payment, the regulator would proceed to take the case to court as per the present system.

3.43 This model, while relatively simple to introduce into the current regulatory landscape, would not be my preferred option based upon the evidence I have seen, because it is punitive in nature and could be seen as encouraging the offender into buying his or her way out of a prosecution. In addition, it would not reduce the evidentiary burden on the regulator and therefore not provide a sanction which could be applied at a significantly lower cost than traditional prosecution. In addition, should the firm choose to not pay the financial penalty, the case would revert back to the magistrates or crown court where the issue of low deterrence in sentencing is a feature (as discussed in chapter one).

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14 s. 36(8) Competition Act 1998

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3.44 I do not consider this the best option for reform.

Model #2 – FMAPs + VMAPs with appeals to the courts

3.45 A second model to consider is one where regulators can have access to Fixed Monetary Administrative Penalties (FMAPs) which, as mentioned above, are for low financial amounts, as well as Variable Monetary Administrative Penalties (VMAPs) which could be for more significant amounts. In this model, if a firm does not agree with the application of either an FMAP or a VMAP, it would appeal to the criminal courts.

3.46 This system would be a hybrid type of arrangement with an intermingling of administrative sanctions and the criminal process. I do not believe this to be an optimal choice for reform because of the lack of separation between administrative sanctions and criminal sanctions. The appeals mechanisms to the courts would again involve the issue of low deterrence, and financial penalties would have to be constrained by the fine maxima outlined in the criminal law, such as the levels on the standard scale in the Magistrates’ Courts. This would reduce the effectiveness and discretion of the regulator in imposing a low cost enforcement option. This model might also place undue strains on the criminal courts, which would have to absorb the appeals cases in their already significant workload.

3.47 I do not believe that this is the best option for reform.

Model #3 – FMAPs + VMAPs with appeals to an independent regulatory tribunal

3.48 This model is very similar to Model #2 in that the regulator would have the discretion to apply either a Fixed or Variable MAP. The only major difference is with regard to the appeals mechanisms.

3.49 Rather than having an appeals avenue to the magistrates courts, in this model, appeals would be heard before a specialist regulatory tribunal. There would be two advantages to this system: first, the tribunal could be composed of members with specialist expertise in the subject matter. I believe such a tribunal, with a fuller understanding of the issues, would deliver better outcomes to industry as well as regulators. Secondly, it would not be considering regulatory cases alongside the cases of violence and dishonesty which constitute the main workload of the Magistrates and Crown Courts but which are, I believe, fundamentally different in nature, and which are prosecuted for different public purposes. Such a tribunal could form part of the unified tribunal structure which the Government is committed to achieve. If, however, looking ahead there is any legislation following the recommendations of my review before general legislation on tribunals the new appeal tribunal should be established in the most cost-effective way possible using existing tribunals already administered by the Tribunals Service, the DCA’s new executive agency.

3.50 In addition, the separation of the administrative sanction from the criminal sanction would avoid any unnecessary confusion between the two. It is important to emphasise that the regulatory tribunal would not replace the criminal court system in any sense: its role would be to provide a route for appeals in relation to administrative penalties applied by a regulator. The financial penalties would not be tied into the criminal system and could fulfil the principle laid out in chapter one of removing the financial gains obtained as a result of non-compliance but without the imposition of a criminal conviction.
3.51 **Overall, I believe that model # 3 is the optimum choice for reform.**

**Table 3.1: Models of administrative penalties for consultation**

<table>
<thead>
<tr>
<th>Model 1: Applied Monetary Penalties (AMPs)</th>
<th>Model 2: FMAPs + VMAPs with appeals to the courts</th>
<th>Model 3: FMAPs + VMAPs with appeals to an independent regulatory tribunal</th>
</tr>
</thead>
<tbody>
<tr>
<td>● Regulator gathers evidence as if going to pursue criminal prosecution.</td>
<td>● Regulators have access to Fixed and Variable Monetary Administrative Penalties.</td>
<td>● Regulators have access to Fixed and Variable Monetary Administrative Penalties.</td>
</tr>
<tr>
<td>● The business has the option of paying the Monetary Administrative Penalty or to let the regulator proceed with the case in court.</td>
<td>● If the business does not agree with the penalty or merits of the case, it can appeal to the criminal courts.</td>
<td>● If the business does not agree with the penalty or merits of the case, it can appeal to a specialist regulatory tribunal.</td>
</tr>
</tbody>
</table>

**Features of Administrative Sanctions**

3.52 There are a number of features that must also be considered when examining the models laid out above. The following common elements would be shared across the models in broad terms but may differ in the detail slightly. Consideration of these commonalities will ensure that appropriate safeguards are built into the system so that it is fair, proportionate and transparent.

3.53 In addition to the elements discussed below, these sanctioning systems must be consistent with the Good Regulation and Hampton Principles as well as the proposed ‘Penalties Principles’ outlined in chapter one.

**How and when to apply the penalty**

3.54 The regulator would have discretion as to when to apply a Monetary Administrative Penalty (MAP) and how much that penalty should be, in the case of variable discretionary penalties. In the case of Fixed MAPs, these amounts will be specified in legislation and be easily accessible to business. In the case of Variable MAPs, regulators should generally publish the methodology they will use in determining the level of financial penalty. These could include mitigating or aggravating factors. If a cap would be appropriate for the maximum VMAP allowed, this should be set out in the relevant legislation.
Level of financial penalty

3.55 Determining the exact methodology for setting the level of the financial penalty will depend on the regulatory regime. However, I have come across a number of different approaches which I believe are useful to inform this discussion. One simplistic approach to determining the level of financial penalty is to estimate the probability of identifying a breach and multiply that by the expected gain from the regulatory non-compliance.

3.56 Another approach, regulators could consider, includes the extent of the deviation from the regulatory requirements and the potential for harm. This could be developed to involve consideration of the cumulative impact of the non-compliance, the extent of the non-compliance, the probability of exposure of the harm or harmful substance and the impact of the exposure of the harm or harmful substance.

3.57 Regulators could also consider some mitigating factors such as the introduction or revision of a management system, the co-operation of the firm, the timeliness of the corrective action and the timely and accurate reporting of the issue. Aggravating factors such as compliance history could also be taken into consideration as well as whether the contravention was due to wilfulness or negligence.

3.58 While I would not suggest that Government take a prescriptive approach to what methodology should be utilised, regulators should be transparent in whatever methodology they select and be held accountable for these decisions and choices.

Box 3.5 Aggravating and Mitigating Factors that could be considered for MAPs

In a system with Monetary Administrative Penalties regulators are required to develop and publicise a method for calculating the penalty for regulatory non-compliance. The following are examples of aggravating and mitigating factors which regulators could take into account when determining the appropriate penalty, although this list is not exhaustive and each decision will depend on the circumstances of the individual case:

**Aggravating factors**
- Seriousness of the regulatory non-compliance, e.g. the harm or potential for harm to human health or the environment, the duration of non-compliance etc.
- Evidence of intention (if any) behind the regulatory non-compliance.
- Disciplinary record or history of non-compliance of the business.
- Economic gain made by the business as a result of non-compliance with regulations.
- Size and financial resources of the firm that failed to comply with regulations.
- The conduct of the business after the regulatory non-compliance has come to the attention of the regulator.
- Previous actions taken by the regulator, or other regulators, to help the business into compliance.
Mitigating factors

- Actions taken to eliminate or reduce the risk of damage resulting from regulatory non-compliance.
- Actions taken to repair the harm done by regulatory non-compliance.
- Co-operation with the regulator in responding to regulatory non-compliance.
- Fast and accurate reporting of regulatory non-compliance.
- Size and financial resources of the firm that failed to comply with regulations.
- The conduct of the business after the regulatory non-compliance has come to the attention of the regulator.

3.59 The financial benefit of non-compliance is another factor that should be part of the methodology. This could include an individual or company that saves money and does not invest its resources in necessary equipment or systems in order to comply or uses those resources for another purpose. The financial benefit can also extend to the costs avoided or deferred and the illegal competitive advantage conveyed by the non-compliance. Therefore, administrative regimes could incorporate the monetary value to the individual or company of the failure to comply as well as consider the other aggravating and mitigating factors to determine the level of the financial penalty.

Box 3.6 Calculation of the Relevant Fine – Office of Fair Trading, UK

The Office of Fair Trading (OFT) has access to a broad range of enforcement tools in consumer and competition policy. It uses financial penalties as its principal sanctioning mechanism available under the Competition Act 1998 and the Enterprise Act 2002.

The twin objectives of the OFT’s policy on financial penalties is to impose penalties on infringing businesses which reflects the seriousness of the infringement and ensures that the threat of penalties will deter businesses from engaging in anti-competitive practices.

The OFT calculates the financial penalty imposed on a business with regard to

- The seriousness of the infringement
- The relevant turnover
- The duration of the infringement

When assessing the seriousness of the infringement, the OFT will take into account a number of factors, including the nature of the product, the market shares of the business, and the damages caused to consumers. The relevant turnover is the turnover of the business in the relevant product market and relevant geographic market affected by the infringement in the business’ last fiscal year.

The financial penalty may not in any event exceed ten percent of the relevant turnover.

Source: Office of Fair Trading response to the Penalties Review, February 2006
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Ability to pay

3.60 Some non-compliant businesses will seek to avoid paying administrative fines because of financial hardship or a lack of the means or ability to pay. Regulators will have to make their best efforts to determine the ability of a firm to pay and be proportionate in their decision making. Some regimes have set thresholds for payment, or introduced settlement options where it is possible to reduce the amount of the variable MAP by investing in preventative measures that would contribute to ensuring that the violation does not recur. I am interested in hearing views on this.

Who makes the decision to impose the sanction

3.61 Depending on the type of administrative sanctioning system, it is important to consider who within the regulator should be making the decision to impose the MAP. I believe that for low level FMAPs, these can usually be handed down by the field staff or inspector because of the low level of the financial penalty. An example of how this might be introduced in the UK is in the area of food labelling. The mis-labelling of food could be sanctioned with an FMAP imposed by a trading standards officer. However, for the VMAPs, which can be for more significant sums, I believe that this decision should be taken independently from the staff on the ground. This would serve to ensure that the relationship between the inspector and the firm is not compromised. In addition, it would ensure that industry is dealt with on a consistent basis by the regulator and that there would be some internal process and negotiation before a VMAP was imposed. The separation of the decision making process would also help ensure that the regulator was transparent and accountable in the use of administrative sanctions and would provide a framework to ensure that industry would be protected from the inappropriate application of administrative sanctions.

Funds would not be accessed by the regulator

3.62 An important principle that I support is that the revenue from administrative penalties should not be accessed directly or indirectly by the regulator that imposed it. This does not preclude the creation of a dedicated fund in a particular area or for the funds to be ring fenced for particular objectives such as consumer advocacy or environmental protection, but these monies should be managed independently from the agency that imposed their collection. A recent example of this type of arrangement is in the area of the congestion charge in London, where any fines collected through this scheme are set aside for Transport for London purposes. An example of this arrangement in the US is where administrative penalties collected by the Environment Protection Agency are apportioned to a superfund for future environmental cleanups if needed. The other option for the funds would be to go to the consolidated fund managed by HM Treasury. In any case, it is important that regulators do not have an incentive to increase their revenues by imposing more MAPs as this could create perverse incentives and undermine business confidence in the system.
3.63 It is important that any administrative penalty system carries with it the necessary protection for any person served with such a notice. On current models, this may either be satisfied with a right of appeal to a specialised tribunal (as with parking tickets) or the right to have the case prosecuted in the normal way before a criminal court (as with speeding offences). If increased use were made of administrative penalties in regulatory areas, my current view is that the best protection for a business which contests the notice lies in the right to have the matter heard before an independent body: either a tribunal or the criminal courts, although of these, my preferred choice is for an independent tribunal.

3.64 In addition, in order to satisfy human rights obligations and to ensure that the rights of the regulated community are protected and ensure that a system of administrative sanctions is fair, it is essential that the offender has a right of appeal to an independent court or tribunal. Each of the three options outlined above meets this essential requirement.

3.65 In the case of appeals to a regulatory tribunal I propose that businesses would have the right to a rehearing of the case and not just an appeal on the level of the penalty.

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**Box 3.7 Proposed key elements in a UK administrative penalties system**

- Fixed and Variable Monetary Administrative Penalties will be available to UK regulators. It is at the discretion of the regulator to decide if an offence should be subject to a Monetary Administrative Penalty or if criminal prosecution would be more appropriate.

- The level of Fixed Monetary Administrative Penalty is determined in the legislation as is the maximum Variable Monetary Administrative Penalty that can be imposed.

- When determining the appropriate level of a VMAP, the regulator must use a publicly available set of criteria including a set of mitigating and aggravating factors, which could for example take into consideration the economic gain made by the offender, the annual turnover of the offender, and the regulatory compliance record of the offender.

- The VMAP must reflect the seriousness of an offence or the economic gain that the offender has made by not complying with regulations as well as any other relevant factors.

- The revenue from Monetary Administrative Penalties will as a general rule not be accessed directly or indirectly by the regulator. The funds can be ring fenced for particular purposes or fall to the Treasury.

- To secure the transparency of the system, the regulator must disclose its policy on when and how a Monetary Administrative Penalty is applied, including a methodology for calculating the relevant fine.

- The recipient of a Monetary Administrative Penalty has a right of appeal either to an independent regulatory tribunal or a criminal court.

- The same system will not be applied universally across all UK regulators, but will be tailored to meet the particular demands of individual regulators and regulated industries within particular sectors or areas of regulation. Given the range of regulatory activity in the UK, there will be no “one size fits all” approach.

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Concerns about the introduction of Monetary Administrative Penalties

3.67 I am aware of a number of concerns regarding the potential introduction of administrative sanctions.

3.68 Some interest groups have expressed the concern to me that this will allow companies to just “buy their way out” of complying with the law. However, I believe that as long as there is transparency in this system, the firm’s non-compliance will still be a matter for the public record and that industry will not be doing a deal with regulators behind closed doors.

3.69 Another concern heard from both regulators and industry is that the availability of administrative sanctions will compromise the relationship between inspectors and industry resulting in an adversarial ticket-writing culture. Again, I believe that if regulators are operating with a published enforcement policy and within the parameters of the Hampton Principles and the Penalties Principles, the relationship between regulators and those they regulate will not deteriorate as a result of having additional tools in the toolkit.

3.70 Some industry groups have also expressed the concern that legitimate business will bear the burden of this additional tool since it is easier to impose than a criminal prosecution and as such will therefore switch the regulatory focus onto legitimate business rather than focusing on catching the rogues. I would argue that administrative sanctions may also be meaningful to capture some of the rogues operating within industries. If the financial gains of non-compliance are minimised, then rogue operators will not continue to obtain financial benefits and continue the non-compliance. Administrative sanctions would give regulators the opportunity to deter these rogue elements by having the ability to impose more significant financial penalties administratively.

3.71 Having access to an additional tool in the enforcement toolkit is an important addition for regulators. It will provide a means of addressing the non-compliance that currently goes unchecked even amongst legitimate business as a result of a lack of appropriate sanctions. This should help to address the issue of the compliance deficit, which is the situation where non-compliance exists, but it is not in the public interest to prosecute and so offenders do not face a sanction to change their behaviour. Instead, the non-compliance may continue, leading to lower compliance rates than if administrative sanctions were available.

Questions for consultation

1. In general, do you agree that regulators should have Monetary Administrative Penalties available to them as an additional sanctioning option in their enforcement toolkits? If no, then please elaborate on your views.

2. Do you prefer Model # 1 (paragraphs 3.40 – 3.44), Model # 2 (paragraphs 3.45 – 3.47) or Model # 3 (paragraphs 3.48 – 3.51). Please explain why you would prefer one particular model?

3. Should regulators have FMAPs available to them? For what types of offences (either in general or giving specific examples) would they be appropriate? What level of financial penalty would be appropriate for FMAPs?

4. Should regulators have VMAPs available to them? For what types of offences (either in general or giving specific examples) would they be appropriate?
5. Should the level of VMAPs be determined with regard to one or more of the following aggravating or mitigating factors:
   - Financial gain made by the offender
   - Offender’s past record of compliance
   - Annual turnover of the offender
   - The co-operation of the offender
   - The timely and accurate reporting of the issue
   - Timeliness of corrective action
   - Please provide other relevant factors which you feel should be included.

6. Should the level of VMAP be unlimited?

7. Should the maximum level of VMAPs be set out in legislation and be capped to never exceed ten percent of the relevant annual turnover as per the details of the Competition Act 1998?

8. Should there be provision to supersede the cap if the financial benefit is greater than the capped amount?

9. Should there be an option for settlement as an alternative to a MAP? In what sort of the cases should this be considered?
Chapter four

Statutory Notices

The last chapter described a system of Monetary Administrative Penalties, their role and options for consultation. I am aware that monetary penalties may not be effective in every instance and in an effort to ensure that regulators have access to a broad range of tools, I propose that regulators should also have access to alternative non-financial sanctioning options which are discussed in this chapter, specifically the introduction of “Enforceable Undertakings” and “Undertakings Plus”, which are explained below.

Enforcement Notices and Enforceable Undertakings

4.1 I argue that financial penalties, whether imposed as a result of a criminal prosecution or through an administrative system, may not always be the most appropriate sanction to get a business into compliance. In some instances, the regulator need only ‘persuade’ the firm and move it into compliance by explaining the merits of the regulation, or explain what it is the firm would need to do in order to comply. In other instances, where persuasion has failed or where a prosecution is not in the public interest or where a financial penalty is not appropriate, the regulator may need access to other types of sanctions. This could be to deal with firms that want to comply but may have some gaps in their management system or are small firms with limited resources.

4.2 Some offenders may be in severe economic difficulties and may not be able to pay even small fines. Other offenders, with significant annual turnover, may consider the monetary penalty as an overhead cost, which can be factored in to the costs of running a business with limited impact on actually changing corporate behaviour.

4.3 In addition to this, a monetary administrative penalty may also be less effective in restoring the harm caused when dealing with individuals or communities which have been harmed or otherwise impacted by the regulatory non-compliance. In some cases the offending business or individual might be able to, and have a desire to, undertake activities which aim to restore the harm that has been done.

4.4 For these reasons I have considered sanctions that look beyond the imposition of monetary penalties. This chapter will discuss regulators’ use of statutory notices such as Enforcement Notices, which are currently applied by regulators in order to bring the business into compliance for ‘minor types’ of offences. This chapter also discusses an additional option, Enforceable Undertakings (“EUs”), and whether it would be a good sanction to introduce to UK regulators. EUs are an alternative type of sanction that has proven effective in Australia and could be appropriate for more serious offences as it can include a strong element of restoration of the damage done by a business’ failure to comply with regulations. This chapter sets out a proposed model for introducing Enforceable Undertakings in the UK.

Statutory Enforcement Notices

4.5 In some instances of regulatory non-compliance, regulators will decide to issue a formal notice. The precise forms of Enforcement Notices and their conditions of use vary in different regulatory areas, but in general, Enforcement Notices require the recipient to do or refrain from doing a particular thing. They specify the steps a business must take to come into
compliance and the timescale for these changes. Depending on the statutory provision, an Enforcement Notice may also include remediation provisions relating to the damage caused by the business’ failure to comply with regulations. Failure to carry out the actions laid out in the notice is a criminal offence.

Box 4.1 Types of Statutory Notices

My report “Regulatory Justice: Sanctioning in a post-Hampton World” identified examples of different types of statutory Enforcement Notices that businesses can be subjected to by the regulator.

- Improvement Notices – demanding certain improvements to work practices while allowing time for the recipient to comply.
- Prohibition/Suspension Notices – prohibits an activity until remedial action has been taken in order to prevent serious harm from occurring.
- Work Notices – to prevent or remedy water pollution.
- Enforcement Notices – served where it is believed that a breach of regulatory consent or licence has occurred. The notice specifies the steps to rectify the breach and the timescale for these changes, and, depending on the statutory provisions, may include remediation provisions relating to the damage caused by the breach.


Box 4.2 Enforcement Notices – Availability and Use

Enforcement Notice powers are available in many areas of regulation considered in my review, from environment and food to trade and health and safety. Statutory Enforcement Notices, depending on the regulatory area and relevant legislative provision, include Enforcement Notices, Prohibition Notices, Improvement Notices, Suspension and Revocation Notices, and Abatement Notices. Provision is also made for Work Notices, Restoration Orders, Clean-up Orders and orders for securing compliance.

The circumstances in which a notice can be served relate not only to an existing state of affairs, but also to a likely future state of affairs – for example where an enforcing authority is of the opinion that a defendant will contravene a condition in the future not just in the present. In most, but not all, cases there is a right of appeal against the serving of an Enforcement Notice, provided for in the empowering legislation.

In the majority of cases, there is a specific criminal offence of non-compliance with a statutory Enforcement Notice (or order), punishable by a fine and/or imprisonment. There are statutory provisions for specific defences to a charge of non-compliance with a statutory Enforcement Notice. Most commonly the defences available are ‘due diligence’ defences; comprising a defence that an offender took all reasonable precautions to avoid the commission of the offence or that the offender took all reasonable steps to secure compliance (see Annex E for more details). The fact that provisions for such defences exist is perhaps a response to the potential severity of imposing criminal responsibility on those with exceptional circumstances.

4.6 The use of Enforcement Notices represents a step up in the enforcement pyramid (see annex A). From giving advice or a formal warning. Typically, it will be used where the regulatory non-compliance represents a risk of future harm, rather than giving rise in itself to significant harm or damage, or where the non-compliance is minor and does not warrant prosecution.

4.7 I commissioned Dr. Carolyn Abbot of Manchester University to examine the statutory provisions relating to Enforcement Notices across a large range of regulatory regimes falling within the scope of the review (see Annex F). Her study notes that statistics relating to the number of Enforcement Notices served under the different regulatory regimes has proven difficult to find. From the information gathered on enforcement by the HSE, it is clear that the number of Improvement and Prohibition Notices served is high when compared with the total number of prosecutions brought under health and safety law. I have identified in a previous report that the use of statutory Enforcement Notices varies across regulators. For instance, in the area of food law, local authorities issue approximately 4,500 improvement notices, while the Vehicle & Operator Services Agency issues almost 87,000 prohibition notices.

4.8 Enforcement Notices represent an important sanction option for regulators. They help regulators to ensure that businesses comply in the future rather than punishing past failures for regulatory non-compliance. Enforcement Notices give the firm an opportunity to change its behaviour rather than to passively accept to pay a fine without making any underlying change in the way the business operates to avoid future non-compliance. As such, notices are consistent with the risk-based approach to regulation, and represent a valuable and proportionate sanctioning tool for regulators.

4.9 The effectiveness of Enforcement Notices is supported by the fact that there can be serious consequences if a business does not comply with the notice. In the majority of cases, non-compliance with an Enforcement Notice is an offence in its own right, punishable by a fine and/or imprisonment. For example, in the areas of environmental and health and safety regulations, non-compliance with an Enforcement Notice is punishable by both fine and imprisonment. The regulator could decide to pursue the case and prosecute the firm for failure to comply with the notice.

4.10 Though being potentially effective in securing compliance, there are regulatory areas where it is currently not possible to use Enforcement Notices. Dr. Abbot's research has identified legislation that does not make provision for the use of statutory Enforcement Notices, for example the Clean Air Act 1993 and the Food Labelling Regulations 1996. Where this is the case, it effectively limits the enforcement toolkit to the use of informal tools such as warnings or the serious option of criminal prosecution with limited intermediate steps in the enforcement pyramid.

4.11 Dr. Abbot's research also identified some pieces of legislation that do not include their own specific Enforcement Notice powers but, rather, incorporate powers contained in other legislation. For example, the Nuclear Installations Act 1986 and the Control of Major Accident Hazards Regulations 1999, which provide for the use of enforcement notices available under the Health and Safety at Work etc. Act 1974.

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1 The Availability and use of Statutory Enforcement Notices, Abbot, C., 2006 [see Annex F].
3 Clean Air Act 1993 and the Food Labelling Regulations 1996 [SI 1996/1499].
4 Nuclear Installations Act 1986 and the Control of Major Accident Hazards Regulations 1999 [SI 1999/743].
4.12 I consider that, for the reasons identified above, the power to serve an Enforcement Notice should form an important element in any contemporary regulatory tool-kit. Enforcement Notices represent a valuable “light touch” approach to enforcement, which does not unnecessarily punish businesses that are willing to take swift action to come into compliance.

4.13 This view finds support in the responses submitted to my call for evidence. As explained in chapter two, more than half of the respondents said ‘Yes’ when asked if they felt that “the current system of Enforcement Notices requiring compliance in the future achieves its goals”. Only 11 percent of the respondents replied ‘No’.

4.14 The evidence submitted to me from both regulators and business indicated a general satisfaction with use of notices as a formal form of sanction which provides an opportunity for compliance without the need to impose a fine. The HSE, for example, notes that, “our experience is that the combination of advice and guidance, plus Enforcement Notices, is sufficient for most circumstances.” The Environment Agency has commented that they “greatly value these orders as they are aimed directly at achieving an environmental outcome by securing compliance with the conditions of the permit. They can be put in place quickly, are flexible, and if well-designed attract few appeals and secure the practical objectives.” The CBI commented that “The Enforcement Notices system works well for business because there is an emphasis on prevention of injury or harm rather than prosecution.”

Scope for strengthening the Enforcement Notices system

4.15 I believe, as do many of the stakeholders that responded that Enforcement Notices generally achieve their goal of securing future compliance. However, there is also much to indicate that the current system could be improved.

4.16 The evidence presented to me suggested that some regulators do not have a system of following up Enforcement Notices once they are served. It seems clear that the failure to follow up such notices to check that compliance has been reached undermines their value as a sanctioning tool, and will encourage those who are reluctant or unwilling to comply not to treat them seriously. Furthermore, without follow-up, regulators are not in a position to evaluate properly the effectiveness of the notice system.

4.17 For example, the Small Business Service notes in its response to the review’s call for evidence that “there appears to be a lack of follow-up action by (some) enforcers, which means that, in many cases, such notices are not taken seriously. While one option would be to link enforcement with administrative penalties, we would also like to see greater activity by enforcers in follow-up activity, either to explain exactly what such a notice requires, but also to illustrate that the Enforcement Notice is not something which should be ignored.” The Small Business Service has also suggested that there is evidence that, for small businesses, Enforcement Notices do not necessarily achieve greater compliance because there can be confusion amongst the business community as to what the notice actually represents in legal terms. Such notices may be treated no differently from an informal warning letter issued by the regulator.

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* Response submitted to the Macrory Review by the HSE, February 2005
* Response submitted to the Macrory Review by the EA, February 2005
* Response submitted to the Macrory Review by the CBI, February 2005
* Response submitted to the Macrory Review by the DTI, February 2005
4.18 I called for evidence on statistics relating to notices, and had difficulty in obtaining figures other than the number of notices issued. As noted above, the research that I commissioned also concluded that statistics relating to the number of statutory Enforcement Notices served under various statutory regimes, together with their compliance rate, was often extremely difficult to find.

4.19 While some regulators keep track of the number of Enforcement Notices issued to businesses, it is difficult to find quantitative evidence of the outcomes of such notices and we cannot say with certainty what happens once an Enforcement Notice has been issued. For example, in the areas of environmental and health and safety regulations, there is statistical data regarding the number of Enforcement Notices that are issued annually and the number of prosecutions. In 2005 the Environment Agency issued 515 Enforcement Notices and prosecuted 26 of these cases for failure to comply. HSE issued 8,445 Enforcement Notices and prosecuted 712 for failure to comply. Neither the HSE nor the Environment Agency has gathered data on the Enforcement Notices that did not lead to prosecutions. I therefore do not have accurate information on whether all of these notices were complied with or whether they were just not prosecuted for non-compliance.

<table>
<thead>
<tr>
<th>Table 4.1 Enforcement Notices and Prosecutions, 2004/2005</th>
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<tbody>
<tr>
<td><strong>Enforcement Notices</strong></td>
</tr>
<tr>
<td>Environment Agency</td>
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<tr>
<td>Health and Safety Executive</td>
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<tr>
<td>Defra</td>
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<tr>
<td>Food Standards Agency</td>
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*Source: Responses from regulators to the Penalties Review’s call for evidence, February – April 2006.*

4.20 As part of their responsibilities for accountability and transparency I believe that regulators should be able to provide more accurate information on the use and effectiveness of Enforcement Notices.

4.21 As it stands today, failure to comply with a notice is generally a strict liability criminal offence. However, as set out in chapter two of this report there is evidence that it might be more effective if failure to comply with an Enforcement Notice could also be sanctioned with a Monetary Administrative Penalty. Of the respondents to my call for evidence, only 15 percent disagreed with this approach.

4.22 A small number of regulators, for example the Pensions Regulator, currently possess powers to impose administrative penalties for failure to comply with Enforcement Notices. I suggest that if regulators were to be given powers to impose administrative penalties with appropriate rights of appeal, an administrative penalty might well be an appropriate sanction for non-compliance with the terms of an Enforcement Notice in appropriate circumstances.

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9 The Food Standards Agency figures cover the number of establishments in England subject to an Improvement Notice in 2004/05.
10 Figures for the Environment Agency and Defra are from 2005. Figures for Health and Safety Executive and the Food Standards Agency are from 2004/05.
I would, however, suggest that it would still remain within the discretion of the regulator to bring a criminal prosecution for breach of a notice which might be suitable, say, in cases of persistent breaches or where there was evidence of intentional or reckless flouting of the obligation to comply.

The Pensions Act 2004 empowers the Pensions Regulator to serve a number of statutory Enforcement Notices. Failure to comply with, for example, an improvement notice or a freezing order is an offence, and section ten of the Pensions Act 1995 (civil penalties) applies to any trustee or manager who has failed to take all reasonable steps to secure compliance. Under section ten an individual can be fined up to £5,000 and in any other case, the maximum fine is £50,000.

Under the Railways Act 1993 section 55 the appropriate authority can make various orders for securing compliance. Under section 57A of the Act, if the appropriate authority is satisfied that a relevant operator has contravened or is contravening such an order, the authority may impose on the relevant operator, a penalty of such amount as is reasonable. No maximum penalty is specified in the legislation, although section 57A goes on to say that the amount imposed may not exceed ten percent of the relevant turnover.

Source: TheAvailability and Use of Statutory Enforcement Notices, Abbot, Carolyn, (Annex F)

4.23 The current use of Enforcement Notices can also lead to some confusion concerning the legal status of Enforcement Notices. The Small Business Service notes in its response to my call for evidence that Enforcement Notices can lead to confusion amongst businesses as to what the notice actually represents in legal terms. Enforcement Notices may be treated no differently from an informal warning letter issued by the regulator.11

4.24 Regulators could ensure that businesses were aware of their legal obligations if these notices were followed up. This follow-up would add credibility to the power of the notice and could be done on a risk adjusted basis.

Summary – strengthened enforcement notice system

4.25 To summarise, the evidence suggests that Enforcement Notices are generally effective, but also that there is scope for strengthening the current system. The box below summarises my proposed key elements for the Enforcement Notices system.

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11 Response by legal advisors in DTI to the Macrory Review, February 2006
CHAPTER FOUR: STATUTORY NOTICES

Box 4.4 Proposed elements in a strengthened Enforcement Notice system

- Enforcement Notices should be available as a tool to secure future compliance in all relevant areas of regulation.

- There is a need for follow up mechanism to Enforcement Notices. This can be done on a risk adjusted basis.

- Regulators should be able to provide accurate data on the use and effectiveness of Enforcement Notices.

- The legal status of Enforcement Notices should be clarified by the regulator issuing the notice to avoid confusion.

- Regulators should have more sanction options when pursuing non-compliance with Enforcement Notices, including the option of applying a Monetary Administrative Penalty.

- It is at the discretion of the regulator when to apply a Monetary Administrative Penalty and when to opt for prosecution in order to sanction non-compliance with Enforcement Notices. This must be consistent with the regulatory enforcement policy, the Hampton Principles and the Penalties Principles.

Enforceable Undertakings

4.26 I have considered if it would be relevant to introduce Enforceable Undertakings to UK regulators as an additional sanction that could be used further up the enforcement pyramid. Enforceable Undertakings are similar to Enforcement Notices in that they are alternatives to paying a fine for regulatory non-compliance. But unlike Enforcement Notices, they are relevant for serious offences and can potentially impose a significant financial or reputational cost on the non-compliant business. Enforceable Undertakings can include a restorative element and can be used as an alternative to prosecuting a business for failure to comply with regulatory requirements.

4.27 I have investigated the role of Enforceable Undertakings in the Australian context as they have been widely taken up across Australian regulators as a sanctioning tool. Enforceable Undertakings are legally binding agreements between the regulator and the offender, which require the offender to undertake specific actions related to the non-compliance. Failure to comply with an Enforceable Undertaking is an offence, which can be prosecuted by the criminal courts.

4.28 Enforceable Undertakings typically include provisions for compensation, reimbursement or redress to affected parties, and typically also include an element to insure that an offence will not be repeated. Enforceable Undertakings may also include requirements that the offender does a service to the community, such as funding or implementing a compliance education program.
In 2005, Sken Pty. Ltd. misled consumers in an advertisement which did not fully explain the costs of purchasing a motor vehicle. The company undertook to publish a corrective notice which invited customers to call the company to discuss the matter. The company was also required to disclose any extra fees that were not included in the price of the motor vehicle advertised for sale.

In 1999 to 2004, a manager of Mr Yummy and International Catering Pty. Ltd. was accused of attempting to fix prices with competing vendors on ice cream products. The offenders accepted an undertaking that required them to publish a statement of the accusations from the ACCC, and an agreement that the company would not contravene the Trade Practices Act 1974 in the future.

In 2000, National Mutual Health Insurance Pty. Ltd. (NMHI) misled the general public in two television advertisements in a newspaper stating the errors it had made and advertisements for their HBA insurance. The undertakings required the NMHI to permanently refrain from broadcasting the advertisements, publicise information to the general public explaining their insurance policy, and to refund persons who took out the insurance during the periods when the advertisements were shown.

Source: Australian Competition and Consumer Commission, 2005.

Enforceable Undertakings are a recent innovation in Australian regulators’ enforcement toolkit. They were first introduced in 1993 by the Australian Consumer and Competition Commission but are now also used by various other regulators, including WorkSafe in Western Australia, the Australian Securities and Investment Commission and the New South Wales Department of Fair Trading.

Effectiveness of Enforceable Undertakings

In Australia, Enforceable Undertakings have proven to be an effective alternative to criminal prosecution or other types of sanctions. Enforceable Undertakings enable regulators to tailor their enforcement response to individual circumstances and to take industry considerations and resources into account. As noted in a study by Parker (2004), Enforceable Undertakings represent a valuable restorative justice alternative to traditional regulatory enforcement action because they can facilitate the agreement of all parties involved in the wrongdoing to correcting and preventing breaches and their underlying causes.12

For these reasons, Enforceable Undertakings have been popular with both regulators and industry. The Australian Law Reform Commission found in its review of undertakings that they provide a quicker and more cost-effective mechanism for resolution of regulatory non-compliance. Consultation responses from businesses to the same review observed that undertakings are a “nice way” of warning and giving the regulated business “another chance”. Businesses also stated that Enforceable Undertakings can encourage greater candour and promote compliance.13

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13 Principled Regulation: Federal Civil and Administrative Penalties in Australia, Australian Law Reform Commission, 2002
In the area of health and safety, Enforceable Undertakings have also proven popular with businesses. In Queensland, businesses can apply to the regulator to be considered for an EU. The Department of Industrial Relations has received 250 applications from organisations wanting to enter into an Enforceable Undertaking. The Regulator accepted 60 of these applications. When an application for Enforceable Undertakings is not accepted, the regulator usually proceeds with prosecution.\textsuperscript{14}

The Australian Law Reform Commission 2002 concluded in its assessment of Enforceable Undertakings that undertakings constitute a valuable alternative to court action, since they enable regulators to secure timely and cost-effective outcomes that would not be achievable by court order.\textsuperscript{15}

The Australian Competition and Consumer Commission (ACCC) was the first regulator to use Enforceable Undertakings as an enforcement strategy. Enforceable Undertakings are now used extensively by the ACCC and are generally considered to be the most successful innovation in its enforcement powers over the past years. Between 1997 and 2002 they ACCC entered into 340 Enforceable Undertakings, which is equivalent to 37 percent of all matters in which it took enforcement action.

Frequently the ACCC accepts Enforceable Undertakings from companies after beginning an investigation of a potential regulatory non-compliance and as a settlement of potential or actual enforcement litigation. The ACCC will only accept an undertaking if there is evidence of a regulatory non-compliance that would otherwise justify litigation.

The factors that the commission considers in deciding whether to accept an undertaking rather than take action in court include whether the conduct should attract penalties, whether the alleged offender’s record suggests that an administrative settlement will be sufficient to deter it from future conduct, and whether there needs to be clarification of the law by the courts to better inform the community at large.

\textbf{Box 4.6 Enforceable Undertakings – Competition and Consumer Commission, Australia}

The Australian Competition and Consumer Commission (ACCC) was the first regulator to use Enforceable Undertakings as an enforcement strategy.

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The factors that the commission considers in deciding whether to accept an undertaking rather than take action in court include whether the conduct should attract penalties, whether the alleged offender’s record suggests that an administrative settlement will be sufficient to deter it from future conduct, and whether there needs to be clarification of the law by the courts to better inform the community at large.


**Enforceable Undertakings in the UK**

Enforceable Undertakings are a sanction that is not currently available in the UK. However, there is much to indicate that Enforceable Undertakings would be an appropriate sanction for regulators to have available as part of their enforcement toolkit. The Office of Fair Trading is the only UK regulator that I have come across with something similar to an Enforceable Undertaking in its toolkit.

The Office of Fair Trading has the power to apply for so-called Enforcement Orders to sanction non-compliance which harm the collective interests of consumers.\textsuperscript{16} Enforcement Orders are injunctions granted by the court to restrain breaches of specified law, but enforcers can accept agreed undertakings as an alternative to being taken to court. Most Enforcement Order cases are, in practice, resolved in this way without litigation.

\textsuperscript{14} Queensland Government, Department of Industrial Relations, August 15, 2005 www.dir.qld.gov.au/law/regulation/undertakings

\textsuperscript{15} Principled Regulation: Federal civil and Administrative Penalties in Australia, Australian Law Reform Commission, 2002.

\textsuperscript{16} Enforcement Orders are available under Part 8 of the Enterprise Act 2002, sections 213-223
These undertakings bear some similarities with Enforceable Undertakings and are relevant as an alternative to criminal prosecution for minor as well as major types of regulatory non-compliance. However, there are some important differences, for example Enforcement Orders are not directly enforceable as such, and do not have scope for applying a monetary penalty, reimbursement orders or community services as part of the undertaking agreed between regulator and business.

4.36 Business responses to my call for evidence strongly supported the notion that there is currently need for more flexible sanctions. Enforceable Undertakings would allow for regulators to use a more flexible and individually tailored approach, which takes business considerations into account when determining how best to deal with cases of regulatory non-compliance.

4.37 Enforceable Undertakings could be used as alternatives to financial sanctions and could be effective when a fine does not have a great deterring impact, for example if an offending business is unable to pay or if the payment would just become part of the business operating cost.

4.38 Undertakings would also introduce an element of restorative justice in the enforcement process (see the next chapter for more on Restorative Justice). They can facilitate negotiations between regulator, business and in some instances the victims of regulatory non-compliance. They represent a powerful alternative to traditional coercive, regulatory enforcement action, and have the potential of imposing sanctions which are more satisfying for both offender and the victims of non-compliance.

4.39 In addition, Enforceable Undertakings would fill a gap in the regulators’ enforcement toolkit. They represent a formal and legally binding agreement between regulator and business. They are likely to be more effective in securing future compliance than warning letters or other means of persuasion currently available to the regulator. However, similar to Enforcement Notices, for Enforceable Undertakings to be credible, they would need to be followed-up by the regulator to ensure they are being complied with.

4.40 As indicated by the example below business representatives in the UK has expressed interest for introducing Enforceable Undertakings in a UK penalties system.

“The IoD would support the use of a much more flexible suite of alternative sanctions; this would allow the courts (or regulators) to tailor the penalty much more accurately to fit the circumstances of the offence.

The IoD has had some contacts with the WorkSafe organisation in Western Australia (similar to the UK’s Health and Safety Executive), and this has thrown up some interesting points about the Australian experience with enforceable undertakings, which are used as an alternative to fines for breaches of the law not involving death or injury.

Under the Australian model, both the offender and the complainant must agree that an enforceable undertaking is the appropriate way forward. The Enforceable Undertaking might require the offending company to improve occupational safety, to publicise details of its offence (perhaps by taking out an advertisement in the local newspaper) or to carry out a project that improves occupational health and safety.” Institute of Directors (IoD)

Source: Response from the IoD to the Macrory Review, February 2006
**“Undertakings Plus”**

4.41 I consider that Enforceable Undertakings would be appropriate in the UK as an alternative to criminal prosecution or Monetary Administrative penalties. In principle, Enforceable Undertakings could be accepted for all types of regulatory offences including where the offender has financial issues, and might not be able to pay a fine. In general, it would be at the discretion of the regulator to consider if, for a particular case, an Enforceable Undertaking is appropriate or if other sanctions would be more effective in delivering the regulators’ enforcement objectives. There could also be cases when the most appropriate penalty would be an undertaking plus a fine and this could be known as an ‘Undertaking Plus’.

4.42 Both the offender and the regulator must agree to enter into an Enforceable Undertaking or Undertaking Plus. This includes determining the actions, costs and timescales for the undertaking. If the offender fails to meet the requirements of the undertaking, the offender may be required to pay an additional monetary penalty at the discretion of the regulator. Any such provision would be made clear in the legislation that would be required to set up such a scheme.

4.43 If the agreement to enter into an Enforceable Undertaking is not respected by the business, the regulator can decide whether or not to initiate prosecution against the business for the original offence. I am also seeking views on whether failure to adhere to the conditions of an Enforceable Undertaking should be a criminal offence.

**Concerns regarding Enforceable Undertakings or Undertakings Plus**

4.44 In Australia, Enforceable Undertakings have raised questions about the extent to which the regulator is accountable for the exercise of its extensive powers. It has been argued that businesses might in some cases accept Enforceable Undertakings simply to avoid the more serious risk of criminal prosecution.

**Summary – Introducing Enforceable Undertakings and Undertakings Plus in the UK**

4.45 Introducing Enforceable Undertakings and Undertakings Plus in the UK implies a number of significant changes to the current system. The box below summarises the key principles for Enforceable Undertakings in the UK.
Enforceable Undertakings will be available to UK regulators as an alternative to criminal prosecution or a Monetary Administrative Penalty. It is at the discretion of the regulator to decide if particular case of non-compliance should be subject to an Enforceable Undertaking or if another sanction would be more appropriate.

An Enforceable Undertaking can be accompanied by a Monetary Administrative Penalty (“Undertaking Plus”)

The cost to the offender of complying with an Enforceable Undertaking must reflect the seriousness of an offence and where appropriate, the economic gain that the offender has made by not complying with regulations.

Enforceable Undertakings are voluntary agreements and can only be entered into in mutual agreement by the regulator and the offender.

To secure the transparency of the system, the regulator must disclose its policy on Enforceable Undertakings and Undertakings Plus, including a set of criteria for when an undertaking would be relevant and the types of conditions that may be included.

Failure to comply with an Enforceable Undertaking or Undertaking Plus could result in the regulator prosecuting the original underlying offence.

Questions for consultation

Enforcement Notices

1. Should regulators follow-up statutory notices such as Enforcement or Improvement Notices on a risk adjusted basis?
2. If a statutory notice is not complied with, should regulators be able to apply a Monetary Administrative Penalty for non-compliance with an Enforcement Notice?
3. If a regulatory appeals tribunal exists, should appeals for statutory notices be heard in this venue?

Enforceable Undertakings and Undertakings Plus

4. Do you think Enforceable Undertakings are a good alternative sanction to have available to regulators?
5. Does the described model suggest the correct key elements for introducing Enforceable Undertakings in the UK?
6. Should business be able to apply to the regulator to enter an Enforceable Undertaking or should it be solely at the discretion of the regulator to suggest an Enforceable Undertaking?
7. Should Enforceable Undertakings be disclosed publicly? Should regulators follow-up Enforceable Undertakings?

8. Would Enforceable Undertakings in principle be appropriate for all types of offences, or are they more appropriate for particular types of offences (please provide details of types of offence or specific offences)?

9. Should Enforceable Undertakings be accompanied by a Monetary Administrative Penalty in order to effectively sanction serious offences?

10. What sort of conditions on a business should an Enforceable Undertaking seek to impose?
Chapter five
Restorative Justice

The previous chapter looked at the importance of statutory notices such as Enforcement Notices and suggested some additional tools including Enforceable Undertakings and Undertakings Plus. This chapter looks at the concept of Restorative Justice and its potential role in working with corporate and individual offenders in the area of regulatory non-compliance.

Introduction

5.1 As a further alternative to criminal prosecution, administrative fines or statutory notices, as part of the regulatory sanctioning regime, I believe there is a role for Restorative Justice (RJ) in addressing regulatory non-compliance.

General concept of RJ

5.2 Restorative Justice is a philosophy that views harm and crime as violations of people and relationships. It is a holistic process that addresses the repercussions and obligations created by harm with a view to putting things right. When compared with current models of punishment, RJ requires a paradigm shift in thinking about reactions to harm. RJ is different from retributive justice. It is justice that puts energy into the future, not into what is past. It focuses on what needs to be restored or repaid and what needs to be learned and strengthened in order for the harm not to re-occur.1

5.3 The concept of RJ can be applied to many conflict situations and is not limited to regulatory non-compliance. In fact, RJ is commonly used with adult and youth offenders, in communities, schools and prisons. It can be used in both formal and informal settings.

What is Restorative Justice?

5.4 The basic principles of Restorative Justice are focused around harm and relationships. In the area of regulatory non-compliance, harms could refer to the harm caused to individuals such as injury at a workplace or a financial loss to a consumer because of mis-selling. Harms to the environment could include industrial spills or emissions into the environment. There are several definitions of RJ that I have come across although none is universally accepted. A frequently used and common definition of RJ is:

“Restorative Justice is a process whereby those most directly affected by a wrongdoing come together to determine what needs to be done to repair the harm and prevent a reoccurrence”2

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5.5 A more detailed definition suggests that ‘Restorative justice is a process whereby:

(i) All the parties with a stake in a particular offence come together to resolve collectively how to deal with the aftermath of the offence and its implications for the future.

(ii) Offenders have the opportunity to acknowledge the impact of what they have done and to make reparation, and victims have the opportunity to have their harm or loss acknowledged and amends made.  

5.6 Restorative Justice as a philosophy has several important values which are relevant to the area of regulatory non-compliance. I discuss some of these values below, but note that many of them are an essential part of the cognitive process of changing behaviour and may assist regulators in obtaining better outcomes, moving firms into compliance and ensuring that future non-compliance is minimised. I do note that RJ may only be appropriate for cases where there are victims following a regulatory offence such as cases that cause damage to property or to the environment or personal injury and even then, it may not be suitable, in every case. Therefore, it would not be appropriate for many examples of regulatory non-compliance where other sanctions may be more appropriate.

5.7 Some of the central values of RJ are outlined below:

- **Healing rather than hurting** – RJ remedies are more focused on providing ways to remedy the harm caused to the victim rather than focusing on punishing the offender.

- **Offenders taking responsibility** - Exposing the offender to the consequences of his or her behaviour is critical for the offender to gain an understanding of the impact of his or her actions. Linking actions and consequences makes it easier for the offender to develop empathy for the victim and increases the willingness to change.  

- **Victims’ Restoration** – RJ allows for all the injuries and damage a victim suffers to be acknowledged and addressed. Victims are empowered by the process as they get to speak for themselves on how they have been harmed and how they think this can be remedied. Victim satisfaction as a result of RJ is greatly enhanced when compared to the criminal justice system.  

- **Community Participation** – RJ emphasises the role of the community and of social networks as part of delivering justice. A company that cares about its reputation may feel a greater responsibility for its actions, and being vilified by the community may not be a desirable outcome for a firm. RJ allows for cooperative agreements to be reached between the community, the victim, and the offender. This provides a chance for the community to take strength out of dealing with the offence where otherwise it might be

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3 Restorative Justice : An overview, Marshal, T., London, 1999. The reference to “offence” is because this definition pertain to the use of RJ in a criminal context. RJ can also be used in other incidents of harm, e.g. in schools.


5 Restorative Justice and responsive regulation, Braithwaite, J., 2001

6 The Effectiveness of Restorative Practices: A meta-analysis, Latimer, J., Dowden, C., Muise, D., Canadian Department of Justice, 2005
weakened by fear and mistrust and be excluded from the process. This also ensures that companies become aware that they are not operating in a vacuum and have some responsibility towards the community of which they are a part. An example of this may be with a firm who has brought a lot of economic prosperity to a particular region but is not in compliance with its regulatory obligations. The community, while valuing the company’s presence may be hesitant to speak out against the regulatory non-compliance in fear of being criticised by other members of the community or political establishment. RJ would provide a good mechanism for this type of involvement.

The RJ process

5.8 RJ works on the premise that the offender accepts some responsibility for the harm caused. If the offender denies any wrongdoing, then an RJ procedure is inappropriate and other action would be required if this is in the public interest. However, if the offender admits to the wrong doing, then an RJ process is possible.

5.9 RJ works with a set of stakeholders primarily consisting of victim(s), offender(s), and affected persons such as the families of the victim(s) and offender(s) and the wider community. The stakeholders affected by the crime in turn can determine what is to be restored. In the context of regulatory non-compliance stakeholders could include the victims of mis-sold cars in the area of trading standards, or injured workers. Offenders can include the car salesperson who mis-sold the cars or the management of the firm where the accident that caused the injury took place.

5.10 These stakeholders are brought together usually for a conference or a series of meetings with external facilitation whereby they have an opportunity to discuss the harm and what needs to be done to put the harm right. Experience in other jurisdictions has shown that RJ conferences or procedures are reliant on respectful dialogue. This requires the presence of a trained facilitator who can help create a safe and comfortable environment for all parties.

5.11 The facilitator explains the process and rules, provide both parties an opportunity to speak openly about the harm and its consequences, provide both parties the opportunity to receive answers to questions and follow up on insights as to how best the harm can be addressed or remedied. Facilitators can be from a wide variety of backgrounds and are usually independently trained individuals that do not have any vested interests in the particular case.

5.12 The outcome of a restorative process will depend on the individual case. Restoration may involve some financial compensation for injuries or property loss or damage. However, RJ processes could also provide other less tangible outcomes such as restoring a sense of security, or restoring a sense of empowerment. In the area of regulatory non-compliance, vulnerable consumers who have been taken advantage of may have lost their confidence in the market place. Through an RJ process, this vulnerability could be dissipated and their confidence could be restored.
CHAPTER FIVE: RESTORATIVE JUSTICE

5.13 Effective Restorative Justice practices foster awareness of how others have been affected by inappropriate behaviour. They can personalise the consequences of the behaviour for offenders and victims. Personalising the issue for both parties, while a difficult process, can also lead to better outcomes.

5.14 The RJ process usually concludes with a plan of action agreed upon and signed by the offender and usually by the victim and, in the case of regulatory non-compliance, the regulator responsible for the case. Because of the personalised nature of the RJ process, it can have a number of positive effects such as offenders taking responsibility for their actions, experiencing remorse and offering practical help and an apology to the victim to right the wrong.\(^7\)

International Practice with RJ in the area of regulatory non-compliance

5.15 This section looks at some examples of how regulatory justice has been used in addressing regulatory non-compliance. The examples set out below indicate how RJ can be utilised in a corporate setting and are meant to provide the reader with an idea of what sorts of outcomes can be realised through such a process. The material draws upon the work on RJ that has taken place in Australia.

Box 5.1 Case study: Mis-selling insurance to Aborigines

In the mid 1980s and early 1990s a number of insurance companies were implicated in systematically defrauding consumers through misrepresentations about policies. In some cases these policies were worthless – it was impossible to claim benefits from them. The mis-selling occurred in 22 remote Aboriginal communities. The economically deprived and sometimes illiterate citizens of these communities were sold policies under false premises and charged directly from their state income support payments. This misconduct is described by John Braithwaite as “one of the most serious and widespread consumer protection frauds ever to come before the agency (Trade Practices Commission)”.\(^8\)

Despite the seriousness of the misconduct the Trade Practices Commission did not proceed straight to the apex of the enforcement pyramid to prosecution proceedings and instead attempted to remedy the situation through Restorative Justice.

This strategy was successful from the first insurance company targeted (Colonial Mutual Life) onwards. Top level managers from CML visited these communities to attend Restorative Justice conferences with the victims, the regulator, and the Department of Social Security. Through co-operating in this process most of these managers returned to their city headquarters deeply ashamed of the conduct of their company. A settlement was reached between CML, the victims, and the regulator whereby the firm agreed to:

- compensate policyholders;
- fund an Aboriginal Consumer Education Fund to ‘harden targets’ for future attempts to defraud illiterate people;

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\(^8\) Braithwaite was a commissioner of the Trade Practices Commission (the regulator that dealt with the case) at the time.
• conduct an internal investigation into the company’s compliance programme;
• identify officers responsible for the crimes, and taking disciplinary action where appropriate (80 employees were dismissed, including some senior managers); and
• introduce new compliance policies.

The broad participation in the Restorative Justice process allowed broader solutions to be reached than might have been possible through a criminal prosecution:

• The participation of the Department of Social Security resulted in reforms to the procedures relating to welfare payments;
• The participation of the regulator and Government resulted in regulatory and self-regulatory reforms concerning the licensing of agents, and changes to the law.

Braithwaite concluded that if a strategy of criminal prosecution had been pursued in this instance, some of these outcomes would probably not have been achieved. He contends that the company would probably have been fined a fraction of what it actually paid out, and there would have been a handful of follow-up claims by victims. Instead, the involvement and engagement of the community who had local knowledge and awareness uncovered and addressed an industry-wide pattern of mal-practice.


In 1988 the Australian federal government took over the regulation of nursing homes from the states. This signalled a change in strategy away from setting standards and criminally prosecuting infringements and towards a responsive – more informal – Restorative Justice approach.

After 1988, criminal prosecution for unacceptable nursing home management became extremely rare, reserved for only the most serious cases (normally where multiple deaths from abuse or neglect occurred). The new federal regime abolished the prescriptive rule-book regulations, in favour of thirty one ‘outcome standards’. These were drafted in a consultative process between industry, consumer groups, unions, and elderly care pressure groups.

This simplified regulatory structure allowed the inspectors to take a much more resident focused and outcome focused approach. Inspection involved more time spent talking with residents and staff about how the quality of care could be improved. Ultimately, nursing homes’ performance against the standards would be discussed at a conference of the inspection team and management to which representatives of owners, staff, residents, and relatives were all invited.

An evaluation of this new regime showed that the quality of life of Australian nursing home residents (calculated through a variety of measures) increased significantly since its inception. Action plans drawn up at the end point of inspection conferences were almost always implemented.

Source: Reintegrative Shaming and Regulatory Compliance, Makkai, T. and Braithwaite, J., Criminology 32: 361 – 385, 1994
Benefits of RJ for regulatory non-compliance

5.16 RJ is an alternative approach and style to that traditionally seen in the criminal justice system. For both victims and offenders, advocates of the RJ approach suggest that it achieves good outcomes in the longer term. Victims have greater satisfaction through the RJ process, and many studies suggest that the re-offending rate of offenders is lower if they have undergone an RJ process. In the field of regulatory non-compliance, firms may not have the same awareness of the harm caused by their failure to comply when working within the traditional criminal justice system, as the criminal justice system keeps the parties apart and is more adversarial in its style.

5.17 An RJ process is also flexible, as there is no pre-conceived notion of what ‘restoration’ is and as such, it is a dynamic process reflecting the needs and capabilities of the stakeholders involved.

5.18 A restorative style approach will have a slightly different focus than the criminal justice system, which is more concerned with fault and punishment. In contrast, RJ is focused on the harm caused and on what can be done to make things right.

The use of RJ in the UK

5.19 I understand that the Government is committed to promote the use of Restorative Justice. The Home Office is leading the work on using RJ and the current position is to encourage, without requiring, its further use in the adult criminal justice system particularly as a service to victims.

5.20 A research programme has been funded under the Crime Reduction Programme to build the evidence base on the input of Restorative Justice on re-offending. Funding was provided for three separate RJ schemes operating from mid-2001 for between two and three years. These schemes dealt mainly with adult offenders and worked at different stages of the Criminal Justice System, including pre-sentence and pre-release from prison. A total of 524 cases reached RJ events across the three schemes during the period of funding. The research will result in four reports analysing different aspects of the findings, summarised below:

- Implementing RJ schemes - focusing on the process of development and setting up RJ schemes.
- RJ in practice - focusing on the process of RJ up to the end of the RJ event. This deals with the extent of participation and what happened in the RJ events.
- Victim Satisfaction – will focus upon the experience of the victim in RJ events, analysing how satisfied they were and why. This should be available in summer 2006.
- Effects on offender – will analyse the effects of RJ events on offenders including the levels of re-offending. This should be available in spring 2007.

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Better outcomes

RJ is a flexible response

RJ is focused on restoring the harm

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*The Effectiveness of Restorative Practices: A meta-analysis, Latimer, J., Dowden, C., Muise, D., Canadian Department of Justice, 2005; The positive effect of Restorative Justice on Re-offending, Restorative Justice Consortium, January 2006*


Restorative Justice in Practice – findings of the evaluation of three schemes, Home Office, 2006.*
5.21 In December 2004, best practice guidance was published to promote consistency and quality of delivery of restorative processes. This has formed the basis for the development of national Occupational Standards which should be issued later this year.14

5.22 This training and accreditation framework will help to safeguard victims and offenders involved in the RJ process. I believe that Government initiatives on RJ could be extended into the area of regulatory non-compliance. The framework for training and accreditation could be built on and extended into this area.

My options for consultation

5.23 I would like to see a greater role for RJ within the area of regulatory non-compliance where appropriate. I believe that my recommendations would be building on the work done already by Government departments in this field.

5.24 I suggest that RJ become a viable option for appropriate regulatory cases within the regulatory sanctioning system. This could result in increased satisfaction for all stakeholders including victims, communities and offenders.

5.25 RJ is a voluntary process and no stakeholder should feel compelled to participate. In these instances, stakeholders should always have recourse to the criminal justice system or another sanction from within the regulatory toolkit. I think RJ could be offered as an option to stakeholders if prosecution or another formal sanction such as a Fixed or Variable MAP is not in the public interest.

5.26 In my opinion, the regulator would have a differing role depending on when an RJ process was initiated. I discuss these roles in the relevant sections below.

Option # 1 – RJ as a pre-court diversion

5.27 Firstly, when a regulator has gathered its evidence and makes a decision whether or not to proceed to a prosecution, I believe that it should consider suggesting an RJ process if appropriate. If the stakeholders agree to this process, then the regulator can defer criminal proceedings in lieu of the RJ process.

5.28 This option would mean that no formal prosecution was initiated. The offender and victim would have the opportunity to engage in an RJ process and agree upon an outcome. If this process was not followed through, or if there was a breakdown in the RJ process, then the regulator could initiate the prosecution as originally intended, if it was still in the public interest.

5.29 In this instance, the regulator would be present during the RJ process to ensure that the regulatory non-compliance was addressed and that it was content that the outcomes of the RJ process were adequate and that no further sanction was required. The regulator may also have a role in ensuring that agreed upon actions are followed through by the offender.

14 Restorative Justice Guidance: Best practice for practitioners, their case supervisors, and line managers, Home Office, December 2004
Option # 2 – RJ instead of a Monetary Administrative Penalty

5.30 When a regulator has gathered its evidence and makes a decision to apply a MAP, I believe the regulator should consider suggesting an RJ process as an alternative if appropriate. If the stakeholders agree to this process, then the regulator can defer the imposition of a MAP in lieu of an RJ process.

5.31 As per Option # 1 above, the regulator could apply the MAP as originally intended, if the RJ process is unsuccessful.

Option # 3 – RJ within the criminal justice system

5.32 Where a regulator pursues a criminal prosecution, magistrates or crown court judges could also recommend an RJ process at various stages during the criminal proceedings as outlined below:

- Pre-sentencing – the judge could suggest that the parties should meet for RJ proceedings in advance of any sentencing. The outcomes of this process could then be taken into consideration when sentencing does happen and may result in a reduced or deferred sentence. Under the existing provision for defining sentences, the courts might want a restorative process to take place and they would then receive a report of the outcome. The court has no direct involvement with the process or management of the outcome.

- As a sentence option – the judge could include RJ proceedings as something that could be entered into as part of the sentence, but this would require evidence that a restorative justice process was appropriate and the parties were willing to participate.

Restorative Justice is already part of the UK system

5.33 Whilst the introduction of RJ into the area of regulatory non-compliance would be a new initiative, the UK has been working with the concepts of RJ in many other areas. I believe that a lot of this good practice can be shared across from the area of individual offenders and applied to corporate offenders with benefits for all of the relevant stakeholders.

5.34 There are many examples of how RJ is working within the UK context. The most recent of these initiatives is conditional cautions which I discuss in Box 5.3 below.
A caution can be issued by an enforcer where there is sufficient evidence for a conviction and it is not considered in the public interest to commence criminal proceedings. To be given a caution, an offender must admit guilt. The Criminal Justice Act 2003 expanded upon this concept by introducing the ‘Conditional Caution’.

This conditional caution is a caution which has conditions attached to it with which the offender must comply. The conditions that can be attached to a caution could include anything that assist in fulfilling the objectives of:

- facilitating the rehabilitation of the offender; and
- ensuring that he or she makes reparation for the offence.

Failure to comply with the conditions may lead to prosecution for the original offence. The implication of this is that Conditional Cautions are only appropriate for cases where there is sufficient evidence to successfully prosecute an offender if the conditions are not complied with.

It is possible for RJ processes to be utilised to generate the conditions for the caution. Equally, taking part in an RJ process might be one of the conditions the offender has to fulfil. Thames Valley Police has pioneered the use of Restorative Justice as the preferred means of delivering cautions to adult offenders in its jurisdiction. Initial evaluation of this initiative showed positive results. Most cautions led to apologies that were usually seen as genuine expressions of remorse. In addition, formal reparation agreements were drawn up in approximately one third of cases where cautions were given. Most participants believed that restorative conditions attached to cautions helped offenders understand the effects of the offence and experience a degree of shame. It can enable offenders to accept responsibility for their actions, express remorse and provide an apology for the victim.

Source: Proceed with Caution: An Evaluation of the Thames Valley Police Initiative in Restorative Cautioning, Hoyle, C., Young, R. and Hill, R., 2002

5.35 Applying a tool similar to conditional cautions in the area of regulatory non-compliance could deliver many benefits for victims, offenders, and communities including improved regulatory compliance.

5.36 I have not come across any evidence of the use of conditional cautions in current business regulation practice in the UK. However, some regulators have expressed an interest in the sanction, and explain that they would make use of such a power if its applicability were extended to cover corporate offenders as opposed to being limited to individuals. The HSE has expressed the view in response to the call for evidence that conditional cautions could be a good tool to deal with offenders that have ‘good records’ and where conventional prosecution may well serve to discourage and not encourage health and safety improvement and performance.

5.37 Similar to Enforcement Notices, and Enforceable Undertakings (see chapter four), Conditional Cautions are unlikely to be effective unless they are followed up on a risk adjusted basis.

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5.35 Restorative Justice: Helping to meet local needs, Office for Criminal Justice Reform, March 2005.

5.36 Response from HSE to the Macrory Review, February 2006.
Concerns around Restorative Justice

5.38 RJ has been criticised as a ‘soft option’ and an inappropriate response to criminal actions. Those who criticise RJ in this way point to the need for deterrence and accountability especially where physical harm has resulted. However, in the context of adult offenders, some evidence would suggest that it is often harder for an offender to confront a victim than to go before a court and accept a punishment. The emotional and psychological burden of a restorative process on both offenders and victims can indicate to judges that the willingness of the offender to participate is in itself an act of remorse.

5.39 A further criticism of RJ is that it leads to ‘softer’ sentencing decisions and therefore can be a ticket to lesser penalties or sentences. These concerns are addressed by the offenders’ accountability to the community as well as the victim. Where the court deters sentencing for a Restorative Justice process to take place it will receive a report on the outcome of the process but if the offender fails to cooperate he or she can be brought back before the court and his or her failure to comply may be taken into account in the final sentence.

5.40 The settlements of cases through an RJ process can offer outcomes more appropriate than those that the criminal justice system may have delivered. Companies, in countries which operate an RJ system, have agreed to outcomes through RJ, which have addressed directly the needs and wishes of the victims of their wrong-doing. Furthermore the practice of executives being forced to acknowledge responsibility for serious consequences seems to be a potent driver of culture change in organisations. This is especially important in the area of regulatory non-compliance where changing corporate behaviour can deliver better outcomes and improved compliance. This is evident in the box on the experience of the insurance industry in Australia.

Questions for consultation

1. Do you agree that Restorative Justice is something that can be applied to the area of regulatory non-compliance? Please elaborate on your views.

2. For what types of offences would it be appropriate?

3. Do you agree with Option #1 (paragraphs 5.27 – 5.29) of RJ as a pre-court diversion? If you disagree, please elaborate on your views.

4. In what cases or for what offences would the use of RJ as a pre-court diversion be appropriate?

5. Should RJ be an alternative to administrative penalties as set out in Option #2 (paragraph 5.30 – 5.31)? In what cases or for what offences would it be appropriate?

6. Do you agree with Option #3 (paragraph 5.32) of RJ having a role within the criminal justice system when dealing with regulatory non-compliance? Please elaborate on your views.
   a. Could it be used at the pre-sentence stage?
   b. Could judges include an RJ element as part of a sentence?

Restorative Justice: A Judicial Perspective, An address to the SACRO Annual Conference February 2005, Carruthers, Judge D.
7. In what cases or what types of offences would the use of RJ as part of a criminal proceeding be appropriate?

8. Should regulators undertake pilots to explore the potential of Restorative Justice to improve outcomes for victims, offenders, and communities in business regulation?

9. Who should contribute to the cost of the RJ process?

10. What safeguards are necessary in the RJ process?

11. Does Restorative Justice have a role to play in remedying regulatory breaches where no identifiable individual victim(s) exists such as in cases of environmental damage?

12. RJ is a voluntary process, so should it ever be suggested by a judge or a regulator as an alternative to a more formal sanction?

13. Will corporate or business offenders be under pressure to accept an offer to enter into an RJ process because it is seen as a lesser or softer alternative?

14. What should happen if a company does not adhere to the agreed upon outcomes of an RJ process?
Chapter six
Alternative penalties in the Criminal Courts

The previous chapter looked at the role of Restorative Justice in addressing regulatory non-compliance. This chapter looks at expanding the sanctioning options available to the judiciary in cases of criminal prosecution.

Introduction

6.1 I have been investigating the area of regulatory non-compliance for several months. As discussed in previous chapters, many cases of non-compliance are sanctioned by way of criminal prosecutions. Evidence submitted to me suggests that the usual sentence resulting from criminal proceedings in cases of regulatory non-compliance, in the vast majority of cases, are fines or – very rarely – imprisonment.

6.2 After extensive investigation, I contend that imposing financial penalties alone may not always be the most effective way in which to change undesirable business behaviour. Relying on financial penalties in isolation may not properly reflect other regulatory objectives, such as restoring the harm caused to victims or improving a firm’s future capacity to comply with its regulatory obligations.

6.3 As discussed in the previous two chapters, financial penalties may not be able to influence a change in behaviour, or be appropriate to the nature of the offence or the offender. I have identified for cases that are not pursued in the criminal courts, a range of sanctioning options such as Enforcement Notices, Enforceable Undertakings or Restorative Justice that could be more suitable in certain instances. Extending the option of non-financial sanctions available in criminal proceedings is another area of reform that I would like to consult upon. I believe that judges should have access to a more complete and diverse set of sanctioning tools that can look beyond punishment through financial sanction and address the potential for securing future compliance and addressing the harm caused to victims.

6.4 In recent years, the criminal justice system in England and Wales has seen many innovations in sentencing options for individual offenders beyond the plain vanilla options of financial penalties or imprisonment. This innovation is evident in the range of community sentencing options made available to judges by the Criminal Justice Act 2003. Amongst these options are ‘Unpaid work requirements’, ‘Curfew requirements’, Supervision requirements, and ‘Alcohol treatment requirements’. In addition, this act also makes provision for enforcers to use ‘Conditional Cautions’ (as discussed in Box 5.3). I believe that similar innovation would be beneficial in the area of regulatory non-compliance.

6.5 I am concerned that some of the evidence submitted to me suggests that there are options for sanctions beyond just financial penalties or imprisonment in addressing regulatory non-compliance, but these are not often used by the judiciary for a variety of reasons. I want to investigate this issue further in the next phase of my review.

\[1\] As defined in Section 199, 204, 213 and 212 of the Criminal Justice Act 2005.
Current sentencing practice

6.6 I have received evidence on the current availability of sentencing options, and of judicial practice in using these options. This has shown that the sentences imposed against corporations for regulatory non-compliance in 2004 consisted of 96 percent financial penalties, with the remaining four percent given absolute or conditional discharges, or otherwise dealt with. This contrasts with the way that the courts sentence individual offenders. In these cases non-financial sentences make up 27 percent of the total sentences handed down of which 13 percent are community sentences. This 13 percent includes:

- three percent Community Punishment Orders
- four percent Community Rehabilitation Orders
- four percent Immediate Custody
- two percent Reparation Orders

Box 6.1 Sentencing options for individual offenders

Besides fines and custodial sentences the main sentencing option available to criminal judges is the Community Order, introduced by the Criminal Justice Act 2003 for individual offenders. This flexible community sentence combines punishment with changing offenders’ behaviour and making amends. It can also encourage the offender to deal with any problems that might be making them commit crime. A court can impose one or more of the following requirements, subject to the specific provisions set out in the legislation in relation to each, for a period not exceeding three years.³

- **Unpaid work requirement** – The offender must work a number of hours without pay.
- **Activity requirement** – The offender must participate in a certain activity for a certain number of days to help tackle his or her offending, or make amends for the offending.
- **Programme requirement** – The offender must undertake an accredited programme aiming to tackle his or her offending behaviour.
- **Prohibited activity requirement** – The offender must refrain from certain activities, such as attending football matches, during a set period specified in the order.
- **Curfew requirement** – The offender must remain at a particular place at certain times (normally his or her home overnight).
- **Exclusion requirement** – The offender cannot go to certain places on certain days, and at certain times.
- **Residence requirement** – The offender must reside at a certain place.

³ Restorative Justice: Helping to meet local needs, Office for Criminal Justice Reform, March 2005.

³ As defined in Section 199, 204, 213 and 212 of the Criminal Justice Act 2005.
CHAPTER SIX: ALTERNATIVE PENALTIES IN THE CRIMINAL COURTS

- **Mental health treatment requirement** – The offender agrees to a period of treatment to deal with problems that lead them to offend.

- **Drug rehabilitation requirement** – The offender agrees to a period of treatment to reduce, or eliminate, the offender’s drug problem.

- **Alcohol treatment requirement** – The offender agrees to a period of treatment to reduce, or eliminate, the offender’s alcohol problem.

- **Supervision requirement** – The offender must meet regularly with a probation officer aiming to promote rehabilitation.

- **Attendance centre requirement** – The offender must attend at an attendance centre for a number of hours.

The community order in the Criminal Justice Act 2003 has replaced other community sentences; it is available for all offences committed from 4 April 2005 (when the relevant legislative provisions came into force), where the offence is serious enough to warrant such a sentence. The new order allows courts to design a community sentence suitable for the specific circumstances of each individual offence and offender.

Source: Home Office 2006

6.8 The chart opposite indicates the range of sentencing practice across five different regulatory areas. This data captures the sentencing of both individuals and businesses.

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4 This requirement is only available in cases where the offender is under the age of 25.

5 The exception to this is that, where the provisions apply to a person aged 16 or 17 convicted of an offence, sections 177 and 179 to 180 of and Schedules 8 and 9 to the 2003 Act (community orders) shall come into force on 4th April 2007.
6.9 I have heard evidence that there is a lack of consistency in the underlying legislation when addressing regulatory non-compliance with some regulatory areas having access to a wider variety of sanctions than others. Ultimately this is a policy decision for departments and regulators, but given that less than one percent of cases heard in criminal courts are related to regulatory non-compliance, I want to explore the possibility that the judiciary may not be made aware on every occasion of what options are available to them for sanctioning purposes. This is an area that I would like to hear more evidence on going forward and I would invite responses dealing specifically with this point.

6.0.73% of cases is from the DCA and is relevant only for businesses prosecuted for regulatory non-compliance. Equivalent figures are not available for individuals prosecuted for regulatory non-compliance.
6.10 For instance, compensation orders are available to judges for the sanctioning of all cases where there is an identifiable victim. In 2004, 72 compensation orders were handed down to corporations in Magistrates courts out of a total of 10,457 convictions in England and Wales, in contrast 10,057 financial penalties were handed down in the same period.7

6.11 There are a number of reasons why I think that use of sentencing options other than fines is limited. I hypothesise that there may be constraints within the underlying legislation itself. For example, in the area of Pesticides Safety, I have been made aware that uncertainties, gaps and omissions in the law stop enforcers from using a number of enforcement tools that are seen as potentially useful. As a result, the regulator is unable to use on-the-spot fines. I would like to be made aware of other legislative inconsistencies in areas of regulation and what if any steps have been taken to remedy inconsistencies or any steps that could be taken, in order to identify whether amendment to the legislative provisions is desirable or appropriate in order to make these options more usable.

Potential options to expand the toolkit available to the judiciary

6.12 Whilst I receive evidence on the reasons behind the lack of utilisation of the alternative current sanctions available, I would also like readers to consider if further alternative sanctions should be made available to the judiciary, such as those described later in the chapter. Of course, it goes without saying that having more sanctions in the toolkit if they are not going to be used is a wasted effort. However, I believe that there should be enough flexibility and availability of a range of options to be available for better meeting needs of victims and offenders in addressing regulatory non-compliance.

Extended Sanctioning options

6.13 The evidence that I have received does suggest that – whilst recognising that more sentencing options exist but are not currently being used on a widespread basis – the current range of sanctioning options available for regulatory offences is too narrow. The discussion in the following section suggests some options to extend judges’ sentencing options in a way that will allow them to deter offenders (and potential offenders), to consider the needs of victims, and to build a firms’ future capacity to comply.

“… where prosecution is the outcome, it is important that courts too have a wider range of sanctions available to them, with publicity orders and environmental service orders, outlined in the paper, well worth considering.” Justices’ Clerks’ Society

Source: Response from Justices’ Clerks’ Society to the Macrory Review, February 2006

6.14 I have already discussed Restorative Justice as an option for the judiciary to consider before or as part of sentencing in chapter five. In addition to Restorative Justice, I want to encourage new sanctions to be developed which would meet more than just the need of deterrence as the main objective of a sanction. The other objectives that I would like to see play a greater role in sentences handed down by the court are already embodied in the principles mentioned in the Criminal Justice Act 2003, such as rehabilitation and remediation.6

7 Statistics from the Home Office, 2004
6.15 I am mindful that I do not want to recommend the creation of a prescriptive list of options that would bind the judiciary, regulators and departments and which could become obsolete. Instead, I want to ensure, through my recommendations, that regulators and departments have the flexibility to evolve the sanctions available within their toolkit and legislative provisions to best reflect the prevalent regulatory style and environment in their regulatory field.

6.16 I intend to recommend the type of sanctions that the evidence and analysis suggests would be desirable in a modern regulatory sanctioning toolkit, but would expect that regulators and departments would be best placed to design their own sanctions for the judiciary to use that follow the Penalties Principles outlined in chapter one and that are appropriate for a risk-based approach to regulation.

6.17 In the discussion below, I suggest some examples of sanctions which could be introduced on a more widespread basis. Many of these are already available in some areas of regulation and I believe that sharing this best practice across regulators would be beneficial. However, this list is by no means exhaustive and there may be other options that I have not mentioned that would be appropriate and relevant for introduction. I would like to invite further suggestions.

Examples of alternative sanctions

6.18 I do not want to limit my recommendations to the introduction of these types of sanctions and invite other suggestions. The options discussed below are not exhaustive.

Corporate rehabilitation orders

6.19 This would involve provisions to enable a court to require a company to undertake specific actions or activities during a specified period (such as one or two years). The activities specified in the order could include training of personnel in regulatory related matters, the adoption and implementation of action plans to address regulatory non-compliance or taking steps to remedy the harm caused by regulatory non-compliance. The relevant regulator could monitor compliance with this order. Failure to comply with the order would lead to the company being brought back to court and sentenced in an alternative way.

6.20 This type of a sanction would seek to rehabilitate the firm and be a forward looking tool in order to improve the company’s capacity to comply in future.

Community Projects

6.21 The court would have the power to order an offender to complete a relevant community improvement project within a specified period and for a specified value related to the underlying harm or benefits that had been caused or obtained by the offender. This could be used in addition to another sanction such as a fine. This type of sanction is available in many other jurisdictions within the OECD such as in the area of environmental regulation in Australia and Canada.

6.22 A community project does not have to be limited to the area of environment but could be extended to many areas of regulation. For instance, in the area of consumer protection, a project could involve an education or training campaign.
6.23 The projects should be:

- carried out in addition to something that the company is already legally obliged to do;
- the firm should not be allowed to utilise the project for its own public relations purposes; and
- the community project could be used where the firm or individual is not in a position to pay a high financial penalty.

**Publicity Orders**

6.24 Reputation is an important asset to many businesses. A publicity order provision would enable a court, in addition to any other sentence imposed, to order that a notice (with wording agreed between the business and the regulator) be placed in an appropriate publication such as a trade publication, local or national newspaper or another media outlet such as radio or television, or in a company's annual report within a specified period.

6.25 This type of sanction would have a strong deterrent element for many businesses and may be more meaningful than a financial penalty for a firm that has access to many financial resources. My discussion explained the use in Australian regulation of 'negative publicity orders'.

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**Box 6.2 Reputation as a motivation for regulatory compliance**

The use of reputation as motivation for regulatory compliance is already in practise in some areas of UK regulation. The Food Standard Agency is piloting a scheme to obtain positive reputational benefits for strong regulatory performers, whilst the Environment Agency publishes an annual spotlight on business report highlighting good and bad regulatory performance. The Health and Safety Executive disclose details of its enforcement actions on its website which the CBI says ‘puts peer pressure on those firms that have issues to address and threatens adverse impact on their reputation’.

Lastly, when the Financial Services Authority imposes a financial penalty on an offender, it is accompanied by a press release giving details of the non-compliance and the size of penalty.

Source: Evidence submitted to the Macrory Review, spring 2006

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* Response submitted by the CBI to the Macrory Review, February 2006
Adverse publicity orders are available in Australia in the areas of environment, health and safety, Consumer Protection and Competition Law. The order involves a judge specifying that a notice – with wording agreed between the enforcement agency and the offending firm – be placed in an appropriate publication. Often the order specifies that the cost of the notice should be paid by the offending firm.

I have spoken to Australian regulators about their use of this sanction. Generally their experience was positive, and the feeling was that they were a strong deterrent to those firms that tend to act as amoral calculators. The Environment Protection Authority (EPA) in New South Wales obtained 21 orders in 2004/05. The EPA believes that publicity orders have particularly effective deterrent value for corporate offenders. A fine can be of little significance given a corporation’s revenue and it can also be passed on to consumers or subsumed as a cost of doing business. Publicity orders explain the circumstance surrounding a corporation’s offence and bring those circumstances into the public, making the offender publicly accountable.

However, Australian research suggests that negative publicity deters more through non-financial impacts than profits considerations. Seventeen case studies of the effects of negative publicity on corporations found that the financial effects were minimal. Rather, executives do not want to risk the potential impact that negative publicity would have on their ‘corporate prestige’. Senior managers placed great emphasis on the maintenance of this prestige and the risk that negative publicity created to this asset was a great motivational factor.


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### Conditional cautions for corporate offenders

6.26 Conditional cautions are being introduced in England and Wales when dealing with ‘individual’ offenders. The power to issue these is contained in Section 22 of the Criminal Justice Act 2003. I consider that extending the application of this sanction to corporate offenders may be of value where it is in the public interest for offenders to have specific conditions attached to the caution, rather than be prosecuted. The conditions must help rehabilitate the offender and/or ensure that the offender makes reparation for the consequences of the regulatory non-compliance on the victim or wider community. Offenders who fail to comply with the conditions of the caution could be prosecuted for the original offence.

6.27 This type of sanction is more focused on rehabilitation and reparation rather than punitive elements of sanctioning.

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10 This might be a local or a national newspaper, or even the trade press used by a supplier firm’s customers.

11 Kagen & Sholtz define ‘amoral calculators’ as those companies that calculate whether to comply through estimating the expected economic costs and benefits of doing so.

12 The Impact of Publicity on Corporate Offenders, Fisse & Braithwaite, 1983.
Mandatory Audits

6.27 As mentioned in my December Discussion Paper provision of the power to compel companies to undertake an ‘audit’ is common in Australian states again in the area of environmental regulation. This type of provision could be used in the case of businesses where there is a deficiency in the business management and where systemic organisational change would help better achieve future compliance. Bringing in external expertise could get the business the help it needs in identifying ways in which it could improve its operations and meet its regulatory requirements.

Questions for consultation

1. Are financial penalties or imprisonment adequate sanctions for addressing regulatory non-compliance in a criminal setting?
2. Why do judges not use other legislative provisions for alternative sentences such as compensation orders?
3. Should judges be afforded a broader range of sentencing options to deal with companies and individuals who have not met their regulatory obligations?
4. Are financial penalties alone sufficient to deter companies from not complying with regulatory obligations?
5. Should regulators and Government departments look to amend their legislative provisions to extend the sanctioning options available to judges?
6. Would the following potential extended sanctioning options be appropriate for sentencing in cases of regulatory non-compliance?
   a. Publicity orders
   b. Corporate rehabilitation orders
   c. Corporate probation orders
   d. Mandatory audits
   e. Community service orders
   f. Remediation orders
7. What sorts of offences would be appropriate for alternative sanctions?
8. What sorts of firms should be considered appropriate for alternative sanctions?
9. Do you have any suggestions for other types of sanctions that should be considered not mentioned on the above list?
10. Which offences would be appropriate for alternative Sanctions?
11. Which firms would be considered appropriate for alternative Sanctions?
12. Do you have suggestions for other types of Sanctions that should be considered, not mentioned on the above list?
13. Should judges seek to remove all of the financial benefit obtained as a result of regulatory non-compliance in their sentencing through a profits order plus a fine?

Chapter seven
Questions for consultation

This chapter sets out the questions for consultation

7.1 This document sets out suggestions for potential reforms in the area of regulatory sanctions. These areas are covered in more detail in chapters three through to seven. The review would welcome views from all stakeholders on any of the issues raised in the report. A list of questions for consultation is outlined in this chapter. Respondents should no feel bound by the list of questions – any response on any issue would be welcomed.

7.2 Consultation responses should be sent, by Friday, 18th August 2006, to:
Macrory Penalties Review
Cabinet Office – Better Regulation Executive
Kirkland House
22 Whitehall
London SW1A 2WH

7.3 The final report is expected to be published in Autumn 2006. Consultation responses received after the August deadline, may not be considered.

7.4 All information in responses, including personal information, may be subject to publication or disclosure in accordance with the access to information regimes (these are primarily the Freedom of Information Act 2000, the Data Protection Act 1998 and the Environmental Information Regulations 2004). If you want your response to remain confidential, you should explain why confidentiality is necessary and your request will be acceded to only if it is appropriate in all the circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on the Department. Contributions made to the review will be anonymised if they are quoted.

7.5 The review would like to hear from you on the following subjects:

My Vision for Contemporary Sanctioning Regimes

1. Do you agree that criminal prosecution and the criminal courts should be reserved for the truly egregious offenders or where regulatory breach leads to severe actual or potential external consequences?

2. Do you agree with the vision that is laid out in Figure 1.3 of a contemporary regulatory enforcement toolkit?

3. Do you agree or disagree with the ‘Penalties Principles’ proposed in chapter one? If you disagree with one or all of the Principles listed below, please elaborate?
   a. Principle # 1 – Sanctions should change the behaviour of the offender to prevent regulatory non-compliance.
   b. Principle # 2 – Sanctions should eliminate any financial benefit or benefit which was the result of regulatory non-compliance.
c. Principle # 3 – Sanctions should be **responsive and take into account what is appropriate for the particular offender and the particular regulatory issue.**

d. Principle # 4 – Sanctions should be **proportionate** to the nature of the offence and the harm caused

e. Principle # 5 – Sanctions should include an element of ensuring that the **harm caused by regulatory non-compliance is put right.**

f. Principle # 6 – Sanctions should aim to **deter future non-compliance.**

4. Are there any principles that should be added to this list? If yes, please provide details including supporting comments and evidence.

5. Do you agree that a regulator must ensure the following characteristics to be present in order for a sanctioning regime to be most effective?

   a. The regulator should have a published enforcement policy
   b. The regulator should attempt to measure regulatory outcomes (such as compliance rates) and as well as outputs (such as the number of enforcement actions taken).
   c. The regulator should be able to justify the enforcement actions they take
   d. The regulator should follow up enforcement actions
   e. The regulator should be transparent in the enforcement actions it takes
   f. The regulator should be transparent in the methodology it uses for setting and calculating monetary administrative penalties.

6. How should regulators be required to report their performance and progress against their enforcement strategies?

7. Should regulators make a more focused effort to communicate their strategy for targeting businesses that are deliberately non-compliant? If yes, how should they approach this?

8. What can be done to capture the rogue elements within industries?

9. Is there need for increased investigative powers to be afforded to regulators to better deal with rogue businesses?

10. Should due diligence defences be included in all areas of criminal offences involving regulatory breach?

11. Would more training be appropriate for judges in the area of regulatory non-compliance and appropriate sentencing?

12. Should sentencing guidance be prepared for areas of regulatory non-compliance?

13. Should the fine maxima in criminal courts be abolished? Should a cap be set?

14. Should the cap follow the principles laid out in the Competition Act 1998 which provides that administrative penalties may not exceed ten percent of the relevant turnover of the undertaking concerned?
15. Should profits gained from non-compliance be subject to a separate profits order which is intended to remove any economic gains from non-compliance as well as a separate fine element?

Monetary Administrative Penalties (MAPs)

16. In general, do you agree that regulators should have Monetary Administrative Penalties available to them as an additional sanction option in their enforcement toolkits? If no, then please elaborate on your views.

17. Do you prefer Model # 1 (paragraphs 3.40 – 3.44), Model # 2 (paragraphs 3.45 – 3.47) or Model # 3 (paragraphs 3.48 – 3.51). Please explain why you would prefer one particular model?

18. Should regulators have FMAPs available to them? For what types of offences (either in general or giving specific examples) would they be appropriate? What level of financial penalty would be appropriate for FMAPs?

19. Should regulators have VMAPs available to them? For what types of offences (either in general or giving specific examples) would they be appropriate?

20. Should the level of VMAPs be determined with regard to one or more of the following aggravating or mitigating factors:
   - Financial gain made by the offender
   - Offender’s past record of compliance
   - Annual turnover of the offender
   - The co-operation of the offender
   - The timely and accurate reporting of the issue
   - Timeliness of corrective action
   - Please provide other relevant factors which you feel should be included.

21. Should the level of VMAP be unlimited?

22. Should the maximum level of VMAPs set out in legislation be capped to never exceed ten percent of the relevant annual turnover as per the details of the Competition Act 1998?

23. Should there be provision to supersede the cap if the financial benefit is greater than the capped amount?

24. Should there be an option for settlement as an alternative to a MAP? In what sort of cases should this be considered?
CHAPTER SEVEN: QUESTIONS FOR CONSULTATION

Enforcement Notices

25. Should regulators follow-up statutory notices such as Enforcement or Improvement Notices on a risk-adjusted basis?

26. If a statutory notice is not complied with, should regulators be able to apply a Monetary Administrative Penalty for non-compliance with an Enforcement Notice?

27. If a regulatory appeals tribunal exists, should appeals for statutory notices be heard in this venue?

Enforceable Undertakings and Undertakings Plus

28. Do you think Enforceable Undertakings are a good alternative sanction to have available to regulators?

29. Does the described model suggest the correct key elements for introducing Enforceable Undertakings in the UK?

30. Should business be able to apply to the regulator to enter an Enforceable Undertaking or should it be solely at the discretion of the regulator to suggest an Enforceable Undertaking?

31. Should Enforceable Undertakings be disclosed publicly? Should regulators follow-up Enforceable Undertakings?

32. Would Enforceable Undertakings in principle be appropriate for all types of offences, or are they more appropriate for particular types of offences (please provide details of types of offence or specific offences)?

33. Should enforceable undertakings be accompanied by a Monetary Administrative Penalty in order to effectively sanction serious offences?

34. What sort of conditions on a business should an Enforceable Undertakings seek to impose.

Restorative Justice

35. Do you agree that Restorative Justice is something that can be applied to the area of regulatory non-compliance? Please elaborate on your views.

36. For what types of offences would it be appropriate?

37. Do you agree with Option #1 (paragraphs 5.27 – 5.29) of RJ as a pre-court diversion? If you disagree, please elaborate on your views.

38. In what cases or for what offences would the use of RJ as a pre-court diversion be appropriate?

39. Should RJ be an alternative to administrative penalties as set out in Option #2 (paragraph 5.30 - 5.31)? In what cases or for what offences would it be appropriate?

40. Do you agree with Option #3 (paragraph 5.32) of RJ having a role within the criminal justice system when dealing with regulatory non-compliance? Please elaborate on your views.
a. Could it be used at the pre-sentence stage?
b. Could judges include an RJ element as part of a sentence?

41. In what cases or what types of offences would the use of RJ as part of a criminal proceeding be appropriate?

42. Should regulators undertake pilots to explore the potential of Restorative Justice to improve outcomes for victims, offenders, and communities in business regulation?

43. Who should contribute to the cost of the RJ process?

44. What safeguards are necessary in the RJ process?

45. Does Restorative Justice have a role to play in remedying regulatory breaches where no identifiable individual victim(s) exists such as in cases of environmental damage?

46. RJ is a voluntary process, so should it ever be suggested by a judge or a regulator as an alternative to a more formal sanction?

47. Will corporate or business offenders be under pressure to accept an offer to enter into an RJ process because it is seen as a lesser or softer alternative?

48. What should happen if a company does not adhere to the agreed upon outcomes of an RJ process?

**Alternative Sentencing in Criminal Courts**

49. Are financial penalties or imprisonment adequate sanctions for addressing regulatory non-compliance in a criminal setting?

50. Why do judges not use other legislative provisions for alternative sentences such as compensation orders?

51. Should judges be afforded a broader range of sentencing options to deal with companies and individuals who have not met their regulatory obligations?

52. Are financial penalties alone sufficient to deter companies from not complying with regulatory obligations?

53. Should regulators and government departments look to amend their legislative provisions to extend the sanctioning options available to judges?

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