



OFFICE *of the*  
RAIL REGULATOR

**GUIDANCE ON INSURANCE AGAINST  
THIRD PARTY LIABILITY**

**A CONSULTATION DOCUMENT**



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## *Regulator's foreword*

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1. The licences granted to operators of trains, stations, networks and light maintenance depots require the licence holder to maintain insurance (including self-insurance) against third party liability. The licences also require that such insurance should be held on terms approved by me. This approval role conferred on me by the licences is a function that I regard as providing important protections for the public and other parties who use the railways.
2. The minimum requirements for third party liability insurance are set out in the *Guidance on Insurance Against Third Party Liability*. This has seen a number of changes since the first edition was published in 1994. As a result of the passage into the private sector of Railtrack and an increasing number of train operating companies, I believe that it is necessary to institute a more formal consultation process for dealing with proposed changes to this guidance in order to allow me to take into account the views of all interested parties before publishing the revised guidance.
3. This consultation document seeks views from industry parties, insurance brokers, insurers and others with an interest on proposed changes to the insurance guidance. One of the most important changes is the proposal to institute a formal consultation process as a regular part of an annual cycle of insurance activity. Another important issue - which was foreshadowed in the current edition of the insurance guidance - is the question of cover for activities undertaken by contractors and sub-contractors on behalf of licensed operators. Proposals are also made for a process for tackling the questions raised in respect of private freight wagons. The other changes proposed are largely clarificatory.
4. I welcome comments from anyone with an interest who feels they wish to contribute.

JOHN SWIFT QC

Rail Regulator

1996



# ***1. Introduction and summary***

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## **Introduction**

- 1.1 The period since the insurance guidance<sup>1</sup> was first published has been a time of continuous change in the railway industry. Railtrack has moved into the private sector and British Rail has been progressively split into subsidiary companies, which have themselves been transferring to the private sector through the franchising and sales process. Simultaneously, the industry has been working to develop new contracts and other bilateral and multilateral arrangements which codify and set rules for commercial activities which were previously, within a single British Rail, a matter of custom and practice. Private sector involvement has brought with it a number of new franchisees, owners, insurance brokers and insurers who are involved in the rail sector for the first time and have an interest in the Regulator's insurance requirements.
- 1.2 Until June 1996 the Insurance Working Group, which comprised rail and insurance industry representatives and was chaired by the Department of Transport, provided a forum for discussing policy and procedures relating to insurance. This group had an important role to play in establishing the new third party liability insurance regime and in acting as a focus for raising and resolving issues. It was widely recognised, however, that the Insurance Working Group would not be able to play a long-term role as increasing numbers of new players entered the railway industry.
- 1.3 With the demise of the Insurance Working Group there is currently no forum for interested parties to get together to explore insurance issues of common concern. It has become apparent that a different approach is needed if ORR is to ensure that it can take on board the concerns of the industry and other interested parties and, where necessary, revise the insurance guidance to take account of emerging issues.
- 1.4 While ORR has always been ready to discuss issues bilaterally with individual operators and insurers, and will continue to do so, this is not necessarily the most effective way of dealing with cross-industry issues. Accordingly, the Regulator has decided that the insurance guidance should be the subject of consultation, which will give all parties, including operators, insurance brokers, insurers and others with an interest, the opportunity to comment on the Regulator's proposed changes. The

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<sup>1</sup> *Guidance on insurance against third party liability*. First published April 1994. Current edition published January 1996 as Enclosure 2 in the Guidance on licensing of operators of railway assets.

objective of the consultation process is to ensure the publication of revised guidelines fit for purpose before operators start to put together their insurance programmes for 1997.

### **The consultation document**

- 1.5 Section 2 of this document describes the Regulator's role and objectives with respect to his third party liability insurance functions and sets out the relevant statutory background. These have been articulated at a number of conferences and meetings with interested parties during the past two years, but the Regulator feels that these matters should be stated in his published insurance guidance so that they are readily available to all those who are, or may become, involved with regulated insurance matters.
- 1.6 Section 3 of this document describes a number of proposed changes to the existing insurance guidance and explains the Regulator's reasons for proposing them:
- (a) an extension of the insurance requirement in respect of licensees' contractors and sub-contractors (further explored in section 4 – including the issues surrounding privately-owned coaches and wagons);
  - (b) clarification and amplification of the Regulator's current requirement that a minimum £155 million of cover be provided;
  - (c) clarification of the process for requesting approval of a different basis of cover from that stipulated in the insurance guidance;
  - (d) clarification of information requirements for applications for approval of self-insurance proposals, in particular abolition of the requirement to complete the Notification of Intention to Self-Insure Part of Third Party Liability;
  - (e) clarification of the procedures and timescales for the submission of insurance documents for the Regulator's approval and request for comments on the greater use of standard wordings and formats; and
  - (f) a proposed annual cycle of consultation with the industry on emerging issues (further examined in section 5).
- 1.7 Section 6 of this document summarises the objectives of the Claims Allocation and Handling Agreement ('CAHA'), its relationship with the Regulator's insurance

requirements and encourages industry participation in the review of these arrangements that is due to start shortly.

- 1.8 A copy of the current insurance guidance showing proposed modifications highlighted (additions in italics and deletions struck-through) is attached at Annex A.
- 1.9 This consultation document seeks written comments on the proposed changes, both in principle and on the specific drafting. Consultees are also invited to raise any further issues they believe to be of concern, together with proposed solutions where possible.

### **Next steps**

- 1.10 Following the end of the consultation period the Regulator will review the insurance guidance (also the guidance on licensing<sup>2</sup>) in the light of the comments received. He may wish to contact some consultees to clarify comments and gain further understanding of the issues raised.
- 1.11 The Regulator will aim to issue the revised version of the insurance guidance by the middle of October 1996.

### **Consultees**

- 1.12 The Regulator will send copies of the Consultation Document inviting comments to:
- (a) all holders of railway operators' licences;
  - (b) all insurance brokers acting for holders of railway operators' licences;
  - (c) all current applicants for railway operators' licences;
  - (d) the insurance brokers to the Central Insurance Facility;
  - (e) Railway Claims Ltd;
  - (f) Office of Passenger Rail Franchising;
  - (g) Association of Train Operating Companies;
  - (h) British Railways Board;
  - (i) Health & Safety Executive;

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<sup>2</sup> *Guidance of licensing of operators of railway assets*. September 1995: published in a package with enclosures, including the Guidance on insurance against third party liability.

- (j) insurance industry representative bodies (Association of British Insurers, Lloyd's Underwriters Non-Marine Association Ltd, British Insurance & Investment Brokers Association and Institute of Insurance Brokers);
- (k) all companies who have pre-qualified as bidders for passenger franchises;
- (l) other insurers or insurance brokers who have expressed an interest; and
- (m) any others who express an interest.

**Address for responses and dates**

- 1.13 Comments in response to this consultation should be sent in writing to arrive at the following address no later than 4 October 1996:

Judith Marshall-Camm  
Office of the Rail Regulator  
1 Waterhouse Square  
138-142 Holborn  
London  
EC1N 2ST

- 1.14 Unless it is clearly stated that a response has been provided on a confidential basis, it will be assumed that responses can be published or quoted publicly by the Regulator.
- 1.15 Additional copies of this document are available free of charge on request from the Office of the Rail Regulator Library. Telephone: (0171) 282 2001; Fax: (0171) 282 2045; E-mail: [orr@dial.pipex.com](mailto:orr@dial.pipex.com); or write to The Librarian at the address shown above.

## ***2. The Regulator's role and objectives in relation to insurance***

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### **The functions and duties of the Regulator**

2.1 Two of the Regulator's principal functions under the Railways Act 1993 ('the Act') are the granting of licences to operators of railway assets and the approval of track, station and light maintenance depot access agreements. The Act requires the Regulator to carry out these functions in the manner which he considers best calculated to achieve the duties set out in the Act. These include:

- (a) protecting the interests of users of railway services;
- (b) promoting the use of and development of the rail network in Great Britain;
- (c) promoting efficiency and economy on the part of persons providing railway services;
- (d) promoting competition in the provision of railway services;
- (e) promoting measures designed to facilitate the making of journeys which involve the use of the services of more than one passenger service operator;
- (f) imposing on operators the minimum restrictions which are consistent with the performance of his functions; and
- (g) enabling persons providing railway services to plan the future of their businesses with a reasonable degree of assurance.

2.2 The Regulator's duties are listed in full in Section 4 of the Act, a copy of which is attached at Annex B.

### **The Regulator's role in insurance**

2.3 The Regulator's licensing function not only includes the initial granting of licences to operators of railway assets, but also modification, investigation of alleged contraventions and enforcement, including revocation where necessary. The licences themselves also confer important functions on the Regulator.

- 2.4 All<sup>3</sup> licences granted to operators of passenger trains, non-passenger trains, stations, networks and light maintenance depots contain a condition which requires the licence holder to maintain insurance (including self-insurance) against third party liabilities. The condition requires that the terms of such insurance, including type, cover, level and identity of the insurer, must be approved by the Regulator. Licensed operation of railway assets without insurance approved by the Regulator would constitute a breach of the relevant licence and could render the company responsible liable to enforcement action by the Regulator.
- 2.5 In order to assist operators in putting together their insurance programmes, the insurance guidance covers the minimum requirements which must normally be met for the Regulator to consider such insurance acceptable.

### **The Regulator's objectives**

- 2.6 Three of the Regulator's key operational objectives are to ensure that all parts of the contractual matrix continue to fit together to promote a better railway, to act to secure compliance and to promote change and improvement where necessary. In relation to his insurance functions, the Regulator is looking to achieve an insurance regime which:
- (a) ensures that operators arrange and maintain sufficient cover to protect third parties;
  - (b) helps to ensure cover is obtainable in the market at the prescribed levels by fostering understanding of the requirements and risks of railway operation among the insurance community;
  - (c) allows for premiums which are reasonably affordable to small operators and proportionate to the risks brought to the industry by each insured party; and
  - (d) ensures that, where no alternatives are available or are not economically feasible for industry parties, joint insurance arrangements are equitable, both in the way costs are apportioned and in providing participants with an appropriate measure of influence in the management of these arrangements.
- 2.7 The Regulator's interest in insurance is confined to third party liability insurance. However, other statutory requirements and commercial prudence will dictate the

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<sup>3</sup> With the exception of the Network (Sidings) licence granted to the British Railways Board by the Secretary of State.

scope and level of other insurances an operator will wish to procure. One of the few circumstances in which the Regulator will be interested in an operator's total insurance cover is for the purpose of approving an operator's level of self-insurance in relation to third party liabilities. In such cases, the Regulator will wish to be assured that an operator has the financial ability to meet his obligations in total: i.e. the potential self-insured liability under all insurance policies held, including third party insurance.

### **The Claims Allocation and Handling Agreement (CAHA)**

2.8 Another condition in all<sup>4</sup> licences requires that Licensees be party to arrangements approved by the Regulator for allocating liabilities between operators and handling claims. CAHA, by which all licensed industry parties currently satisfy this requirement, is due for review shortly and will be the subject of consultation separately by the Rail Industry Disputes Resolution Committee under the procedures in Clause 19 of CAHA. CAHA is further discussed in section 6 of this document.

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<sup>4</sup> With the exception of the Network (Sidings) licence granted to the British Railways Board by the Secretary of State.



### ***3. Proposed changes to the insurance guidance***

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- 3.1 Currently, the insurance guidance is published as an enclosure to the guidance on licensing. However, restructuring of the rail industry is now well advanced and a considerable number of licences to operate railway assets have now been granted. There are likely to be new entrants to the rail industry in the future who will require to be licensed, particularly freight operators, but, for existing operators, the insurance guidance is now a matter of continuing compliance rather than an element in a new licence application. It is therefore necessary that the insurance guidance should be capable of being read as a stand-alone document which is clearly relevant to existing Licensees as well as to new applicants.

#### **Scope of policies: contractors and sub-contractors**

- 3.2 Paragraph 6(d) of the draft revised insurance guidance at Annex A seeks to extend the current requirement on the Licensee to include in its insurance arrangements other parties to the extent required by any underlying contracts or agreements. This issue is examined in more detail in section 4 of this consultation paper.

#### **Scope of policies: level of cover**

- 3.3 The Regulator currently requires Licensees' third party policies to provide insurance of no less than £155 million, though operators can insure to a higher level if they consider this to be in their commercial interests. From time to time, certain industry parties have questioned whether £155 million cover is necessary in all circumstances. The question of whether £155 million remains sufficient in the future is one which the Regulator will keep under review. However, he does not believe that there is a case at this stage for changing the £155 million minimum.
- 3.4 This does not rule out requests from operators for a different, lower level of cover. However, paragraph 9 of the draft revised insurance guidance at Annex A explains that any request for the Regulator to consider a different level of cover must be made on the basis of a fully argued case including a full risk analysis. Any such application should be made as early as practicable, since the Regulator will wish to examine such proposals rigorously. All such applications will be judged on their merits. A particular factor will be the type and scope of operations undertaken by the applicant. Should the Regulator agree to a request for a lower level of cover, it is likely that he will wish

to restrict the scope and location of operations covered by the lower level of insurance.

### **Basis of cover**

3.5 The basis of cover which the Regulator believes is appropriate is set out in paragraph 10 of the draft revised insurance guidance at Annex A and no changes are proposed. Cover up to £60 million should be on an 'occurrence' basis, but it is generally acceptable for cover in excess of £60 million to be on a 'claims made' basis, which reflects the reality of the cover available through the market at these higher levels. It will also be acceptable for the cover in excess of £60 million to be obtained through a shared policy provided that there is provision for pre-paid reinstatement in the event of erosion of cover. Any request for the Regulator to consider a proposal resting on a different basis of cover should be made at an early stage to allow for thorough examination. However, the Regulator wishes cover to be on the best possible basis. As long as sufficient capacity exists for cover on an 'occurrence' basis up to £60 million, the Regulator is unlikely to consider proposals for a 'claims made' basis to be acceptable.

**3.6 Although no specific changes are proposed to this section of the insurance guidance, the Regulator would nevertheless welcome comments on how shared limits have worked in practice and whether operators generally consider this meets their commercial needs.**

### **Self-insurance**

3.7 Paragraphs 15 - 20 of the draft revised insurance guidance at Annex A contain guidance to Licensees proposing to self-insure part of their third party liability. In each case the Licensee will be required to demonstrate to the Regulator that it has acted prudently to limit the risks of self-insurance, that the level of self-insurance proposed is appropriate and that it has the ability to meet its self-insured liabilities. Paragraphs 18 and 19 of the draft revised insurance guidance at Annex A describe what Licensees must submit to the Regulator to provide the required evidence.

3.8 The existing insurance guidance requires applicants for approval of self-insurance to complete the Notification of Intention to Self-Insure Part of Third Party Liability ('the Notification'). When the insurance guidance was revised in January 1996, new requirements relating to the quantification of liability and confirmation of the Licensee's ability to meet these liabilities (set out in paragraphs 18 and 19 of the draft revised insurance guidance at Annex A) were introduced in addition to the

requirement to complete the Notification. The new evidence requirements have proved to provide far better and more meaningful information on the applicant's self-insurance proposals than the information requirements contained in the Notification. Accordingly, the requirement on applicants for approval of self-insurance proposals to complete the Notification has been removed from the draft revised insurance guidance at Appendix A. Although the other changes to the insurance guidance will only be applicable to insurance arrangements entered into or renewed after 31 March 1997, the removal of the requirement on applicants to complete the Notification will have effect from a date shortly after the publication of the revised insurance guidance (date to be advised in the revised insurance guidance).

- 3.9 Where there is a lack of reliable statistical information with the result that it may be difficult to provide a sufficiently reliable quantification of risk on the basis of a risk analysis, the Regulator will expect to see evidence that all liabilities that may occur can be met. In particular, consideration should be given to the merits of negotiating a cap on aggregate self-insured exposure.

### **The Regulator's approval of insurance proposals**

- 3.10 Paragraph 20 of the draft revised insurance guidance at Annex A explains that it is a licence requirement that Licensees shall, in respect of licensed activities, maintain third party liability insurance on terms approved by the Regulator. The Regulator's approval of proposed insurance arrangements is a necessary precondition for the grant of any licence and, as a matter of licence compliance, is needed when any material change occurs and whenever third party insurance policies are renewed. The Regulator's approval is also needed for insurance policies arranged by franchisees on behalf of licensed train operating companies moving from British Rail ownership into the private sector through the franchising process.
- 3.11 The insurance guidance states that Certificates of Insurance must be provided no later than 15 days before the inception of policies or expiry of any previous policies. Full copies of policies must generally be lodged with the Regulator no later than 30 days after the policy has come into force. The Regulator acknowledges that, in the past, neither operators nor insurers have placed significant priority on the production of full policy wordings, and it has taken several months before full policies have been available. This is not appropriate or acceptable for the future. The Regulator cannot be certain that insurance fully meets his requirements until the full policy is available and operators themselves similarly will not know until then that their policies are acceptable. The Regulator sees no reason why full policies cannot be available within

30 days and expects Licensees to have mechanisms in place to ensure that they are able to comply with these requirements.

- 3.12 Timely production of documents is not only a matter of licence compliance, but also relevant to the smooth and efficient operation of the Regulator's approval procedures. The Regulator wishes to develop mechanisms and procedures which will enable Licensees, insurance brokers and insurers to fulfill his requirements without imposing undue administrative burdens on them. He expects that the industry will share this aspiration.
- 3.13 There is clearly a trade-off between shorter approval time for highly standardised wordings and a longer lead time for approval for those which are more highly customised. Paragraph 23 of the draft revised insurance guidance at Annex A expresses the Regulator's support for greater use of approved standard wordings and formats for certificates and policies. However, the Regulator does not consider it appropriate either to insist on standard wordings or to propose areas which might be standardised. This must be a matter for licensees themselves in the light of their own commercial judgement.
- 3.14 The Regulator invites comments and suggestions from consultees on the effective use of standard wordings and formats and the processes by which the industry might agree and seek the Regulator's prior approval to standard wordings.
- 3.15 Paragraph 24 of the draft revised insurance guidance at Annex A asks Licensees to note that, in all cases, the Regulator's approval will be conditional upon a requirement that he is notified of any changes to the relevant insurance documentation and any material changes to the Licensee's financial position that would have the effect of invalidating its written confirmation of its ability to meet its self-insured liabilities. Licensees will need to have in place mechanisms which will enable them to comply with these conditions.

### **Annual consultation**

- 3.16 Paragraphs 27 and 28 of the draft revised insurance guidance at Annex A explain that the Regulator proposes, in addition to ad hoc consultation, a formal round of consultation each summer. Where appropriate, this is intended to allow for publication of revised insurance guidance in the autumn, in good time for the preparation of insurance arrangements ready for renewal the following spring, when the majority of annual renewals fall due.

**3.17 The Regulator invites comments and suggestions on the proposal to institute an annual cycle of insurance consultation.**

**Summary of questions asked**

5. In addition to inviting comments on the proposed changes to the insurance guidance, this section raises a number of more general questions. Views are invited on:
- (a) how shared limits have worked in practice and whether operators generally consider this meets their commercial needs (paragraph 3.6);
  - (b) the effective use of standard wordings and formats and the processes by which the industry might agree and seek the Regulator's prior approval to standard wordings (paragraph 3.14); and
  - (c) the Regulator's proposal to institute an annual cycle of insurance consultation (paragraph 3.17).



## ***4. Contractors and sub-contractors***

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### **Contractors and sub-contractors**

- 4.1 The current edition of the insurance guidance notes the need for further consideration of issues raised by the situation of contractors and sub-contractors who are not themselves licensed operators. Such contractors cannot be obliged to carry £155 million of insurance. There is the possibility of a gap in cover in cases where the Licensee has not entered into a contractual obligation to provide third party liability insurance cover on behalf of its contractors and sub-contractors for the difference between the cover carried by the contractor or sub-contractor and the £155 million required by the Regulator. In the emergent railway industry, where the employment of contractors and sub-contractors is likely to increase, this is a potentially significant and undesirable gap in the protection afforded to third parties.
- 4.2 The Regulator wishes to establish an appropriate mechanism for ensuring that all contractors and sub-contractors undertaking activities which would otherwise be carried out directly by Licensees themselves are covered by the type and level of insurance specified in the insurance guidance. The Regulator's initial view is that all contracts between Licensees and contractors or sub-contractors relating to such activities should specify a requirement to insure to the levels required by the Regulator. Some operators already have such a standard clause in all contracts as a matter of good business practice. The issue is the appropriate mechanism for making this good practice a universal standard practice.
- 4.3 There are various options. It would be possible, for example, for the Regulator to consider licence modifications to require contracts to include an 'obligation to insure' clause. However, this might be considered to be intrusive and would require burdensome and time-consuming compliance monitoring and enforcement mechanisms. The Regulator wishes to avoid placing such burdens on the industry and on his own administrative resources, which are financed by the industry through licence fees. He would therefore welcome views from the industry on other means of achieving the objective - perhaps through standard wording in insurance policies themselves.
- 4.4 One closely related issue is that of the cost to operators of a contractual commitment to include contractors and sub-contractors in their insurance policies. The Regulator

does not believe that there is necessarily a case for premiums to rise as a result. There are two main reasons:

- (a) it does not result in an increase in total railway risk; and
- (b) the Licensee will generally wish to ensure that the contractor and sub-contractor have substantial indemnity limits in their own insurance. The Licensee would therefore only contract to include them in his own insurance over and above these limits, so the majority of claims for which contractors are liable will be covered by their own policies.

**4.5 The Regulator invites views from consultees on the proposal to require that contracts include an obligation to insure and the mechanisms for achieving that objective.**

**Private passenger coaches and freight wagons**

4.6 In principle, the insurance issues raised by privately-owned passenger coaches and freight wagons appear to be similar to those raised by contractors and sub-contractors discussed above. It is recognised that the situation concerning private passenger coaches and freight wagons is complex as there may not always be a direct contractual relationship between the Licensee and the owner of the vehicles. In considering the position, the following key issues need to be taken into account:

- (a) where responsibility lies for ensuring continuing safety of the vehicles;
- (b) the precise nature of the contractual relationship between the licensed operator and the other parties involved;
- (c) the role of the Railtrack certification regime; and
- (d) the differences between the arrangements for domestically-owned and registered vehicles and those owned or registered elsewhere.

4.7 The complexity of the issues involved means that the Regulator is not currently in a position to make a firm set of proposals. He does not consider that the current situation is sustainable in the longer term and believes that it is important that progress is made towards workable solutions. One way forward would be for a group to be constituted to explore the issues and, where appropriate, suggest solutions. The group might include representatives from Railtrack, the Health & Safety Executive, freight operators and private coach and wagon owners.

**4.8 The Regulator would welcome comments on the proposal to establish such a group, in particular whether this would be the best way to make real progress in establishing workable solutions.**

**Summary of questions asked**

4.9 Views are invited on:

- (a) the proposal to require that contractors' and sub-contractors' contracts include an obligation to insure (paragraphs 4.1 to 4.5); and
- (b) the proposal to establish a group to discuss and resolve the issues raised by private passenger coaches and freight wagons (paragraphs 4.6 to 4.8).



## ***5. Keeping the insurance guidance under review***

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- 5.1 Paragraph 27 of the revised insurance guidance at Annex A outlines the Regulator's proposal to set in place an annual cycle of consultation with the industry. Paragraph 28 explains that, in addition, the Regulator will continue to undertake ad hoc consultation as appropriate.
- 5.2 The Regulator is conscious that the railway industry has yet to develop a forum for discussing common insurance concerns. To some extent the Insurance Working Group served this purpose during the early years of the industry's restructuring, although it offered only limited representation of the views of operators in the private sector. The Regulator is aware that some Licensees see benefits in establishing a 'buyers' forum' and that there have also been suggestions that Licensees' insurance managers might also wish to meet to discuss their common interests. The Regulator will wish to establish relations with any such groups as well as to continue to discuss matters of concern, in confidence where appropriate, with individual Licensees, insurance brokers and insurers.
- 5.3 A separate issue is the extent to which operators wish to develop current insurance arrangements to meet their needs, in particular the Central Insurance Facility. The industry in general is not currently involved in the management of this facility. This would matter less if there was more than one facility competing for business and offering operators a choice. It is not for the Regulator to offer a solution, but he has a general concern that, without dialogue between industry parties, it is difficult to see how the industry in general will be able to ensure that the insurance market develops to meet operators' needs in the most effective way. The Regulator considers that this is an issue for which the industry itself will need to find solutions. He will, nevertheless, keep under review any initiatives that might develop in this area.
- 5.4 The Regulator invites comments and suggestions on the best way to foster an effective dialogue with the industry and other parties with an interest and would be interested in views on the prospects for the development of a more competitive insurance market in the future.**



## 6. *The Claims Allocation and Handling Agreement*

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- 6.1 The Regulator's requirements regarding the licence condition dealing with Third Party Liability Insurance are the subject of this consultation. As mentioned in section 2, another relevant licence condition requires that Licensees be party to arrangements approved by the Regulator for allocating liabilities between operators and handling claims. CAHA, by which Licensees satisfy this requirement, is due for review shortly and will be the subject of consultation separately by the Rail Industry Disputes Resolution Committee under the procedures in clause 19 of CAHA.
- 6.2 The objectives underpinning CAHA are:
- (a) to provide a mechanism which enables claims to be settled quickly through a single focal point so that claimants do not have to wait for operators to reach agreement on the precise allocation of liability;
  - (b) to avoid costly and time-consuming inter-operator litigation through pre-agreed liability for smaller claims;
  - (c) to provide a central agency for the collection of claims data so as to establish an industry claims history; and
  - (d) to provide operators with a ready-made means of complying with the licence requirement for claims handling arrangements.
- 6.3 These public interest objectives are vitally important in a disaggregated railway and the Regulator believes that it is important that the industry does not lose sight of them. However, CAHA is also an integral part of the third party liability insurance arrangements for the industry, so it is vitally important that it works effectively. The industry has perhaps not fully appreciated the importance of CAHA and may not have given sufficient attention to its implications in the past. The Regulator intends to participate fully in the review of CAHA and believes it will be in the best interest of rail operators and other relevant parties to similarly to play an active and constructive part in that review.



# ***Annex A: Proposed amendments to the Guidance on Insurance against Third Party Liability***

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## **Introduction**

1. Licences for operators of railway assets contain a condition requiring the operator to maintain insurance against third party liabilities in respect of licensed activities. The terms of such insurance (including type, cover, level and the identity of the insurer) must be approved by the Regulator. This guidance indicates the minimum requirements which must normally be met for the Regulator to consider such insurance acceptable.
2. This edition of the guidance is applicable to policies entered into or renewed after *31 March 1997*. Licensees will also be required to procure that policies entered into or renewed prior to *1 April 1997* and which continue in force after that date are modified to comply with the requirements of this edition of the guidance unless otherwise agreed with the Regulator. Copies of the *January 1996* edition of the guidance outlining the requirements applicable until *1 April 1997* can be obtained from the address at the end of this guidance.

## ***The Regulator's role and objectives in relation to third party liability insurance***

3. All licences granted to operators of passenger trains, non-passenger trains, stations, networks and light maintenance depots contain a condition which requires the licence holder to maintain insurance (including self- insurance) against third party liabilities. A copy of the condition is in the Appendix to this guidance. The condition requires that the terms of such insurance including type, cover, level and identity of the insurer, must be approved by the Regulator. Licensed operation of railway assets without insurance approved by the Regulator would constitute a breach of the relevant licence and could render the company responsible liable to enforcement action by the Regulator.
4. *Three of the Regulator's key operational objectives are to ensure that all parts of the contractual matrix continue to fit together to promote a better railway, to act to secure compliance and to promote change and improvement where necessary. In*

*relation to his insurance functions, the Regulator is looking to achieve an insurance regime which:*

- (a) *ensures that operators provide and maintain sufficient cover to protect third parties;*
- (b) *ensures that cover is obtainable in an open market at the prescribed levels by fostering understanding of the requirements and risks of railway operation among the insurance community;*
- (c) *allows for premiums which are reasonably affordable to small operators and proportionate to the risks brought to the industry by each insured party; and*
- (d) *ensures that, where no alternatives are available or are not economically feasible for industry parties, joint insurance arrangements are equitable, both in the way costs are apportioned and in providing participants with an appropriate measure of influence in the management of the schemes.*

### **Scope of policies**

- 5. In addition to such insurances as are required by law, the Licensee will be required to effect and maintain in force for the duration of the licence a policy or policies of insurance in respect of third party risks which cover the Licensee, his employees and any other person expressly required to be included as an insured in respect of any legal liability which may be incurred by him or them in respect of death or bodily injury to any person and loss or damage to property arising from the activities permitted under each licence held.
- 6. To comply with the licence condition, such third party policies must, inter alia:
  - (a) provide insurance of no less than £155 million in respect of all liabilities;
  - (b) ensure that any exclusion of damage to property in the care, custody and control of the Licensee shall not apply to accompanied personal luggage;
  - (c) include liability for damage to the property of any railway industry party; and
  - (d) include as an insured any other party to the extent that such party is required to be insured or indemnified in any underlying contract or agreement with the Licensee *and provide on behalf of its contractors or sub-contractors third*

*party liability cover for any difference between the cover carried by the contractor or sub-contractor and the £155 million required by this guidance.*

7. The Licensee must ensure that his insurers are given a copy of this guidance and that they are also provided with any subsequent editions.
8. Such third party policies are not required to cover:
  - (a) liabilities in respect of death or injury to employees arising in the course of employment, for which separate insurance is necessary to comply with statutory requirements;
  - (b) liability in respect of damage to goods carried for hire or reward, eg in the case of freight, parcels operations or other property in the care, custody and control of the Licensee, except as provided for in paragraph 6 b) of this guidance; or
  - (c) liabilities covered under other statutory or standard classes of insurance, eg motor insurance.
9. *Operators who wish to request approval for a type or level of cover different from that described in this guidance should, at an early stage, submit a fully argued case for the Regulator's consideration. The Regulator believes that the type and level of cover set out in this guidance is necessary in the public interest and he will expect any application for a derogation to rest on a robust case, including a full risk analysis.*

#### **Basis of cover**

10. Cover up to £60 million should be on an 'occurrence' basis *as the Regulator believes that this provides the best available protection.* However, it will generally be acceptable for cover in excess of £60 million to be on a 'claims made' basis. Cover in excess of £60 million may be either on a 'stand alone' basis or on the basis of a shared policy. In the latter case, however, the Regulator will expect any shared policy to provide for pre-paid reinstatement in the event of any erosion of cover. *Any application involving a different basis of cover must be made in the form of a fully argued case and at an early stage as the Regulator will wish to examine such proposals rigorously.*

#### **Notice of changes to policies**

11. The policy(ies) are required to be endorsed to provide that:

- (a) insurers will provide the Regulator with at least 30 days' notice of the insurer's intention to cancel or avoid the policy in the event of non-payment of premium;
  - (b) insurers will provide the Regulator with at least 30 days' notice of the insurers intention to cancel the policy for any reason, including where at the request of the insured; and
  - (c) insurers will provide the Regulator with at least 30 days' notice of any material reduction in the cover provided under the policy(ies) arising after the inception date of the policy, including where at the request of the insured.
12. The inclusion in policies of the endorsements in paragraph 11 above means that, if the required period of notice is not given, any proposed cancellation or change to the policy shall have no effect.
13. Licensees should note that cancelling a policy, allowing it to lapse, or materially reducing the cover provided without having in place alternative arrangements approved by the Regulator will render them liable to enforcement proceedings in accordance with Sections 55 to 57 of the Railways Act 1993.

### **Identity of insurers**

14. The Licensee will be responsible for the selection of insurers duly authorised and of good repute, including any 'captive' insurers which the Licensee proposes to use, and should explain to the Regulator what steps it has taken to satisfy itself on those matters.

### **Self-insurance**

15. Licensees should note that they must seek the Regulator's approval to any level of self-insurance they propose in respect of third party liability, *including any deductibles held on insurance policies.*
16. It will be for the Licensee in each case to demonstrate to the Regulator both that the level of self-insurance proposed is appropriate and that it has the ability to continue to meet its total obligations. *In forming his view of any proposal for self-insurance, the Regulator will expect to see evidence that the Licensee has acted prudently to limit the risks of self-insurance.* Although the pre-arranged facility mentioned in Part 3 of the Guidance on Licensing of Operators of Railway Assets currently offers cover from £5

million upwards, that should not be taken to imply that the Regulator will consider £5 million to be an acceptable level of self-insurance.

17. *The Regulator's letter of approval will normally provide that the Licensee must notify the Regulator of any changes which would have a material effect on its ability to meet its potential obligations arising under self-insurance. The Licensee will need to have in place appropriate mechanisms to allow it to comply with this condition. The Licensee will normally be required to resubmit its self-insurance arrangements for the Regulator's approval at least annually, normally at the same time as approval is sought in respect of the insurance policies held for the layers up to £155 million not covered by the self-insurance arrangements.*

### **Evidence of ability to meet self-insured obligations**

18. It is for the Licensee to demonstrate to the Regulator that it has the ability to meet its self-insured obligations. This should normally take the following form:

- (a) a quantification of the Licensee's potential third party liability risk:

**either**

*an aggregate cap on self-insured liabilities (the Licensee must provide a statement of the amount provided for in the cap and evidence that the cap is in place from the date of commencement of insurance cover);*

**or**

*a statistical analysis of third party risk by a risk management consultant or other appropriate professional adviser, including analysis of the number, type and expected total cost of occurrences on an annualised basis and an indication of the degree of statistical variation around estimates;*

**and**

- (b) confirmation of the Licensee's ability to meet its potential self-insured liabilities:

**either**

*a certificate signed by the Licensee's directors certifying that they have considered the information produced under paragraph 18(a), that they have reviewed the likely insurance cost in light of the company's business plan and*

*that they confirm they have a reasonable expectation of meeting such insurance liabilities for the foreseeable future. This certificate is to be accompanied by a statement from the company's auditors certifying that the directors' statement is not inconsistent with the information of which the auditors are aware from their audit work on the company's accounts;*

**or**

*where the Licensee believes such a certificate to be inappropriate, such other evidence of sufficient financial provision as may be agreed with the Regulator.*

19. The Licensee should contact the Office of the Rail Regulator if it is not possible to establish a satisfactory statistical analysis of risk to allow the estimation of the expected total cost on an annualised basis of occurrences. In such cases, a cap will normally be required on the annual aggregate self-insured liability.

#### **The Regulator's approval of proposals for third party liability insurance**

20. *The Licence condition requires Licensees to maintain insurance against third party liabilities on terms approved by the Regulator. The Regulator's approval must be obtained before the grant of any licence and, as a matter of licence compliance, at any material change and when policies are renewed. Insurance policies fall due for renewal annually and, in order to remain compliant with their licences, it will be necessary for Licensees to obtain the Regulator's approval of their proposed new arrangements in advance of each policy renewal. At each application the Regulator will consider whether the proposed arrangements meet his requirements as set out in this guidance.*

#### **Certificate of Insurance**

21. The Licensee must provide Certificate(s) of Insurance no later than 15 days before inception of the policy(ies) or expiry of any previous policy. Such Certificates are required to be binding irrespective of a change in circumstances. The Certificate(s) must identify each insurer and the proportion of cover each has taken, the period of the policy and must summarise the scope of the policy and its exclusions. If the policy is not subject to English or Scots law, then the governing law under which the policy is to be interpreted should be stated.
22. Licensees should lodge full copies of their policies with the Regulator no later than 30 days after the policy has come into force, unless it has been agreed in advance with the Regulator that there are good reasons why a different timescale would be more

appropriate. Licensees should note that the Regulator is likely to give only a conditional or time-limited approval to insurance arrangements until the full policy has been submitted.

### **Use of standard wordings**

1. *Wherever possible the Regulator wishes to reduce the administrative burden on Licensees, their insurance brokers and insurers in respect of approval and reapproval of insurance arrangements. He therefore welcomes the use of standard wordings and formats for certificates and policies, where these meet the needs of Licensees and are consistent with his requirements.*

### **Form of approval**

24. *The Regulator's approval will be conditional upon a requirement that he is notified of any changes to the relevant insurance documentation and any material changes to the Licensee's financial position that would have the effect of invalidating its ability to meet its self-insured liabilities. Licensees will need, therefore, to have in place mechanisms to ensure that they are able to comply with the requirement to notify such changes.*

### **Summary checklist**

25. When submitting third party liability insurance arrangements for the Regulator's approval, the following documents and information should be provided, together with a copy of this checklist with each box ticked to indicate that the details have been provided:
  - Certificates of insurance signed by the Licensee / applicant's Broker or Lead Insurer in respect of each of the relevant policies.
  - Each certificate must specify the governing law under which the policy is to be interpreted.
  - Each certificate must identify all of the Insurers and their proportions.
  - Each certificate must specify the inception date of cover and the expiry date.
  - Each certificate must specify the Limit of Indemnity provided and whether it is per occurrence or in the aggregate for the policy or other period. If any limit is in the aggregate for the policy or other period, the certificate must state the provisions for reinstatement. If an additional premium is required, the Licensee

must confirm by separate letter its intention to pay such additional premiums when due so as to maintain the minimum limit required by the Regulator.

- Each certificate in respect of any excess layer must state the attachment point.
- Each certificate must summarise the scope of the policy and all its exclusions.
- Each certificate must specify whether the policy provides cover on a "claims made" basis or a "loss occurring" basis.
- Each certificate must confirm that the policy described provides specifically that:
  - Insurers will provide the Regulator with at least 30 days notice of their intention to cancel or void the policy in the event of non-payment of premium;
  - Insurers will provide the Regulator with at least 30 days notice of their intention to cancel the policy for any reason, including where at the request of the Insured; and
  - Insurers will provide the Regulator with at least 30 days notice of any material reduction in the cover provided under the policy arising after the inception date of the policy, including where at the request of the Insured.
- Each certificate must confirm that the policy covers:
  - the Licensee;
  - his employees; and
  - any other person expressly required to be included as an insured.
- An explanation as to what steps the Licensee has taken to satisfy itself on the selection of insurers duly authorised and of good repute.
- If self-insurance by excess or other means is proposed, provide evidence of the ability of the Licensee to meet his obligations (see also Notification of Intention to Self-Insure Part of Third Party Liability).
- Confirm date by which full copies of all policies will be lodged with the Regulator.

- Confirmation that any exclusion of damage to property in the care, custody and control of the Licensee shall not apply to accompanied personal luggage.

### **Keeping the guidance under review**

26. *The Regulator will keep this guidance under review in the light of experience and of regular consultation with the railway industry, insurers and insurance brokers. Formal consultation will take place during each summer on developments generally and the need for any changes to this guidance. Revised guidance, if appropriate, will be published in the autumn of each year. As the majority of the industry's liability policies currently expire during the spring, this will allow Licensees and their insurance brokers to review their third party liability insurance arrangements in good time for submission of renewal proposals to the Regulator.*
27. *The Regulator will also undertake ad hoc consultation, both generally and with individual Licensees, insurers and insurance brokers, on emerging concerns. Licensees, insurance brokers and insurers are encouraged to contact the Office of the Rail Regulator to discuss insurance matters at any time.*
28. If you have any queries please contact:  
  
Peter West  
Office of the Rail Regulator  
1 Waterhouse Square  
138-142 Holborn  
Tel: 0171 282 2058  
Fax: 0171 282 2043
29. Further copies of this guidance can be obtained from:  
  
The Librarian  
Office of the Rail Regulator  
1 Waterhouse Square  
138-142 Holborn  
London EC1N 2ST  
Tel: 0171 282 2001  
Fax: 0171 282 2045  
E-mail: orr@dial.pipex.com

## **Appendix: The Licence Condition**

### **Insurance against Third Party Liability**

1. *The licence holder shall, in respect of licensed activities, maintain insurance (including self-insurance) against third party liabilities on terms approved by the Regulator (including, but without limitation, with respect to the type, cover and level of insurance and identity of insurer), with any such modification as may be required pursuant to paragraph 3.*
2. *The licence holder shall, except as the Regulator may otherwise consent, procure that every insurance policy maintained pursuant to paragraph 1 shall bear an endorsement to the effect that 30 days' notice shall be given to the Regulator by the insurer or insurance broker of any lapse or cancellation of, or material change to, the policy.*
3. *Where the Regulator notifies the licence holder that the Regulator reasonably requires any modification of the insurance approved by the Regulator pursuant to paragraph 1, the licence holder shall, no later than 60 days (or such longer period as the Regulator may approve) from the date of the notice, procure that such modification is made.*
4. *In this Condition:*  
  
*"self-insurance" means the licence holder's financial capacity to meet any liability to a third party in respect of which the licence holder does not otherwise have insurance.*

## ***Annex B: - Section 4 of the Railways Act 1993***

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- 4.-(1) The Secretary of State and the Regulator shall each have a duty to exercise the functions assigned or transferred to him under or by virtue of this Part in the manner which he considers best calculated-
- (a) to protect the interests of users of railway services;
  - (b) to promote the use of the railway network in Great Britain for the carriage of passengers and goods, and the development of that railway network, to the greatest extent that he considers economically practicable;
  - (c) to promote efficiency and economy on the part of persons providing railway services;
  - (d) to promote competition in the provision of railway services;
  - (e) to promote measures designed to facilitate the making by passengers of journeys which involve use of the services of more than one passenger service operator;
  - (f) to impose on the operators of railway services the minimum restrictions which are consistent with the performance of his functions under this Part;
  - (g) to enable persons providing railway services to plan the future of their businesses with a reasonable degree of assurance.
- (2) Without prejudice to the generality of subsection (1)(a) above, the Secretary of State and the Regulator shall each have a duty, in particular, to exercise the functions assigned or transferred to him under or by virtue of this Part in the manner which he considers is best calculated to protect-
- (a) the interests of users and potential users of services for the carriage of passengers by railway provided by a private sector operator otherwise than under a franchise agreement, in respect of
    - (i) the prices charged for travel by means of those services, and
    - (ii) the quality of the service provided,

in cases where the circumstances appear to the Secretary of State or, as the case may be, the Regulator to be such as to give rise, or be likely to give rise, to a monopoly situation in the passenger transport market; and

- (b) the interests of persons providing services for the carriage of passengers or goods by railway in their use of any railway facilities which are for the time being vested in a private sector operator, in respect of
  - (i) the prices charged for such use; and
  - (ii) the quality of the service provided.
- (3) The Secretary of State and the Regulator shall each be under a duty in exercising the functions assigned or transferred to him under or by virtue of this Part-
  - (a) to take into account the need to protect all persons from dangers arising from the operation of railways, taking into account, in particular, any advice given to him in that behalf by the Health and Safety Executive; and
  - (b) to have regard to the effect on the environment of activities connected with the provision of railway services.
- (4) The Secretary of State shall also be under a duty, in exercising the functions assigned or transferred to him under or by virtue of this Part, to promote the award of franchise agreements to companies in which qualifying railway employees have a substantial interest, "qualifying railway employees" meaning for this purpose persons who are or have been employed in an undertaking which provides or provided the services to which the franchise agreement in question relates at a time before those services begin to be provided under that franchise agreement.
- (5) The Regulator shall also be under a duty in exercising the functions assigned or transferred to him under this Part-
  - (a) until 31st December 1996, to take into account any guidance given to him from time to time by the Secretary of State;
  - (b) to act in a manner which he considers will not render it unduly difficult for persons who are holders of network licences to finance any activities or proposed activities of theirs in relation to which the Regulator has functions under or by virtue of this Part (whether or not the activities in question are, or

are to be, carried on by those persons in their capacity as holders of such licences); and

- (c) to have regard to the financial position of the Franchising Director in discharging his functions under this Part.
- (6) In performing his duty under subsection (1)(a) above so far as relating to services for the carriage of passengers by railway or to station services, the Regulator shall have regard, in particular, to the interests of persons who are disabled.
- (7) Without prejudice to the generality of paragraph (e) of subsection (1) above, any arrangements for the issue and use of through tickets shall be regarded as a measure falling within that paragraph.
- (8) For the purposes of this section, "monopoly situation" has the same meaning as it has in the Fair Trading Act 1973 (in this Part referred to as "the 1973 Act"), except that in relation to the passenger transport market-
  - (a) the expression includes a monopoly situation which is limited to the passenger transport market in some part of the United Kingdom; and
  - (b) in the application of section 7 of the 1973 Act (monopoly situation in relation to the supply of services) for the purposes of paragraph (a) above, references in that section to the United Kingdom shall accordingly be taken to include references to a part of the United Kingdom.
- (9) In this section-
  - "environment" has the meaning given by section 1(2) of the Environmental Protection Act 1990;
  - "the passenger transport market" means the market for the supply of services for the carriage of passengers, whether by railway or any other means of transport;
  - "through ticket" means-
    - (a) a ticket which is valid for a journey which involves use of the services of more than one passenger service operator; or
    - (b) a combination of two or more tickets issued at the same time which are between them valid for such a journey.