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TRANSCRIPT OF PROCEEDINGS

O/N H-959651

THE HONOURABLE K. HAYNE AC QC, Commissioner

**IN THE MATTER OF A ROYAL COMMISSION
INTO MISCONDUCT IN THE BANKING, SUPERANNUATION
AND FINANCIAL SERVICES INDUSTRY**

SYDNEY

9.30 AM, FRIDAY, 23 NOVEMBER 2018

Continued from 22.11.18

DAY 64

MS R. ORR QC and MR M. HODGE QC appear with MR M. COSTELLO, MS E. DIAS, MR A. DINELLI, MR T. FARHALL, MR M. HOSKING and MS S. ZELEZNIKOW as Counsel Assisting
MR P. COLLINSON QC appears with MR L. HOGAN for ASIC

<JAMES ROGER FRANCIS SHIPTON, ON FORMER OATH [9.30 am]

<CROSS-EXAMINATION BY MS ORR

THE COMMISSIONER: Yes, Ms Orr.

MS ORR: Mr Shipton, at the end of yesterday I was asking you questions about ASICs approach to investigations. And I had asked you questions about the investigation of NAB in relation to the introducer program. I want to ask you now about ASICs handling of another matter which was CBAs mis-selling of consumer credit insurance. You know that there was mis-selling to tens of thousands of customers by CBA?---Yes, I'm aware of that.

And prior to the evidence that was given by CBA about those matters in the first round of public hearings in the Commission, had ASIC taken any enforcement action against CBA for those matters?---No.

As at today's date has ASIC taken any enforcement action against CBA in respect of those matters?---Not as at today's date, no.

When did ASIC first commence an investigation into those matters for the purposes of considering whether to take any enforcement action?---I believe that a referral was made in October of this year.

So it was, according to your statement, about a month ago, on 22 October, nearly two and a half years after the notification by CBA and months after the matter was examined in the public hearings in the Royal Commission that your enforcement team accepted that referral?---That's correct.

And that investigation will consider now whether any enforcement action should be taken against CBA?---Yes, that's right. And may I add that we were waiting for a review that was being undertaken into that business, which finished, as I remember, in September. So following that independent review by an independent firm, that – that review came in in September and then the referral went through in October, and as I understand it that independent review will form part of the evidence as a part of the investigation.

Why were you waiting for that review, Mr Shipton?---I understand that we were waiting for that review because that review was going to be important to the body of evidence.

Important to the body of evidence brought together as part of the investigation. Is that right?---Could you repeat the question, please?

I just want to distinguish between the decision to commence the investigation, which was not made until 22 October this year, I want to distinguish between that and the evidence gathering process within the investigation once it's commenced. Why not commence the investigation much earlier?---Well, I would certainly agree with you that it was a mistake not to commence the investigation much, much, much earlier.

When should it have been commenced, Mr Shipton?---It is difficult for me to say with absolute precision, except to say that I think we should have been commencing an investigation along the same timeline as we were working, as I understand it, very hard on a remediation program.

So the notification of these matters by CBA to ASIC was in May 2015. Should ASIC have commenced an investigation into those matters following that notification?---I believe that it was a mistake not to give thought, not – let me rephrase that. It was a mistake not to give enough consideration to commencing a – an investigation at a commensurate time to the notifications and the awareness of the issue, and to run an investigation in parallel with the remediation program. And if I may add, that if this matter or those facts were to present themselves today, then the processes and the questions that would apply would most likely trigger the commencement of an investigation.

And why didn't they in 2015, Mr Shipton? You've been asked to reflect on this matter for the purpose of preparing your witness statement. Why didn't that happen in 2015?---Well, I understand that I've been – and this is what I've been told by the team because I wasn't involved in the matter at the time – I've been informed that there was a focus on the remediation of CBA. I'm also informed that this was an industry-wide challenge that we were dealing with industry-wide issues. And if I remember correctly, we're dealing in the CBA matter with approximately 156,000 customers who are literally out of pocket because of this concern. And that this was a systemic issue across the entire industry. And as I understand it, at that time there was a focus on industry-wide reaction and as I also understand it there was a focus on trying to advance the remediation, advance industry change, get independent reviews on 11 financial institutions involved, but I most certainly agree that it – the investigation component should have started much earlier. And my last observation is when you're dealing with industry-wide, arguably systemic misconducts, and systemic mistakes and failures of the financial institutions, we only have 80 – about 80 personnel in the team that handles that issue. So the context is, is that this was an overwhelming amount of work being dealt with by a team which is only staffed to 80 people.

None of the things that you've just referred to in your answer to my question, Mr Shipton, precluded you from commencing an investigation into CBA for the purposes of considering enforcement action, did they?---Correct. And – and I have already considered the point to the earlier question, if I remember correctly, that I've said that it was a mistake not to commence that investigation at that time.

Yes. And I'm just trying to understand why that mistake occurred. That's why I'm asking you these questions, Mr Shipton. Do you agree that the matters that you referred to, the fact that this was an industry-wide challenge, the fact that 156,000 customers were out of pocket, the fact that this was a systemic issue, were all matters that reinforced the need for you to take strong action and commence an investigation?---Most definitely. And I believe I've been saying that throughout all of my responses. So I'm in most definite agreement that it was a mistake not to commence an investigation at that point in time.

What confidence can we have that those same matters arising today would not have the same result; would not lead to a focus on remediation to the exclusion of enforcement action?---Well, I – and if I may, I would like to reflect upon the NAB case study and the – the CCI case study in answering that question, because we have today processes that would mean that we are asking the teams very different questions than they were asked at that particular point in time. We now have processes today that have been instituted that did not – were not in a – in effect or in place at a – at that particular time, in both NAB and in relation to the CBA matter - - -

I want to be very clear - - -?---Yes.

- - - about the point in time you're referring to in your answer, Mr Shipton?---Of course.

Because the point in time in relation to CCI was May 2015?---Yes.

The point in time that I took you to in the NAB case yesterday was July this year?---Yes. And so I'm referring to the interim measures that I – we've put in place very recently, I think within the last three or four weeks.

I see?---And so today – today these matters would be handled very differently. And I am deliberately using the word "mistake", because I believe that there were mistakes made in relation to the NAB introducer. I believe that there were mistakes made in relation to this CCI matter. And I used the word "mistake" deliberately, because mistake, in effect, constitutes a misguided decision because there was – and this is answering your direct question – on why we – you should have confidence that it's different today, because we now have issued guidance that would mean that a decision like the one in CCI or the discussion that you were referring to in relation to NAB yesterday would have a very different starting point. The starting point today would be to ask the question and turn our minds to why not litigate this demonstrable breach. That is the clear guidance today that stands today.

And that's as of a few weeks ago?---That is of two or three weeks ago, yes.

Yes. I see. All right. Now, I want to come back to information sheet 151 and the flowchart of the process followed within ASIC in relation to enforcement action. So if we could go back to ASIC.0902.0001.0067. I had paused in taking you through

this flowchart to ask you questions about investigations. But if we continue through the flowchart, we see that if a formal investigation is conducted and ASIC does not find suspected misconduct, ASIC then considers whether non-enforcement regulatory tools such as surveillance or stakeholder engagement might be more effective?---That's correct.

And if the result is that the investigation does find suspected misconduct, then ASIC moves to assess what the appropriate remedy will be?---So you're now looking at the – the – the yes flow.

Yes?---Yes.

Having found suspected misconduct you're directed to the white box towards the bottom of the page which requires assessment of the appropriate remedy?---Yes.

So is it only at the point that ASIC has completed its investigation into potential misconduct that it moves to assess the appropriate remedy?---Well, that would be a point in time in which it is assessed, but there would be, in practice, a continuum and an assessment and a formulation of – of thinking around what would be the appropriate approach. I think that you would add – it would be – it would be best to add the words "investigate different contraventions", as well as "remedy". I would add that this chart is drafted, as I understand it, for brevity and for simplification, but it is remedy and also an investigation or assessment as to the potential contraventions and breaches.

I'm sorry, where would you add the words "investigate different contraventions" in the flowchart?---Well, all the way through. But you're asking me about assessment of appropriate remedy.

Yes, I am?---And what I'm saying is that is – that is co-existent with the – the alleged or potential contraventions.

But is the appropriate time to assess the appropriate remedy at the conclusion of your investigation?---Yes, it is. And that's why I think – that's why I was referring to it being a continuum and an ongoing – an ongoing – an ongoing assessment. Again, this flowchart is a very simplified version of the process, and is – is drafted, as I said, for brevity.

I understand that. I'm just asking you to assist me to understand what the point is at which that assessment of the appropriate remedy should be made. And I understand you to say it's appropriate to do that at the conclusion of the investigation?---Yes. And – and I also understand, from reviewing files and – and also discussing with team members, that at the point of – at the point of referral, then there is discussion, there is reference made to the – not just the appropriate remedy or course of action or potential – let me say potential course of action but that is co-existent, as I said before, with the – the contraventions, the potential contraventions that we're looking at. And I would also add that these processes aren't rigid. The teams have to

exercise professional judgment throughout, and that throughout the course of an investigation, and then throughout the flow of the entire matter, professional judgment needs to be exercised and assessments can change, new evidence can be obtained and new courses of action can be followed.

The project team that assesses the appropriate remedy makes a recommendation about that. Is that correct?---Yes, that's correct.

And the ultimate decision about the action or outcome or remedy is made by either a senior executive, a Commissioner, or the enforcement committee?---That's correct, depending on the classification of the case.

So what sorts of matters are significant enough to require a decision by a Commissioner?---Well, it would be preferable – and this is – this is – this is now the case – that significant matters should be channelled towards the enforcement committee, and we are also moving away from Commissioners making executive decisions in relation to these matters. But returning to this particular case study, and the procedures that existed before this change that we're transitioning, serious matters, major matters, are the ones that are escalated to a Commissioner, Commissioners, or the – sorry, the enforcement committee.

Now, the final row on the page, on the flowchart, tells us that the appropriate remedy will depend upon the purpose sought to be achieved, whether that be a punitive purpose, a protective purpose, a preservative purpose, a corrective purpose or a compensatory purpose. Is that right?---That is how it's drafted at the moment. And, again, I will just quickly add that this – this draft – and this entire document is under intense review with our internal review.

I understand that. But this is the current – the current system. I understand it's under review but I want to work with what your system is presently and the appropriate remedies are assessed depending on which of those purposes is to be achieved?---Again, this is a summary for brevity written in part for public understanding.

Yes?---But that is – that is how it is demonstrated on this particular slide, but if I remember correctly from the broader document – it goes into much greater detail – and I believe, if I remember correctly, other matters like deterrent – deterrent effect is also considered.

Yes. Within these categories. That's how the document approaches it. Within punitive, protective, preservative, corrective and compensation?---Yes.

Now, I want to ask you about these sorts of remedies listed in the line at the bottom of this page, but before I do that I want to ask you a bigger picture question. ASIC is required to publish an annual corporate plan?---That's right.

And in the most recent corporate plan that you've published for the 2018 to 2022 years, ASIC has explained that it has a performance evaluation framework that sets out how it's going to measure and evaluate its performance. Is that right?---That's right. And that framework, as I understand it, was developed after the capability review.

And ASIC uses, according to that corporate plan, both qualitative and quantitative measures to evaluate its performance?---Yes, that's right.

And what measures does ASIC use to evaluate its performance in relation to enforcement?---That is a matter that I have already identified that is, I don't think, prevalent enough in that particular document. And I have already issued guidance to the team that when we develop this plan next year that we should give more thought to the enforcement aspects of that report. So I agree with the premise of your question that there is an insufficiency of detail as regards our enforcement actions. If you wanted my observation on that corporate plan, from what I remember, implicit – implicit in the reporting is the enforcement outcomes, but I most certainly am of the view that it should be explicit moving forward.

So do you currently evaluate your performance in relation to enforcement with qualitative and quantitative measures as the corporate plan suggests that you do?---We do. That corporate plan is a plan that is produced specifically for the public domain.

Yes?---And what we are now doing is working on – and this is a body of work which will take some time, because it does – it does require, I think, some degree of engineering – is to develop a performance framework, not just for enforcement, but for our entire regulatory activities, that will better assess the performance of our enforcement teams, our regulatory teams, and every other team, because I – I do not think right now we have sufficient frameworks in place for that type of measurement and assessment.

So can I ask you to address my question about how you currently measure your performance in relation to enforcement with quantitative and qualitative measures. I understand you've got work to do and plans about what it might look like. How do you currently do that?---Currently, we have metrics which are produced on, I think, both publicly and – and internally about our enforcement outcomes. That is – that is our clear sort of quantitative assessment. And then we have an annual review as a part of our strategy planning whereby we do have feedback as – as the last stage of our annual planning cycle, our strategic planning cycle where each team, including the enforcement teams, will have to provide feedback on the – on their qualitative performance from the previous year. I will stop there, but I will say that I have – again, I have some comments on how those processes could be improved.

Well, what are the quantitative metrics that you currently use in relation to your enforcement?---As I mentioned before, the quantitative metrics are detailed delineations of the types of different proceedings that we pursue, and those metrics

were the metrics that I was, indeed, updating for the Royal Commission yesterday and amending in my witness statement.

I see. I just want to understand this in very simple terms, Mr Shipton. Do you have targets for the number of each type of enforcement outcome that you want to take or pursue in a – in a year. Is that what happens?---No. And this is the difficulty. It would be, I think, unwise to have targets in relation to enforcement outcomes. But those quantitative assessments are very informative as a guide, over time, as to where we are deploying our resources and our capabilities. And I think that is an important metric. I think another metric that we do, which is an internal on resourcing and staffing or – or activity, we monitor the amount of activity that we undertake in the enforcement space versus other parts of our organisation.

I'm sorry, Mr Shipton, I'm still struggling to understand. Are the quantitative metrics measures of the number of types of enforcement action that you take each year? Is that what you measure, presently?---Yes. Once again, we measure, year-on-year, the number of cases, whether it's a criminal case, civil matter, infringement notice, banning order – we measure that on a case-by-case notice and that is - - -

THE COMMISSIONER: I understand, Mr Shipton. You record what you've done. Let's go beyond the fact that you record what you've done during the period. How do you use the record of what you've done during the period?---That record then is assessed to reflect upon the usage of different types of tools, and I believe that that is a good metric to reflect upon, you know, the – the types of activity or the utilisation of, let's say, an enforceable undertaking versus a civil penalty. That is a retrospective guide for us to determine – to determine the future, and I think that's a very good benchmark. There are no targets. It is also a useful - - -

I just don't understand what you've told me, Mr Shipton. I really do not understand what you have told me?---Well, I apologise for any confusion. We measure, year on year, the different types of - - -

You record what you have done?---Yes.

I'm with you so far. What do you do with the record of what you have done. You look at it, you assess it, you reflect on it. I understand all of that?---Yes.

But what do you draw from the fact that this year, the numbers are so, and if we go back, as this chart does, back to 2011/12, we see how they go through each of the years. What do we then do – what do you then do with the data that is assembled in that way?---Well, as I said, that is – that, as I understand it, informs the team as to what has been allocated in previous years and in the past. But I will also add – and I know this wasn't part of the question but it's – it's important to understand – I don't think we do enough with those metrics, and that is why I have asked the team to do more thought and give more consideration to how we can better utilise statistics and metrics like this.

MS ORR: What is it that you should be measuring to evaluate your approach to enforcement, Mr Shipton?---Well, I think it starts with evaluation at the very – at the very start. And this is why, with apologies to the Commission, it's a complicated subject. Measurement of regulatory performance is a complicated area that every single regulator, in my experience, globally, has struggled with. And that is why I want our organisation to give advanced, world-leading thinking to what sort of assessment and measurement frameworks should be applied. Very quickly, because I know I need to be brief, we should be starting with how the financial system is improving and performing as regards fairness and equity towards customers and adherence to the law. Once we develop those metrics, then we – and assessments, both quantitative and qualitative, that will be a measure of our performance, because if we are using the tools that we're applying, we are helping that improvement in the overall financial system, that would indicate our regulatory work, our enforcement work is helping. If that is not taking place, then that would be indicating that it is not working and new ideas and methods and deployment of tools needs to be applied. This is a core part of what I am trying to do with the reform agenda that I'm trying to take place, because I agree with your line of questioning that we do not have, at this point in time, sufficient quantitative and qualitative methodologies to assess our overall and individual performance, and that is something I am very committed to addressing.

Mr Shipton, I want to turn to the remedies that you can pursue, again by reference to the items we see in the last line on this flowchart. That the last item in that last line is a negotiated resolution?---Yes.

Now, one form of negotiated resolution that we've heard a bit about in the course of the year, and which you and I have already discussed, is an enforceable undertaking. And I want to come back and ask you some questions about that particular form of negotiated resolution. But other negotiated resolutions don't involve an enforceable undertaking. They, instead, involve an agreement between ASIC and the entity that the entity will take certain steps and that ASIC will not take any further action if the entity takes those steps?---Yes. They are, from time to time, on a small number of occasions, entered into, yes.

A negotiated resolution is treated separately in this document from each of the purposes listed in the bottom line. It doesn't appear to be considered to be punitive, protective, preservative, corrective or compensation. What is the purpose of a negotiated resolution?---Well, I would – I would say that if that is the impression from this brief flowchart document, then that's not the correct impression, because a negotiated resolution is designed, and procedures – our internal procedures reflect this, to have one or a number of those elements embedded in it.

So broadly, in what circumstances do you say a negotiated resolution is appropriate?---Well, a negotiated resolution right now would only be appropriate if – if there is a demonstrable – there is a demonstrable – sorry, if there is not a clear need to pursue court-based enforcement outcomes, because, as I've said, we now, as of today, have a process that we will first look at a matter and say, "Why not litigate".

It's difficult for me to say, because this is all case specific, in what particular circumstances we would be addressing a negotiated outcome. It's very difficult for me to generalise.

I understand?---But – but I will say that there is a place for these types of arrangements, but I will also say that I have observed that we have over-utilised and over-relied on these types of outcomes, and that is exactly why we have different guidance now in relation to our enforcement procedures.

Under a negotiated resolution, an entity might agree to create a remediation program. Is that right?---Most certainly. That is – that is something that is a very common part of the – of the – of the arrangement.

And you tell us in your statement that since 1 July 2011 ASIC has negotiated a customer remediation program on 20 occasions?---Yes. I believe that's correct.

And you also say in your statement, you explain the lack of stronger enforcement action by ASIC in a number of specific matters that you dealt with in your statement by reference to the fact that ASICs focus had been on remediation. You make that observation in relation to the mis-selling of the credit card insurance, in relation to ClearView's mis-selling of life insurance and in relation to the NAB introducer program?---That's correct.

And in your view, has ASIC sometimes been too focused on customer remediation to the exclusion of enforcement action?---In some cases, yes. In some cases I clearly am of the view that we should have tried to and work towards running both remediation program and the enforcement investigation at the same time in parallel.

Now, something that a financial services entity might also agree to as part of a negotiated resolution is to pay a community benefit payment?---That's correct.

And that's most commonly done, it seems, as part of an enforceable undertaking?---Correct.

Is that a fair statement?---Yes, that's a fair statement, yes.

And what is the purpose of getting a financial services entity to make a community benefit payment?---The purpose, essentially, is to ameliorate the – the – the wrongdoing, and to provide a benefit to the community. It is, as I understand it, analogous to a community benefit order that we have under our legislation. And it is also – it is also a point that I personally believe provides some form of deterrent effect, because we are, in effect, making the organisation pay something that they otherwise would not have paid.

In exchange for not taking further action against the entity?---I would not describe it as an exchange, because that would connote that it's somehow a contract. What it is is an arrangement whereby a body of different responses, remediation, is one;

community benefit payments is another, but a tremendously important part of most – the vast, vast majority of enforceable undertakings is compliance programs and compliance improvement programs. So taken together, that is not an exchange, but that is the consequence of entering into a enforceable undertaking, because it does, and is designed, to have a consequence.

A different consequence from taking the entity to court?---Most definitely. And that's why, right now, we have a guidance and a process whereby we believe we should be asking ourselves whether or not we should be taking financial institutions to court and we are minded to use the enforceable undertaking tool less and court enforcement action more.

You tell us in your statement that since 1 July 2011 ASIC has negotiated a community benefit payment on 30 occasions?---Yes.

And the highest number in any one year was last year when ASIC negotiated 10 community benefit payments?---I believe that to be the case, yes.

And who are the community benefit payments generally made to, Mr Shipton?---Generally, they are made to non-government institutions such as financial counsellors and advocates. So I believe in relation to some superannuation-related matters we funded a superannuation consumer organisation. So these payments, again, go to ameliorating the – the misconduct and go directly to the – to a body or are designed to go to a body that would somehow ameliorate the misconduct and help in the future prevent or – and deter these types of activities again. May I just quickly add that I have also instructed the team that we need to look very carefully at the methodology and the processes around community benefit payments, and that forms part of our internal review.

In what way do you say that the payment of a community benefit payment ameliorates the misconduct?---I would say because, essentially, we are trying to – take the superannuation case, as I understand it, there was – and I can't remember the exact details of the party, but there was misconduct in the superannuation space. A community benefit payment was made to a superannuation consumer organisation. So since the misconduct took place in relation to superannuation, to try and make the entire superannuation sector better, making a payment to support an organisation that we will – we believe will help improve the superannuation sector and consumer – consumer – consumer engagement in that sector, that is what I would describe as a – an amelioration.

But you haven't always chosen an entity to receive the community benefit payment that has a direct link with the sort of conduct involved, have you?---That's – that is correct. Sometimes it's more industry-wide. The enforceable undertakings in relation to the BBSW case is funding a wider financial capability and financial literacy arrangement. But, again, I will emphasise that I believe we need to look very closely at our processes and procedures around community benefit payments, and we need to be taking financial institutions to court more often.

Do you know the average size of community benefit payments that have been sought by ASIC in recent years?---No, I do not know the – the average size, but, you know, they can range, from memory, from hundreds of thousands or thousands to – to millions.

You've exhibited to your statement a pilot study by academics at the University of New South Wales that was recently commissioned by ASIC, and that study provides some detail about ASICs practices in respect of enforceable undertakings. But in the course of the study, the authors interviewed a number of participants in the financial services industry about topics connected with enforceable undertakings, including community benefit payments. Are you aware of that?---Yes, I remember reading that – that – that paper.

And one respondent in that study expressed the view that community benefit payments provided the recipient with a more palatable way to acknowledge noncompliance than through a fine. And another respondent said that community benefit payments might be seen as a goodwill contribution to demonstrate an entity's goodwill towards fixing the problem. Do those sorts of observations concern you, Mr Shipton?---Yes, they would not be – they would not be the way that I would describe a community benefit payment.

But what if that is the way they are perceived by your regulated population?---And I agree, and that's why it – it has triggered a review and an instruction by me to look very carefully and closely at community benefit payments, and also look very carefully and closely at the utilisation of enforceable undertakings. So, yes, it is something we need to look at.

In the sixth round of public hearings in the Royal Commission, the Commission examined a case study in which ASIC accepted a community benefit payment without an enforceable undertaking from CommInsure. That's one of the cases that we asked you to reflect on in your statement. The community benefit was part of a negotiated outcome from December last year in response to advertising that misled customers about the circumstances in which a policyholder would be entitled to cover under a life insurance policy if they suffered a heart attack?---Yes.

And ASIC considered initially using infringement notices to deal with that conduct?---Yes. And if I remember correctly, we were timed out because of a – a 12 month limit.

Yes. So it was worked out within ASIC that that option was not available because you were out of time to issue an infringement notice?---Yes.

But before that, there had been some discussions with CommInsure about draft wording for an infringement notice before you appreciated that you were out of time?---I'm – I – I understand that to be the case.

And why was there discussion with CommInsure about the wording of an infringement notice to be issued by ASIC?---I do not know, and I do not have that – that detail at hand. But I will make the observation that an infringement notice is – it has to be voluntarily accepted by the – by the entity. It is not a – it is not – it is not something that attaches unilaterally to an entity. It has to be accepted. If it's not accepted, then that then triggers enforcement action, but the way that infringement notice is structured, as I understand it, it has to be accepted by an entity.

I want to understand what you mean by that, that an infringement notice has to be voluntarily accepted by the entity. An infringement notice imposes a penalty, an infringement penalty on an entity. And if the entity does not pay that penalty, they can be prosecuted for failing to pay that sum?---Correct.

So in what way does an infringement notice have to be voluntarily accepted by the entity?---Well, what I – apologies if I put it clumsily. My understanding is is that the way we operate with a infringement notice is that we want to get an indication as to whether or not they will accept and pay the infringement notice so as to be sure that that course of action is the right course of action. And that is why, as I understand it, generally – I don't have the specifics in this case – generally, our practice is to ascertain whether or not there will be an acceptance by that entity of the imposition of an infringement notice. And that is what I meant by – and I retract the word "voluntary" – but that is what I meant by that process.

Why do you do that, Mr Shipton? Why do you need to get an indication as to whether they will accept and pay it? The parking inspector doesn't seek an indication from the person he's giving a parking fine to as to whether they will accept and pay it. He just does it. Why don't you just do that?---My understanding from the team is that if there is an unwillingness to accept an infringement notice we would just go straight to court. In other words, what it is is trying to be as efficient as possible as we can with our limited resources, and so it is a matter that we apply, given the limitations that we have on our resources, but I can absolutely assure you if there is not an indication in that discussion – and, again, I don't want this to – to – to give the impression – and I fear it might be – there may be an impression that somehow we are sort of negotiating in a – in a cosy fashion these enforceable undertakings. What that – and pardon me, infringement notices. What we are doing is seeking an indication whether or not this is an efficient use of our time and resources, because once we issue an – issuance of an enforceable undertaking not only takes up the time of our enforcement teams, it then has to go to an internal delegate, and so there is a whole flow of procedure and resource usage that we need to ensure is appropriately and efficiently – sorry, efficiently applied.

What would you do if you wanted to issue an infringement notice and you said that to the entity and they said, "We won't accept it and we won't pay it"?---I – I have asked that question of the team, and they have said that they would pursue civil court enforcement issues. That's – that's my understanding. And that is certainly my instruction to the team, that if that happens, then that – if that situation is said back to us, then that would be the consequence.

I see. But the practice going forward will be to continue to seek an indication from the entity to whom you want to direct an infringement notice that they will accept it and pay it?---Yes. I would also add that right now there is an additional procedure in relation – or coming from our interim measures that we will – we will – we will have to check at the Commission level, particularly by our deputy chair for enforcement, we will check before any infringement notice remedy or action is pursued. And, again, asking the question before that process is embarked upon, why shouldn't we be going straight to court and not utilising the infringement notices process.

Now, I want to correct part of this discussion between you and I, Mr Shipton. The consequence, the statutory consequence of not paying an infringement notice is that ASIC can litigate the contravention. That's the statutory consequence of non-payment, not prosecuting for failing to pay the amount. Is that what you understand the case to be?---That's what I understood. And with that – thank you for that clarification. With that in mind, you can now hopefully better understand that what we're trying to apply is whether we just jump to - - -

I see?--- - - - that next step. Jump to that next step, which is the civil action.

And what are the cases – what are the criteria for identifying the cases where it's appropriate to take that first step and see if the entity will accept and pay the infringement notice?---Well, they should be – they should be – and – and we're tightening up the process – they should be minor matters, matters that – where there are mitigating circumstances. Again, I can't – this is very case specific, but put it generally, it should be a less serious matter.

All right.

THE COMMISSIONER: Well, the reason for that being the simple one that the infringement notice penalty is fixed, is it not?---I understand it to be so.

And I would have thought the critical question was whether the fixed penalty was an appropriate penalty for the contravention that was in issue?---That is one of the considerations, as I understand it.

Well, what other considerations would there be other than whether the penalty to be fixed is appropriate?---Well, I think it's also to do with the – whether the frequency, the willingness to – the willingness to respond and amend processes, the helpfulness and timeliness of the response of the entity involved, and mitigating factors like that that go to, in collection, to determine whether or not it would be appropriate. I will quickly add that I do believe that we need to and we have sharpened up our process and got tougher on our internal processes of when we apply infringement notices. And I have said in my witness statement we will be using that tool less often, particularly in relation to large financial institutions.

MS ORR: So coming back to the CommInsure case after you worked out that you couldn't use an infringement notice because you were out of time, ASIC then had to

reconsider its approach to dealing with that misconduct, and it decided to negotiate a resolution with CommInsure. And that resolution involved the payment of a community benefit payment?---That's correct.

Now, can I show you two internal ASIC email chains that show how this decision unfolded. Could we go to ASIC.0076.0006.5270. Now, at 5270 we see that in an email dated 21 September 2017, partway down the page, after it had become clear that you were out of time to use an infringement notice, Mr Mullaly, your senior executive leader of financial services enforcement said to Mr Saadat – you may have seen that from the email chain above – Mr Saadat being the senior executive leader of deposit takers credit and insurers, Mr Mullaly said:

> *We either resolve by way of an enforceable agreement with a community benefit payment of 250,000 or we push for a community benefit payment of 300,000.*

Do you see that?---Yes, I do.

And further up the page we see Mr Saadat's response – do you see in the middle of the page:

> *Yes, I think we start with 300,000.*

?---Yes, I do.

And then above that, up the top of the page, Mr Mullaly said:

> *Dear all, I spoke with James Myerscough yesterday and advised that we were generally in agreement with the proposed resolution. However, we could not issue infringement notices as we do not consider it is legally possible. I suggested that they should consider increasing the community benefit payment to take into account the lack of infringement notices. He was concerned that there was no "hook" upon which to found any agreement or resolution if there were no infringement notices.*

?---I'm afraid my screen has gone blank.

Yes. And mine, Mr Shipton.

THE COMMISSIONER: The service has resumed.

MS ORR:

Continuing:

> *I advised that the hook would be potential civil penalty action.*

Do you see that? I will take you back to that last paragraph:

> *He was concerned that there was no hook upon which to found any agreement or resolution if there were no infringement notices. I advised that the hook would be potential civil penalty action.*

?---Yes.

So we see from that email that CommInsure was concerned that there would be no infringement notice?---That – that would, on the face of it, appear to be the case. That would – yes.

But they agreed to consider whether to pay a higher community benefit payment to take into account that there was no infringement notice?---I was not part of this conversation but that is what is said on this email.

Do you have any observations about what we see from this email about the communications, Mr Shipton?---The observation that I understand is a broader context of another email chain, and I believe at least one telephone call, between NAB and Mr Mullaly which was trying to ascertain - - -

I think you may mean CMLA or CommInsure?---CommInsure. I – thank you for that correction. Yes. That there was a – a telephone conversation which was trying to ascertain what was the foundation or the grounding – I think that is reflected in the word "hook" – as to what would be the rationale or the grounding, the jurisdiction, as it were, in relation to the payment of the community benefit payment.

Because CommInsure was uncomfortable with just making a community benefit payment without a hook, without an infringement notice or some form of action. They were concerned about the perception of just making a payment to ASIC to make this go away?---I understand. I do not have the level of detail as to what was in the mind of CommInsure. But I do understand that they were trying to ascertain the jurisdictional hook in the absence of both an enforce – sorry, absence of both an infringement notice and, as I understand from a telephone conversation, the absence of an enforceable undertaking, what would be the foundation or the hook, which is the term used for that payment. That's what I understand to be the context of this exchange.

Well, I will take you to another email that makes CommInsure's concern clearer. First if I could tender this email chain.

THE COMMISSIONER: Emails of September '17 concerning CMLA advertising ASIC.0076.0006.5270, exhibit 7.69.

EXHIBIT #7.69 EMAILS OF SEPTEMBER '17 CONCERNING CMLA ADVERTISING (ASIC.0076.0006.5270)

MS ORR: If we could bring up ASIC.0076.0004.6951. We see an email from Mr Mullaly to Penny Beck at ASIC a few weeks later on 16 October 2017. You see that, Mr Shipton?---Yes, I can.

And at the top of the page we see that Mr Mullaly refers to an earlier conversation that he had had with James Myerscough. Now, James Myerscough is the chief risk officer of wealth management within CBA. Is that right?---I – I do not know his title but I understand him to be a senior executive there.

The nature of CommInsure's concern about paying a community benefit payment without an infringement notice becomes very clear from this email:

> *As you will recall, James Myerscough was concerned that by just paying a community benefit payment and not having any regulatory outcome, it looks like they are paying off ASIC to avoid action. He was hoping to see something from us about how this would be messaged. I intend to send him the following tomorrow morning to advance the matter.*

Now, how do you respond to that concern expressed by one of your regulated population, that by making a community benefit payment, CBA would look as though it was paying off ASIC to avoid action?---Extremely concerning.

Well, what does that say to you about the way community benefit payments are perceived by your regulated population?---It is concerning, and that is why we have – I have instructed that we need to be very disciplined moving forward about the utilisation of community benefit payments and non-court related agreements.

I will tender that email, Commissioner.

THE COMMISSIONER: Email concerning CommInsure advertising October '18, ASIC.007.0004.6951, exhibit 7.70.

EXHIBIT #7.70 EMAIL CONCERNING COMMINSURE ADVERTISING OCTOBER '18 (ASIC.007.0004.6951)

MS ORR: In your statement, Mr Shipton, you say that having observed the evidence that was given during round 6 of the Commission, it's apparent to you that ASIC should have considered whether a more robust approach was necessary with CommInsure in order to ensure an appropriate level of deterrence and public censure prior to agreeing to negotiate an outcome or as part of the negotiated outcome. You recall that from your statement?---Yes. Yes. Most definitely.

Why did the evidence in the sixth round of hearings change your views on this?---Because it is demonstrably clear to me, having not lived with this case, that this case was one that required, I believe, a more robust public denunciation of the

overarching conduct. And it also triggered, as the NAB case study yesterday, it's a very good example of why we need to and we are improving our guidance and processes around our enforcement decision-making.

Was there any evidence adduced in that case study in the sixth round of hearings that ASIC didn't already know about?---I cannot comment with any certainty on that because I haven't asked that question, but I would imagine that the gravity of the situation was known to us, and that is why, as I've said before, it was a mistake not to act quicker, swifter, and earlier.

You say in your statement that ASIC should have sought a stronger public admission of wrongdoing from CBA. Do you recall that?---Yes, I do.

And what do you mean by that, an admission that ASIC could have referred to in a media release?---Yes. Both in a media release and – and more generally. I think a public denunciation has tremendous deterrent effect because it goes – it impacts upon the reputation of the institution, and that is something that we should have done in a more robust fashion.

And what if CommInsure wasn't prepared to give you that public admission of wrongdoing, as the evidence suggested they were not at that time prepared to do?---Well, let me answer that question as of today. If this situation came to us today, I would be asking the team why are we not just going to court with very robust responses in relation to this. And if we decide not to, then we need to have very strong, very clear admissions of wrongdoing and responsibility in relation to these matters. And this is another point of instruction and guidance for the team, that if we are – if – if we are to enter into any agreements, or enforceable undertakings, then we need, as a starting point, to have a clear admission of wrongdoing and/or responsibility – and responsibility moving forward.

Do you intend to continue to try and resolve matters going forward on the basis of a community benefit payment?---I've – I've asked – I've asked the team to look very seriously at the utility of community benefit payments, but more broadly, what I've asked the team to look at is the utility and the appropriateness of enforceable undertaking and similar arrangements, given the fact that it's very clear to me that we need to be more agile, willing and faster in applying court-based enforcement actions.

Does that answer mean, Mr Shipton, that you don't know if you are going to continue to try and resolve matters on the basis of a community benefit payment?---That – that means that it is under review right now. It also means that I have asked for more discipline, structure, and rigour around community benefit payments. But one – when one is reviewing community benefit payments, it's not just in isolation. It is, as I've mentioned before, in relation to these enforceable undertaking arrangements, it is a combination of different matters that are included in that arrangement. As I said, remediation, compliance improvements, community benefits payments. What we are doing is looking – is looking at that together,

separately and collectively. So, yes, we are looking at community benefit payments. I am disturbed and worried about some of the descriptions of – that you've referred to of the community benefit payments. That is very disturbing to hear. But I also refer to that University of New South Wales study, that also points, if I remember correctly, to the fact that taken as a whole, that there is – there is early indications, or at least some indication that the entire enforceable undertaking arrangement does have a deterrent effect. As I said, taken as a whole. And I think it's important to look at both a community benefit payment process in isolation, which we're doing, but also in combination.

ASIC issued a media release about the negotiated outcome with CommInsure, didn't it?---They did, yes. We did, yes.

And when ASIC reaches a negotiated resolution with a financial services entity does it tend to issue a media release about that outcome?---Yes, that is the usual protocol.

And why? What is the purpose of that, Mr Shipton?---The purpose, in part, is – is deterrence, denunciation, and indication as to – indication as to the matter at hand, and our – and – and our reaction to it.

So those purposes of deterrence and denunciation will only be served if what it is that you're publicising is something that is perceived by the public to have a deterrent effect and to involve denunciation of the conduct. Do you agree with that?---I most certainly agree with that.

And you tell us in your statement that since 1 July 2011 ASIC has issued 1222 media releases in the course of or as a result of a formal investigation conducted by an enforcement team?---Yes, that's right.

And the number of those media releases, according to the table in your statement, has tended to be between about 140 and 180 a year?---Yes, I believe that's correct.

Now, when the media release is announcing that ASIC has negotiated a resolution which the entity has agreed to, do you say that that achieves denunciation of the conduct?---I believe that in – in some occasions it does. But we need more robust procedures around enforceable undertakings to ensure that we are clearer and more forthright in our denunciation of the wrongdoing because there are, from my understanding of the processes, there – and the history, that the denunciation hasn't been strong enough and has not been forthright enough.

Well, what do you say to the proposition that the message that is being sent is that if another entity engages in that sort of conduct, they too will be able to negotiate an outcome with ASIC?---Well, that's not the message that we want to send and, again, that is why we are applying procedures that now, in effect, that we hope will arrest that problem.

Well, in the case study involving CommInsure that I've been asking you questions about, the terms of the media release, your media release, were the subject of negotiation with CommInsure?---That was a mistake, but I also understand that – and there are many lessons to be learned in this particular case study – I understand in that case study, what happened was there was a conflation of documenting the arrangement with what the media would – media release would look like. In other words, instead of an understanding memo or a drafting of an engagement memo which should have happened, instead, the focus point for determining what the arrangement would look like was through the prism and through the medium of the media release. That was inappropriate. That was wrong. That should not have happened. And, again, we now have processes and procedures that that won't happen again.

You tell us in your statement that ASIC generally communicates with the affected party its intention to issue a media release in relation to the outcome of an investigation before issuing the release?---Correct.

Why do you do that?---We do that now because we want to ensure that anything in the media release is factually correct. Please do not conflate the case study that you've just referred to with current practice. Current practice is very different, radically different to that unfortunate case study. All we do now is check for factual accuracy. Oftentimes, that is motivated, again, by just fairness and – and – and being a model litigant, as it were, or a model agency, but also in relation to listed corporations, factual inaccuracies of media releases relating to enforcement outcomes or enforceable undertaking could have market consequences, market movement consequences. So it is very important that we be factually correct.

So since when has it been the practice to only discuss the content of the media release for the purposes of confirming factual accuracy? When did that start, Mr Shipton?---Well, that should have started, from what I understand – from what I understand the guidance a number of years ago, but that – that is a very clear instruction that I have had throughout my nine months at ASIC that we do not negotiate the terms of a media release. We do not negotiate the terms of media release. We will check the factual accuracy of a media release. Nothing more than that.

So that's something that you say has become the practice, the position in your time. Is that right? Because to the extent that there was guidance before, it was clearly not effective?---In this particular case, I grant that there was a conflation and that shouldn't have happened. There should have been a different process applied. The people involved in this case do recognise and realise that. I can't speak to if there are any other examples. I'm not aware that there are any other examples. All I can speak to is the rigour, the discipline that I have impressed upon the team that we will not negotiate media releases.

All right. So that's a change in practice?---And that – if I may, when you speak about change in practice, it highlights the point that this is an important time in

ASICs existence to have a rigorous look at not just the procedures but the practice to make sure that our practices are first class.

And this was not a first class practice. Do you agree, Mr Shipton?---As I've said, this was a mistake. This was not first class. And – and I believe, and the team believes, that there are very valuable lessons to be learned from this case study, and the NAB case study, and no doubt other case studies that you will bring me to, and I am very motivated, very committed and very dedicated to learning those lessons.

THE COMMISSIONER: I just wonder whether this reference to factual accuracy and checking factual accuracy may not benefit from a little unpacking, Mr Shipton. When you're making a media release about the outcome of a resolution of a regulatory matter, do you not begin from what it is that ASIC alleged?---Pardon me, Commissioner, I don't quite follow the question.

There are not only – is there anything more than two or three things that are going to form the basis of a media release recording the final resolution of a regulatory matter? What ASIC alleges, what the entity admits, and what the outcome is?---There's also background to – there's background in – in a note. There's often a background to the note of the media release that talks about dates and times of – of what happened, when it happened. We're also checking, for instance, making sure that we've got the legal names right, and that sort of factual accuracy. There is not – there is not – for the avoidance of any doubt, there is not checking of the factual accuracy of the misconduct, the contravention, or the denunciation. What I'm talking about is dates – names, dates, and times.

Exactly. And those are matters which are at the core of what ASIC alleges?---Correct.

And ASIC should know what it alleges. Is that right?---Correct. And - - -

And it should know what the entity admits. Is that right?---Yes.

And there should be no controversy about either what is alleged or what is admitted. Is that right?---Correct.

And there should be no controversy, therefore, about what you describe as "background". Would you agree with that?---There shouldn't be but we want to make sure that we are applying a final check, as it were, as to that accuracy.

Yes?---And, again, I – I want to just emphasise, Commissioner, if I may, that this is all about ensuring the factual accuracy about what we're saying, and in my observation, in my time, there has not been any amendments made – and you're absolutely right, we have been accurate about what we do. The background to this, if I may, is an unfortunate story coming out of the United Kingdom involving the FCA where there was, as I understand it, factual inaccuracies. And as a consequence of that, many regulators, ASIC included – and I remember when I was in Hong Kong –

was having a look at that case study to just put robust procedures in place to ensure that accuracy.

Yes.

MS ORR: Mr Shipton, I want to talk now about enforceable undertakings, a particular species of negotiated resolutions. And could we start by you explaining what the purpose of an enforceable undertaking is?---The purpose of an enforceable undertaking is an alternative to court-based enforcement actions to – I use the expression "package up" a range of different possible resolutions, remediation, compliance improvement programs. We've discussed community benefit payments before. Package it up into – into an undertaking in the interests of timeliness, swiftness, and – and efficiency in trying to get all of those aspects and other aspects and behavioural change in one document, in one fell swoop, as it were.

What sort of misconduct do you say is appropriately dealt with by an enforceable undertaking?---Well, it's – it's difficult, again, to generalise because an enforceable undertaking, like other aspects, is case specific.

Could I ask you about on a spectrum of seriousness of the conduct, at what end of the spectrum from very serious to not very serious is it appropriate to use an enforceable undertaking?---Well, to generalise, and of course it's always dangerous to generalise, it would be somewhere in the middle.

Somewhere in the middle of the spectrum?---Middle – middle to serious nature of the spectrum, because, of course, we have a very broad spectrum in relation to the tools that we can apply and use.

Again, you give us some statistics in your statement. You tell us that since 1 July 2011, ASIC has negotiated 121 enforceable undertakings after formal investigations conducted by your enforcement people. Do you enter into enforceable undertakings other than following a formal investigation by an enforcement team?---Yes. I understand that there can be enforceable undertakings entered into by the surveillance team. May I just sort of amend that generalisation before, because, of course, there are exceptions. There has been some enforceable undertakings which have been part of a broader court settlement in relation to matters which are very serious. So I think of the BBSW case, for example, or the BBSW cases, where there was a package of very serious matters. And one part – one part of – of – of that settlement, that court settlement, were enforceable undertakings. So I just qualify my generalisation with that statement.

In your statement you refer to enforceable undertakings as representing relatively timely and proportionate regulatory outcomes in respect of less serious conduct?---Yes.

So do you – which is it? Is it less serious end of the spectrum or middle to serious end of the spectrum?---Middle to serious. Middle to serious. As I said, there was a

qualification to the generalisation. As I said, the – in – in relation to my first response, the spectrum is very wide.

Yes?---And so I think my – my spectrum generalisation, again, qualified by some exceptions which I pointed out, stands.

So why did you refer to them as being used for less serious conduct? What were you intending to convey by that in your statement?---I was intending to convey that it's not the most serious of conduct, nor is it the least serious of conduct.

I see. Now, the pilot study that you've exhibited to your statement, which I asked you some questions about earlier, gives an overview of the types of potential contraventions that have most frequently been the subject of an enforceable undertaking?---Yes, I recollect that.

And the time period examined by that study was different to the period that we asked you to address in your statement, and the study wasn't explicitly confined to enforceable undertakings following a formal investigation, but do you agree that, otherwise, the parameters were broadly the same?---Could you elaborate on that – on that statement?

Well, I – I want to compare the information that you've provided about enforceable undertakings in your statement with the information in that study. And I'm asking you whether or not you accept that the parameters of what we asked you to explain and what you asked the academics to explain were broadly the same?---It – would it be possible to quickly glance at that study because it's - - -

Of course?---It's – I – I would like to comment with certainty.

Yes. ASIC.0800.0016.0317. The part that I want to take you to – and perhaps you could consider my question in light of these pages – is 0322 to 0323. We see there that the study indicated in 323 – I think, I'm sorry, we've just lost the numbers from the top of the screen – on the right-hand side – I think I need to take you, I'm sorry, one page further in to 0324. Yes, that was the page I was looking for. That the study indicated that about 58 per cent of enforceable undertakings obtained by ASIC related to conduct in financial services. I'm sorry, if we could – if you see that from 323, firstly, and then I will take you to the table on 324. Do you see that figure up the top of 323, 57.6 per cent relate to conduct in financial services?---Yes.

And about 15 per cent related to conduct in consumer credit?---Yes.

Bringing the combined figure of financial services and consumer credit enforceable undertakings to about 73 per cent of all enforceable undertakings?---Yes.

Now, of the enforceable undertakings given in respect of financial services and credit activities, I want to put to you that 0324 shows us that many related to serious conduct?---It – it's – it's difficult to extract from that table.

Let's do it step-by-step, Mr Shipton. We see from this table that about 36 per cent related to:

> *... providing inappropriate advice and/or deficiencies in an organisation's systems to train or supervise representatives.*

Serious matters?---Serious matters, but we are – we are providing a headline here because, of course, even – even though there could be – and I don't – I don't know the details of this study, so I can't speak with – with great expertise of the underlying matters in this study, but what I can speak to about is that, yes, on the face of the – on the face of the – of the column that you're referring to, yes, they are serious matters. But, of course, there is the underlying case – there, of course, is a spectrum of seriousness in relation to the underlying cases that make up this – this study, which – which I don't have knowledge of.

No. And nor do we, Mr Shipton. This is a study that you've put forward in your statement. Neither of us have the underlying data but we have the results. And you would not suggest, would you, that providing inappropriate advice or having deficient training or supervision systems of representatives was a not serious matter?---No, of course I would not say it is a not serious matter.

And we see about 16 per cent of enforceable undertakings related to breaches of section 912A of the Corporations Act, excluding the supervision deficiencies?---Yes, that's right. And if I may make an observation in relation to 912A, the utilisation of enforceable undertakings is utilised to a great deal in relation to 912A matters because 912A currently does not have a penalty that attaches to it. And so, therefore, there is great utility in applying an enforceable undertaking approach to provide some form of better redress that the current penalty regime does not have, but soon will have, and because there soon will be meaningful penalties to 912A, I expect that there will be a decline in the utilisation of enforceable undertakings in relation to 912A matters.

But you accept that a breach of 912A is a serious matter?---As a starting point, I agree with that, yes.

And eight per cent related to providing consumer credit without a licence. Another serious matter?---Correct.

And about 10 per cent related to not making reasonable inquiries when entering into consumer credit contracts and deficiencies in training or supervision systems. Do you see that?---Yes, they're all – they're all serious matters.

Well, about seven per cent related to misleading or deceptive conduct. Another serious matter?---Yes.

So in your view, is it appropriate – and I heard what you said about the 912A penalty – so if we could leave that to one side for now – is it appropriate for enforceable

undertakings to be used by ASIC for contraventions of this nature?---Well, assuming, for the purposes of – of your discussion and our discussion that these – these serious matters also have serious underlying facts and serious underlying circumstances, I would agree with the premise of your question that we should be asking – we should – we should not be relying on enforceable undertakings and that's exactly what the processes and procedures we now have in place to capture this concern that you raise.

I want to ask you about a particular enforceable undertaking that ASIC obtained from NAB at the end of 2016. This is one of the matters that we asked you to reflect on in your statement. Could I take you to RCD.0006.0016.0022, which is a copy of a media release in relation to this matter. We see from this media release that in late 2016 ASIC accepted an enforceable undertaking from NAB in relation to its wholesale spot foreign exchange business?---Yes.

An enforceable undertaking in relation to similar matters was accepted from CBA on the same day?---Yes, it would appear so from that – from that press release, yes.

And the conduct that underpinned the enforceable undertaking is set out in the three dot points under the heading NAB, about halfway down the page. If we could blow those up. We see that:

> *On several occasions, a NAB employee on an offshore spot foreign exchange desk acting together with an employee of another Australian bank shared confidential information and entered offers into the trading platform without any apparent legitimate commercial reason for placing the offers. And on a number of occasions, NAB employees disclosed specific confidential details of pending client orders to external market participants, including identification of the client through the use of code names; and on several occasions NAB employees on an offshore spot foreign exchange desk inappropriately exchanged confidential and potentially material information about the bank's client flow or proprietary positions.*

Do you see that?---Yes, I do.

And underneath this, we see that having identified this conduct, ASIC was concerned – if we could blow that up:

> *Concerned that NAB did not ensure that its systems, controls and supervision were adequate to prevent, detect, and respond to such conduct, which had the potential to undermine confidence in the proper functioning of the market.*

?---Yes.

Now, in your statement you make some observations about the process by which ASIC decided to enter into this enforceable undertaking with NAB. And I want to go to that. I will tender this media release first.

THE COMMISSIONER: ASIC media release 16-455MR, exhibit 7.71. It's ASIC.0006.0016.0022.

EXHIBIT #7.71 ASIC MEDIA RELEASE 16-455MR (ASIC.0006.0016.0022)

MS ORR: You tell us in your statement that the NAB foreign exchange matter was led by ASICs market enforcement team from the commencement of initial inquiries through to formal commencement of the investigation, and the acceptance of the enforceable undertaking. That's paragraph 266 of your statement, Mr Shipton?---Yes.

And you say that the investigation team, in conjunction with the senior executive leader for market enforcement, and one of the Commissioners, recommended to the enforcement committee that ASIC enter into an enforceable undertaking with NAB?---Correct.

And the relevant Commissioner was Ms Armour, and she had, in your words, "ultimate responsibility for the conduct of the matter"?---Correct.

Now, while Ms Armour was responsible for the conduct of the matter within ASIC, did she discuss the matter with senior representatives of NAB?---I'm not aware.

From the documents that you reviewed in reflecting on this matter for the purposes of your statement, did you see any documents recording discussions between Ms Armour and senior representatives of NAB?---Not that I can recall.

You don't recall seeing any documents recording discussions between Ms Armour and Mr Gall who was then the chief risk officer of NAB?---Yes. And I'm now recalling. Thank you for that prompt, yes.

All right?---Thank you for that prompt, yes.

Could I take you to an email from Ms Armour to others within ASIC that summarises a conversation that she had with Mr Gall during the investigative phase of this matter in August 2016. ASIC.0089.0004.1051. Now, we see this was an email from Ms Armour to a number of people within ASIC. And Ms Armour says:

> *David Gall and I had a telephone conversation this morning. David asked that the conversation be on a without prejudice basis – with which I agreed. David explained that he was interested in just confirming the basis on which ASIC may entertain a proposal from NAB to settle the matter. Apparently, the FX investigation has had a degree of attention internally at NAB including at its board level. David said that the bank team understood from the 18 May meeting and subsequent conversations that ASIC was inviting NAB to put a*

proposal to it for an administrative outcome. He wanted to confirm that this was correct.

Now, just pausing there for a moment. Was it common, to your knowledge, for Commissioners to discuss enforcement proposals directly with senior representatives of banks during an investigation in this way?---At that time, yes.

Do you have any observations to make on that practice, Mr Shipton?---Well, that practice is changing because I believe that the Commissioners should be stepping out of – this would be a day-to-day operational matter in relation for enforcement and I believe that the Commissioner should be stepping out of these discussions and leading – and leaving them to the executive responsible.

And why do you believe the Commissioners should be stepping out of these discussions?---Because I believe that the Commissioners should be providing a strategic direction and guidance role, and we've discussed some of the case studies where I believe that was lacking – lacking, and I also believe that the Commissioners should have a role of providing a objective checking and challenge of decisions being made by the executive team. The conflation of strategic decision-making, oversight and direct – and direct operational matters, I think, is not optimal, and that is why we're changing our structure.

What do you mean "the conflation is not optimal", Mr Shipton?---In my experience, if I could step out of this case study – in my experience, having had a role previously in a previous – in a previous role as a regulator, I saw and observed that when you have Commission-like – Commission-like positions with executive responsibility, there was a degree where objectivity was lost because of closeness to the matter at hand. What I believe is best practice for a regulatory agency is to have distance between the strategic oversight, the strategic direction, that being separated and distinct from the operational day-to-day management of matters. This, I understand, is consistent and aligned with the capability review. So stepping back into this case study, this type of scenario, moving forward, would not happen.

I see. Well, stepping back - - -

THE COMMISSIONER: Well, it wouldn't happen at that level?---It wouldn't happen at that level. There would be engagement.

But the officer having primary responsibility for carriage of the matter and initial decision rights would be the person who would have a discussion of this kind. Is that what I'm to take from your evidence?---It would be more appropriate for that person to have that discussion, yes.

So we're not debating whether the discussion should have happened, we're debating who should have it?---You will hear some comments about the case study in – in – in a moment, no doubt, from Ms Orr's questioning, but I – stepping out of the case study for a moment as regards those discussions, general discussions by a senior

executive leader or what we are now constituting an executive director, that should be done with absolute professionalism and highest professional standards in mind. And also, pursuant to guidelines and guidance that we are issuing and plan to issue in relation to how matters like this are conducted, particularly when it comes to enforceable undertakings.

MS ORR: I want to direct you to some other parts of the email, Mr Shipton, and ask you to consider whether the problem here is a lack of professionalism, or whether there are different problems that appear from this email, because Ms Armour goes on to say:

> *My response to David was that the proposal and its nature was a matter for NAB but I thought we would be willing to consider a proposal along those lines depending on its content. I did say to him that, given the relatively early stage of the investigation, we would be willing to consider a proposal that did not involve a court outcome if it otherwise met our key regulatory outcomes. I did urge him, though, to put a proposal to us shortly. I explained that the longer investigations go, the more prospect of us developing case theories more definitely and there can be a risk of there being entrenched positions which would limit our flexibility on outcomes.*

Now, can I ask you to reflect on whether anything about that response by Ms Armour, a Commissioner of ASIC, to Mr Gall, is problematic beyond a lack of professionalism?---I – I just want to be absolutely clear that I firmly believe in Ms Armour's professionalism at all times and that shouldn't be in any doubt in this case study - - -

THE COMMISSIONER: You were asked a question, Mr Shipton. If you would be good enough to answer it?---Yes, of course. I just wanted to clarify. I will, sir. The back – can I give you, from what I understand, to be the background - - -

No, can you put the question again, Ms Orr.

MS ORR: Well, I was asking you to reflect, Mr Shipton, on whether the communication by Ms Armour in response to the approach from Mr Gall reflected far greater problems than concerns about professionalism?---No. And the background and context is important, because the background and context to this discussion, as I understand from Ms Armour, is that at that particular point in time there was not a great degree of confidence that outside 912A actions, that there was sufficient evidence or legal hook, as it were, to pursue the other matters. And that – that is the background and context. Yes, as I understand it from Ms Armour, we were prepared and willing to continue with the investigation, but at that point in time – and I might add, at that point in time we had spent millions of dollars looking at not just the FX issue, but also the BBSW issue, because it's the same business, same – happening at the same time. And we, as I understand it from the team and Ms Armour – we went out and got a whole range of legal advice, and there was not the degree at that point in time of sufficient confidence. And, therefore, what Ms

Armour was doing was exploring how we could come to an arrangement in relation to this matter by way of an enforceable undertaking.

Well, Mr Shipton, what Ms Armour went on to say here was that she said to Mr Gall – and I'm reading three paragraphs from the bottom now:

> *I said that we will continue our investigation and there would be a risk of us developing more information and forming views on different outcomes in the meantime. So encouraged David to have his team come back to us as soon as they could with a proposal. He asked me to let him know if we had an issue (beyond the warning I had given him on investigation risk) with the early September timetable.*

Now, the Commissioner was telling NABs chief risk officer that if the investigation progressed there was a chance that ASIC would uncover evidence of serious misconduct which would render a weaker remedial outcome inappropriate. That is what she was referring to when she referred to investigation risk. What do you say to that, Mr Shipton?---Well, she's referring to – she doesn't – she's referring to more information and forming different views on outcomes. She doesn't use your expression which is the word "serious". And, again, I do think the background and context was is that there was a very clear willingness to conclude – sorry, willingness to continue the – the investigation which could – could, as I understand it, from the team, could have formed views of different outcomes. But at that particular point in time, given the resource constraints, given the very large BBSW case at hand, a decision was made – and I think it's the right one on the back of not just one counsel, senior counsel, but a whole series of senior counsel, that at the time of this email that there wasn't a high degree of confidence that further – further investigation would lead to different outcomes, even though there was a willingness and a possibility to do so. So that is the context in which that discussion was had.

Well, what Ms Armour said to Mr Gall, as recorded in this email, was that if Mr Gall wanted to make an offer, he better do it quickly because otherwise the investigation might progress to a point where misconduct was uncovered to an extent that a deal of this nature could no longer be done with Mr Gall?---We're reading a lot into – into that paragraph. And, again, I wasn't part of the conversation, but my understanding of this conversation with – with – between Ms Armour and Mr Gall – and, again, this is all hearsay because I'm only receiving it second-hand – was there was a clear willingness on our part to continue with the investigation. But equally, what we clearly didn't say or Ms Armour didn't say to Mr Gall at that particular point in time was that there wasn't overwhelming confidence that the continuation of the investigation would come up with anything. And, therefore, she put – she put the – the – the matter to Mr Gall in strident terms.

Well, I want to suggest to you that the appropriate way to handle this situation would be to complete your investigation, form your views about what an appropriate outcome is on the basis of the completed investigation, and then use whatever measures are available to you to pursue that outcome. That is not what happened

here, is it?---The investigation, as I understand it – of course, investigations can continue and can continue and can continue. The investigation was plateauing at this particular point in time. And I take your point - - -

THE COMMISSIONER: Plateauing when it's described as the "relatively early stage of the investigation". That's what appears at line 3 on the screen, "relatively early stage of the investigation"?---Could I have a look at that, because I – my understanding - - -

Line 3 of the screen?---It was my understanding – my understanding – and I can't spoke to that line – my understanding is that the – the issue was – the issue was plateauing, and there wasn't a high degree of confidence as regards what else would be found. I cannot explain that line.

MS ORR: Commissioner, I will tender that email.

THE COMMISSIONER: Email concerning NAB FX 10 August '16, ASIC.0089.0004.1051, exhibit 7.72.

EXHIBIT #7.72 EMAIL CONCERNING NAB FX DATED 10/08/2016 (ASIC.0089.0004.1051)

MS ORR: Commissioner, I wonder whether it might be an appropriate time to have - - -

THE COMMISSIONER: Just before we do - - -

MS ORR: I'm sorry.

THE COMMISSIONER: - - - could we go back to ASIC.0006.0016.0022, the media release. 0006.0016.0022. The answer to my question is no, we can't. Now, the three bullet points underneath:

ASIC identified the following conduct.

Do those three bullet points, as you understand it, represent reasonably accurately the state of ASICs knowledge at the time of the issue of the press release?---To my knowledge, yes.

The press release was issued on what date?---I can't see it on my screen, Commissioner.

MS ORR: If we – if we pan back we can see the date above the heading Wednesday - - -

THE COMMISSIONER: 21 December.

MS ORR: - - - 21 December.

THE COMMISSIONER: And the email from Ms Armour was 10 August '16. Is that right?---I believe so.

We knew – ASIC knew at or about the time of Ms Armour's conversation with a representative of NAB that the conduct being examined was of a kind described in the three bullet points. Would you accept that?---Yes, I would.

Yes. Thank you. Ms Orr.

MS ORR: Perhaps if we could have a brief adjournment, given that this is a long session for Mr Shipton in the witness box, and a break - - -

THE COMMISSIONER: If I come back at 11.20.

MS ORR: Thank you, Commissioner.

ADJOURNED **[11.13 am]**

RESUMED **[11.20 am]**

MS ORR: Now, the - - -

THE COMMISSIONER: Yes, Ms Orr.

MS ORR: The email that we were just discussing, Mr Shipton, took place – recorded conversations from August 2016. You will recall that the media release was from December 2016. We know from your statement that the enforcement committee considered the NAB foreign exchange matter on 14 November 2016. We see that from paragraph 268 of your statement?---Yes.

And the enforcement committee decided to accept a recommendation to resolve the matter with NAB by entering into an enforceable undertaking?---Yes.

And in your statement you say that ASICs acceptance of the enforceable undertaking in this case was not unreasonable?---Yes.

And is that as high as you would put it, not unreasonable?---That would be as high as I would put it, yes.

You would not say it was reasonable?---I was using the expression yesterday that there is a spectrum of reasonableness, and it is on the spectrum of reasonableness.

Sorry, it's on the spectrum of reasonableness?---Yes.

You might have to explain that to me, Mr Shipton?---Well, what – what I'm saying is that under the – at the time and the circumstances of the case, remembering that we were spending at that stage, millions of dollars – millions of dollars on the investigation. By way of background, we ended up spending $45 million on the BBSW investigation and action. So this was sort of a part, it was an expensive part, it was international, it was multi-jurisdictional, it was expensive, it was intense. BBSW was taking place at the same time. So I would agree that – and, again, I – I was not there at the time, so it's difficult for me to put myself in that position then, and, therefore, I need to qualify my observation as to the decision, because, as I said, I – I just wasn't there at the time. I would hasten to add – I would hasten to add, again, the processes and procedures that we have right now are very different to what existed in 2016.

I want to show you the enforceable undertaking that ASIC entered into, Mr Shipton. It's ASIC.0089.0004.1062. Now, if we turn to 1067. We see at paragraph 2.15 that the enforceable undertaking set out ASICs concerns. Do you see that?---Yes, I do.

That NAB had:

> *Failed to comply with its obligations under section 912A(1)(a) of the Corporations Act by failing to ensure that its systems, controls, training, guidance and framework for monitoring and supervision of employees in its spot foreign exchange business were adequate to respond to various forms of misconduct.*

?---Yes, that's right.

And at 2.18 over the page at 1068, we see at 2.18 that:

> *NAB acknowledged ASICs concerns and that they are reasonably held and offered an enforceable undertaking in the terms set out below as a resolution of ASICs concerns.*

Do you see that, Mr Shipton?---Yes, I do.

And if we turn to 1069 and we bring up 3.5, we see that by the enforceable undertaking, NAB undertook to do various things, including to develop a program of changes. We will need to pan back. If we could just have the entirety of 3.5 brought up:

To develop a program of changes to its existing systems, controls, monitoring and supervision of employees within its foreign exchange business to prevent, detect and respond to conduct –

Particular types of problematic conduct. And that program was to be developed and provided to ASIC and an independent expert by 30 June 2017?---Yes.

And if we turn to 3.7 at page 1071, we see in 3.7 that the:

The independent expert was then to assess the effectiveness of the program –

The program that NAB was required to develop –

assess the effectiveness of that program to prevent, detect and respond to the particular types of problematic conduct.

And the independent expert was to provide a written report about any deficiencies in the program to NAB and to ASIC?---Yes.

The independent expert was to be appointed by ASIC?---Yes.

And if we turn to 1073 we see at paragraph 3.17 that NAB was also required to make a community benefit payment of $2.5 million to Financial Literacy Australia:

to fund the advancement of financial literacy in the aged care sector, including by providing assistance for aged care financial consumers with cognitive difficulties and the promotion of ethical behaviour in Australian financial markets.

How did – how did that come to be the place to which the $2.5 million community benefit was directed, Mr Shipton?---I do not know the exact rationale for the choice of – of Financial Literacy Australia, which is, of course, a fine organisation, but as regards its choice, I'm not aware of, and I'm aware of the concern that is a premise of your question and I'm doing my level best to address it.

What do you understand the concern to be that is the premise of my question, Mr Shipton?---The – with apologies, I'm jumping ahead of myself. The determination of what organisation receives the community benefit payment.

Yes. Well you referred earlier to community benefit payments having a purpose of ameliorating the particular misconduct being addressed. Was this a community benefit payment that ameliorated the misconduct in NABs spot foreign exchange business?---May I step out of the case study for a moment?

I would be grateful if you could answer that question in relation to the case study first, Mr Shipton?---It's difficult for me – it's difficult for me to comment on the – because I do not know what other agencies or organisations were out there. And this

is why I wanted to step out of the case study, because I do understand that as the procedures apply probably – or – you know, probably applied at that time, that absent – absent a direct – a direct or referable organisation for the misconduct, then another suitable or another alternative would be found. I can only imagine – and this is now conjecture, but knowing the spot FX market and knowing that it is indirect to the consumer, as in the retail consumer, that the thinking was – and this is only conjecture – the thinking was to – to find a – an alternative or a proxy, but that is pure conjecture, and that's why I requested to step out of the case study.

So you're unable to explain why the community benefit payment in this enforceable undertaking was directed towards the advancement of financial literacy in the aged care sector?---I'm unaware. I can only observe – I can only observe that I can imagine that it would be difficult to find a equivalent organisation that is referrable to the spot FX market, which is very wholesale, very international and very institutional.

And therefore, Mr Shipton, very difficult to use a community benefit payment to ameliorate this particular misconduct?---I agree with you. And that is exactly why we're looking exactly at these types of issues.

Now, the independent expert who was to receive the program to be developed by NAB and assess the effectiveness of that program was Promontory. Is that right?---Yes, I believe so.

And NAB provided its program for assessment by the independent expert in November 2017?---Yes, I understand that.

And at the end of March 2018, Promontory provided its independent expert report on phase 1 of the program that NAB had developed pursuant to its undertaking under the enforceable undertaking?---Correct. On that phase 1 program, yes.

And that report identified significant deficiencies and explained that NAB had not yet designed items to be included in the program so its effectiveness was not even able to be assessed?---Yes, there were, as I understand it, deficiencies in that program which is the remediation program, as in the improvement program, and the design of that improvement program.

Now, I want to take you to a presentation that Promontory gave to ASIC and NAB in April, but first I will tender the enforceable undertaking, Commissioner.

THE COMMISSIONER: Enforceable undertaking of NAB ASIC.0089.0004.1062, exhibit 7.73.

EXHIBIT #7.73 ENFORCEABLE UNDERTAKING OF NAB (ASIC.0089.0004.1062)

MS ORR: If we could now bring up ASIC.0089.0002.2242. We will see the presentation that Promontory provided to NAB and ASIC. I want to show you two slides which contain the key findings. If we could go to 0005. We see that the independent expert reported that:

> *Progress in developing the program has been slow. The program appears to have evolved iteratively during 2017 rather than through a well-designed process. There appears to have been no comprehensive risk assessment across NABs spot foreign exchange business against the enforceable undertaking requirements and relevant regulatory standards and guidance. Some key stakeholders have had limited engagement in the program to date. NABs independent risk and assurance functions have had limited involvement and the human resources function has also had limited engagement. In combination, these have led to gaps in the program and a lack of detail in the action plans.*

And if we could then go to 0015. We see here the assessment of NABs FX program design :

> *We are unable to assess the overall effectiveness of the program or of any program work streams to prevent, detect and respond to the enforceable undertaking conduct types. We found action planning has progressed but not completed in any of the assessment areas.*

Further down:

> *Little progress has been made in the detailed design of the action plans.*

And further down:

> *The action plans are relatively high level and lack sufficient detail to enable us to evaluate the effectiveness of their design to address the concerns raised in the enforceable undertaking.*

Now, Mr Shipton, these are troubling findings from the independent expert tasked with assessing the effectiveness of the program that the enforceable undertaking required NAB to develop?---They are, indeed, very troubling.

The program had not been developed to a point where its effectiveness could be assessed?---That is correct.

But the enforceable undertaking required NAB to develop a program of changes that was capable of assessment by the independent expert?---The enforceable undertaking required the development of a plan. This is my understanding. The enforceable undertaking required the development of a plan. And the plan was clearly deficient.

Well, it required the development of a program to prevent, detect and deal with the sorts of misconduct that was the subject of ASICs concerns. Do you agree with

that?---I agree with the – the fact that it was a – there was – that the term – and I think there was – and it would be helpful, actually, to refer to – I think it's about 3.7 in the enforceable undertaking - - -

We could bring that back up. I - - -?---Yes, because I think that's a key provision as I understand it.

I will tender this document first, Commissioner.

THE COMMISSIONER: Promontory presentation concerning NAB FX EU program ASIC.0089.0002.2242, exhibit 7.74.

EXHIBIT #7.74 PROMONTORY PRESENTATION CONCERNING NAB FX EU PROGRAM (ASIC.0089.0002.2242)

MS ORR: And the enforceable undertaking is ASIC.0089.0004.1062. And you had referred to 3.7, I think, Mr Shipton?---Around 3.7, Ms Orr.

3.7?---I'm going from memory. There is – there is basically a key provision in the enforceable undertaking as regards the deliverable.

3.7 is at 1071. This is one of the deliverables, which is that the independent expert was to conduct an assessment of the effectiveness of the program. Do you see that?---Yes.

And another deliverable appears at 3.5, which I took you to earlier. That's at 1069. That other deliverable was the provision by NAB to ASIC and the independent expert of a program of the nature described there. Do you see that?---Yes.

Now, that program had to be in a form that enabled the independent expert to conduct an assessment of its effectiveness?---My understanding – and this is what I have been told by the team, because they looked at – they looked at this at the time, as I understand it. They looked at the – these provisions, and there may be other relevant provisions, and there were certainly concerns as to the efficiency of the program itself, but there was not a conclusion at that point in time – there was not a clear conclusion, as I understand it from the team, that there was a breach of these provisions.

And in your view, based on what I just showed you, Mr Shipton, was there a breach of these provisions by NAB?---It's difficult for me to come to a conclusion as to that, because I understand that the point of uncertainty and – and I – it's a very difficult situation for me to opine on, but the point of doubt was whether or not – whether or not there is a quality or sufficient – a quality sort of provision built into – into this. The conclusion was – and I think it's a reasonable conclusion – that there was doubt,

at the very least doubt, as to whether or not there was a breach of the EU at that particular point in time.

Well, Mr Shipton, what is the point of having, in your words, a deliverable like this if NAB could produce a program that was so deficient that it was incapable of being assessed by your independent expert?---I totally agree that there is room for improvement and there are certainly lessons to be learned as regards – and I've certainly learned a lesson from going over this case study, as to the robustness of agreeing and documenting, particularly documenting, enforceable undertakings, because my observation is, is that the documentation should have gone further to make sure – and make it very clear to avoid any doubt that I referred to earlier as to the sufficiency and the quality, as it were, of the deliverable. And that is a key, key lesson for me from this case study.

All right. Well, Mr Shipton, about a week after the presentation that Promontory gave, the market supervision team discussed how to proceed in light of that presentation with Commissioner Armour. Have you seen the documents about that?---I have seen some of the documents, yes.

Can I take you to ASIC.0089.0002.0560. Perhaps if we could have the second page on the screen as well, which will enable you to see that the primary email in this chain on 20 April at 6.43 pm is an email from Mr Grantly Brown, senior manager, market supervision, to Cathie Armour and Greg Yanco. You see that?---Yes, I can.

And in this email, Mr Brown recommended to Commissioner Armour that the enforceable undertaking be amended to allow NAB to have another go at developing a program that was capable of being assessed by the independent expert?---Yes, that's right.

Mr Brown said that he recommended:

> *Tell NAB they have three months to deliver a credible reviewable, FX program, and then have Promontory review it.*

Do you see that?---Yes, I do.

And further down, two paragraphs down, he said that:

> *This would require a revision to the EU, the expert contract and a new section 23 memo, but we think this is the best way forward. Of course, this revision to the EU and the reasons why it has been amended will have to be made public*

?---Yes, that's right

And at the top of the page we see Commissioner Armour's response. She said that this was fine with her?---Yes.

And did ASIC then propose to NAB that the enforceable undertaking be varied?---I – I imagine that to be so, from my – my briefing on the facts.

And NAB agreed to that variation?---Yes, they did. And I also understand that there were very forthright discussions from our team as to our disappointment.

Well, under the varied enforceable undertaking NAB gave some additional undertakings to prepare an updated program that was capable of assessment by the independent expert. Is that right?---That's right.

And in your statement you say that ASICs acceptance of the variation of the enforceable undertaking was not unreasonable?---That's right.

Was it reasonable, Mr Shipton?---I think it's – it's – it's reasonable. It's reasonably held, yes.

Why didn't you say it was reasonable in your statement?---I – at my – at the time of the statement – at the time of the statement, these – I was given a very short period of time for drafting the statement, and there has been time for me to reflect since the – since the drafting of the statement. I was travelling overseas and unfortunately I was also very ill at the time. And I – and that would be the explanation as to the evolution of my thinking on this.

Well, you were given a matter of weeks to prepare your statement, weren't you, Mr Shipton?---I was, but I believe, if I remember correctly, this particular case study came a little bit later, and, as I said, my – as I got further into these cases, my views have – have evolved in relation to some of those case studies.

So you now say that this was a reasonable decision, not just an unreasonable – not just a decision that was not unreasonable. Is that right?---Yes. I – I – I can – I think that this is a reasonable decision.

Was it an appropriate decision, Mr Shipton?---Yes. I think in the – in the broader circumstances, I believe that it was an appropriate decision.

The upshot of accepting the variation of the enforceable undertaking without any additional action was that NAB did not face any negative consequence for its failure to adhere to the letter or the spirit of the enforceable undertaking?---May I just, before we go on, may I just sort of add the context in which I said "not unreasonable", because I also think that there could have been better escalation of this matter and involvement of the – either the enforcement committee or, more broadly, the Commission. And so I – I do believe that there could have been procedural improvements. And, again, right now this matter would be handled very differently to what it was at the time. So pardon me, would you, please, repeat the question, given that supplement.

I put to you, Mr Shipton, that the upshot of accepting the variation of the enforceable undertaking without taking any additional action was that NAB did not face any negative consequences for failing to comply with the letter or, at the least, the spirit of the enforceable undertaking?---Except to say that we did, in our public media release on this, express publicly our disappointment in relation to the matter at hand.

Those are the negative consequences, that in a media release you expressed disappointment?---This was a difficult regulatory choice. This was a very difficult regulatory choice. As I was mentioning before, our resources are not limitless. There was uncertainty as regards the alternative, because the alternative, which I imagine that you're alluding to, is going to court. There was not any degree of certainty in relation to going to court to enforce this matter. There was also a consideration, which I think is entirely appropriate, to get a speedy resolution to get this issue back on track. So with those considerations in mind, that broader context in mind, and also keeping in context that we had spent millions of dollars already on this and related issues, that was the broader context in which this decision – this difficult decision was made.

In that broader context, Mr Shipton, NAB was not punished for failing to adhere to the enforceable undertaking?---Again, it was not clear – it was not clear whether there had been a legal breach of the enforceable undertaking.

And - - -?---I agree with your sentiment and your concern and your disappointment of which I totally agree, but I am advised that there was no certainty that there could have been a resolution or a court-based referral which would have given credence to that – that degree of punishment.

Well, the consequence of the approach that ASIC took to this situation was that ASIC was not seen by those that it regulates and the broader community that it serves to be taking action where a major financial services entity failed to adhere – and I will put to you again, to if not the letter, the spirit of the enforceable undertaking?---I can see your sentiments without a shadow of a doubt, and I do agree with your sentiments. But from what I understand at that time by the team we had very limited options. We also were pursuing at the time a large number of other complex matters. That's the difficult regulatory choice we took. There was no clear-cut, quick way of getting to that degree of punishment. That is why I firmly agree with the sentiment of your questioning that we need to sharpen the documentation of any enforceable undertaking so that it is absolutely crystal clear that should a circumstance like this arise where the spirit, as you refer to, is in breach, then we do have a clear path, an efficient path to that degree of punishment and denunciation that you are alluding to.

Do you think that your approach sent the right message to NAB?---Our approach – we wish our approach was stronger but we sent the strongest message we could have which was a public expression of disappointment, and also a private expression of disappointment.

That is the strongest message you could have sent, Mr Shipton?---That – that is what I have been advised.

A media release which read:

> *ASIC is disappointed with the delay in the development and assessment of a remediation program to address the conduct outlined in the EU. However, we are pleased that the process has been sufficiently robust to ensure any ongoing deficiencies have been identified and are being addressed with oversight by an independent expert.*

That was the condemnation of NAB?---Well, that is – that is factually accurate, because I also understand that the team – from the team, that there was a very quick – a very efficient redress in that three-month period. But I certainly agree – and this is part of – this is part of my direction – that we need to be clearer and more forthright in our public denunciations. And you asked me whether or not it's appropriate. I agree it's appropriate. And that's why, you know, I used – I oscillated between the expressions reasonable or not unreasonable. But I agree, moving forward – and this is part of the direction moving forward – we need to be very firm, very clear, very forthright on our public statements of denunciation.

How many times has ASIC taken action against an entity for breaching an enforceable undertaking in the last 10 years, Mr Shipton?---A handful of times.

Twice. Is that right?---I believe twice, yes.

I will tender that document, Commissioner.

THE COMMISSIONER: Emails concerning NAB FX EU 20 April '18, ASIC.0089.0002.0560, exhibit 7.75.

EXHIBIT #7.75 EMAILS CONCERNING NAB FX EU DATED 20/04/2018 (ASIC.0089.0002.0560)

MS ORR: In your statement, Mr Shipton, you tell us that the use of enforceable undertakings for larger financial institutions is going to decrease going forward?---It is, yes.

And do you accept that in recent years ASIC has over-used enforceable undertakings in response to misconduct by larger financial institutions?---May I respond by saying I think there has been an undue reliance, yes, and one of the reasons why there has been a reliance in the past and why there will be less of A reliance in the future is that we will have a more effective penalty regime for that fundamentally important provision 912A. That is also part of the forward projection here, and also, I think, an important consideration when one looks back in time over the usage of an EU.

And enforceable undertakings have tended to proceed on the basis not of an admission of contravention – and we see this from the one I just took you to, the NAB one – not on the basis of an admission of contravention, but on the basis that the entity acknowledges that ASIC holds particular concerns. Are you changing that practice moving forward?---Yes. I believe I've referred to – to that change of practice and my desire to change that practice moving forward. I believe I mentioned maybe yesterday that the starting presumption should be a stronger, forthright and robust admission of wrongdoing and responsibility.

Now, I want to move from enforceable undertakings, Mr Shipton, to civil proceedings. What sorts of civil proceedings can ASIC commence against financial services entities?---A range of civil proceedings. Misconduct, 912A, investor protection, consumer protection. There's a range of different remedies – sorry, civil actions available to us.

So you tell us in your statement that since 1 July 2011 ASIC has commenced civil proceedings on 169 occasions following formal investigations by enforcement teams. How many of those civil proceedings were commenced against the major banks?---Can you direct me to – remind me which paragraph?

151, Mr Shipton?---I do not have the breakdown of the large financial institutions in front of me.

What proportion of the 169 do you think were brought against the major banks?---Let me respond by saying not – not enough. Not a high enough proportion.

In the statement that Mr Mullaly gave the Commission in advance of the third round of the Commission's hearings, Mr Mullaly indicated that since 1 January 2008, ASIC had commenced 10 proceedings against the major banks, the Bank of Queensland, and Suncorp. Do you recall that?---I recall that. What was the date again that Mr Mullaly was referring to?

Since 1 January 2008. So further back in time than the period that you've dealt with in your statement?---Yes. And if I remember correctly also, you break out the statistics in the interim report which is also a good indication of – and support to my earlier comment that we need to do more.

How many of the 167 proceedings that you refer to in your statement were civil penalty proceedings?---Sorry, can you just take me back. There's a lot of numbers flying around.

I'm sorry, 169. That was a number that you amended in your statement. It's now 169. It was originally 167. This is of civil proceedings in the table - - -?---Yes.

- - - at paragraph 151?---Yes.

So what I'm asking you is of those 169 civil proceedings, how many were civil penalty proceedings?---I do not have that to hand, but I would hazard a guess that – and this is only a guess, a reasonable significant amount but that would only be a guess.

Sorry, I missed – your guess?---A reasonably significant amount.

A reasonably significant amount?---But I'm only hazarding a guess because - - -

You don't know, Mr Shipton?---I haven't asked – I haven't had a breakdown of these – of these figures.

And what's the purpose of a civil penalty proceeding commenced by ASIC?---The purpose of a civil penalty proceeding is to punish and deter both – and deter both general and specifically the wrongdoing. And it should be applied in serious cases. And also to get redress in relation to the – the wrongdoing.

Now, in ASICs submissions in response to the interim report, ASIC said that it accepted that it needs to make changes to its approach to court-based enforcement and initiating litigation?---Yes. Yes, we most certainly do.

And you gave some evidence about this yesterday. More proceedings brought more quickly. And there was a third aspect to it that I now can't recall. You might remember that, Mr Shipton?---More quickly, and then, amongst other things, we were going to compartmentalise or sequence out our undertakings. I also think I mentioned novel – use of novel and creative ideas. And one thing that I failed to mention, but since you prompt me now, is that I think we should be looking at – at trying to commence civil actions in relation to the individual decision-makers, because my view of deterrence in relation to the corporate field, given that the academic literature shows that it is difficult to establish deterrence of a corporation, my personal and professional observation is that we should be looking at deterrent effect on the decision-makers and the individuals themselves, and that is also a core priority of ASIC moving forward.

In those submissions by ASIC in response to the interim report, ASIC accepted that the proper starting point of enforcing compliance with the law is litigation. Do you recall that?---Yes, I recall the expression which I drafted that we should be turning our minds in relation to breaches to ask ourselves the question why we should not be proceeding using court-based litigation actions.

And the only circumstances in which litigation should not be pursued are where there is insufficient evidence or it is contrary to the public interest. Is that right?---They are considerations, but I will also add a practical observation is that we are resource constrained and there may be cases – there very well may be cases – in fact, I expect there to be cases that we are constrained either by budget or by personnel as to our ability to pursue. So our – our keenness, our willingness and our resolve unfortunately is tempered by the practical reality of resource and budget constraints.

But that should not be an excuse or any way limit our first question of – and this is procedural – why not litigate. And that is why the guidance, the decision-making structures that I refer to throughout the case studies, in my belief are so fundamentally important moving forward.

So resourcing, I understand, you've referred to that and the impact that that might have on things, but the two matters that ASIC, it seems, from its interim report submissions, needs to be satisfied of before commencing litigation are sufficiency of evidence and that it's not contrary to the public interest to bring the proceeding, borrowing heavily from the Commonwealth DPPs prosecution policy. Is that right?---Yes. So I refer, I believe, on paragraph 45, we should satisfy ourselves of two things: that there's sufficient evidence and the evidence of the facts of the case and all of the surrounding circumstances that the prosecution would be in the public interest, and we go on, as you say, to say that that is consistent with the DPP.

And I just want to ask some questions about each of those points of satisfaction. What is the standard that ASIC applies in determining whether it has sufficient evidence to commence litigation?---Well, that would be on a case-by-case basis. And my understanding of the process is that there is – there is an assessment by the enforcement teams. There is also input from our chief legal office as to the – the prospects and the sufficiency of evidence, and oftentimes we also go out to external counsel. And in the case of criminal matters, we would liaise with the – with the DPP and that is the process – but, again, I must emphasise it's on a case-by-case basis.

Of course the application of the standard is done on a case-by-case basis but I want to understand what the standard is that is applied. What basis are you looking for for sufficiency of evidence. Are you looking for a proper basis to bring the proceeding, are you looking for it being more likely than not that you will win the proceeding? What is the standard that you are looking for?---I – I see. The standard is – the standard that should apply – and this is a part of the enforcement review right now, because we also want to look at, as I said, more novel cases and cases that test the law – would be a proper basis. But, again, that's the starting point. And, of course, case specific matters are very important to – to that broader – to that base consideration.

And can you give any content to that? How do the people assessing the sufficiency of evidence know when they've got to the point when there is a proper basis to bring the proceeding?---Well, that would be very difficult for me to generalise because that relies on the professional judgment of the case officer, the separated legal officer and often is the case in complex matters, external counsel in relation to criminal matters. It would relate to the professional judgment of the CDPP.

So accepting that professional judgment is involved in that, is there any guidance given to them about what to look for to be satisfied that there is a proper basis?---I'm not – I'm not personally aware of any guidance, but these are exactly the types of matters that we are looking into as a part of our enforcement review. I defer to the

leadership of that review to a leading silk, Mr Crennan, because these types of questions that you rightly ask are appropriately led by a person like Mr Crennan who has knowledge and experience of those types of questions and procedures that you ask about.

So turning from sufficiency of evidence to the proceeding not being contrary to the public interest, the second limb, Mr Shipton, ASIC says in its response to the interim submissions that:

> *It must be evident from the facts of the case and all of the surrounding circumstances that the prosecution would be in the public interest.*

Do you see that in paragraph 45 of those submissions that - - -?---Yes.

- - - I think you are looking at now. What does ASIC mean by that?---Well, my understanding is that – that there is a test which is applied in relation to taking a matter to court to determine whether or not it's in the public interest to do so. And in my experience and understanding, that most, if not every case – or the vast majority of cases are – are – are in the public interest to – to proceed with.

Did you say most, if not all?---That's my – that's my experience, at least. Again, I – I do not practise and do not have expertise in the determination of these matters. This is not an area that I have practised over my – my – my professional career. And from what I understand, it is a matter which is very case specific, and from what I understand, again, it depends on the circumstances and the considerations at the time. And I also understand, but I'm not an expert in, that there are – there are – there's a body of case law and a body of jurisprudence, as it were, around these – around this – around this topic, but, again, I do not profess expertise in it.

Can I ask you about four matters that ASIC articulated in its submissions in response to the interim report might militate against bringing a proceeding in the public interest. The first of those was that litigation can be expensive and resource intensive both in its preparation and its outcome. You refer to that in paragraph 48(a) of the interim report submissions, Mr Shipton?---Yes.

Now, that is not an issue unique to civil litigation, is it?---Pardon me?

That is not an issue that is unique to civil litigation. It is a necessary corollary of taking any enforcement action that there will be a cost involved in doing that?---That's right. And usually – and oftentimes, a very expensive cost and this – my reference – and I – and this is what I was talking about when I was mentioning about the resource constraints.

But a number of other enforcement outcomes can be expensive and resource intensive such as enforceable undertakings that can require ongoing supervision by ASIC, such as the issues that we've seen in relation to the NAB FX enforceable undertaking?---That is right. Although, in my observation, I find that civil litigation

can be extremely expensive. And I would point out again that the BBSW experience for us, which was court-based enforcement, cost us $45 million.

Well - - -?---If – and if we had lost, Ms Orr, if we had lost and had orders against us, that means we would have been looking at an expense of over $100 million. So these are the types of factors that I'm – sorry, we are alluding to in – in this paragraph.

So going to court also presents ASIC with opportunities to potentially recoup costs, doesn't it?---Exactly right. And – and – but there is no certainty. You're absolutely right but there is no certainty.

Well, if you litigate and you're successful, then as a matter of course you will ordinarily be entitled to your costs?---That is absolutely right.

And if you litigate and you're successful, then you have a specific power to make an order that the unsuccessful party pay the costs of your investigation under section 91 of the ASIC Act?---And we are – we are very proactively utilising that section, that provision. We did in BBSW.

But the power to recover the cost of a formal investigation in that way is contingent upon you litigating and succeeding. Is that right?---Correct.

And you've also got similar powers under section 319 of the National Consumer Credit Protection Act?---It would appear so, yes. I believe.

But you can't make an order to cover the costs of a formal investigation if you use other sorts of enforcement outcomes?---I believe that to be the case.

So is that a factor that you take into account when you're assessing the potential cost of going to court?---We – pardon me, would you be most kind to – to repeat the question?

The fact that you can, if successful, not only recoup your costs but also make an order under section 91 of the ASIC Act to recoup the costs of the investigation, is that a factor that you take into account when you're assessing the potential costs of litigation?---Yes. Yes, it would be.

Now, the second public interest factor that ASIC describes as potentially militating against litigating is that it can be time consuming to prepare and conduct litigation?---That is correct, yes.

Well, I want to suggest to you, Mr Shipton, that that's not really a public interest factor. It's inherent in the nature of litigation that matters take some time to be prepared, heard, and decided?---That is – yes, that is exactly right. And that is why in my earlier comments I was somewhat departing or adding to public interest and

adding the resource considerations which we are now going across. I – I see the distinction and that's why I was alluding to that distinction earlier.

I see. And the third public interest factor that ASIC says might militate against litigating is that civil litigation is uncertain in outcome?---That is certainly my experience in life, yes.

There's no certainty that a court will find a contravention?---That is my experience, yes.

And there's no certainty that if a contravention is found as to the penalty that will be imposed by the court?---Correct. And I am minded by the BBSW experience of recent time whereby our enforceable undertakings got a payment of 50 million in two cases, 25 million in one case, and we – when we went to court, we only got 3.3 in costs.

Well, Mr Shipton, I don't want to comment and I'm not going to ask you to comment on the specifics of particular cases in the courts?---Yes.

But I do want to discuss this with you at a level of generality. Do you accept that when ASIC goes to court it needs to have a very clear idea of the case that it is presenting for adjudication?---Absolutely, yes.

It needs to have a clear understanding of its interpretation of the law?---Absolutely.

And of the application of the law to the particular facts of that case?---Absolutely.

And it then presents that for the court to rule on?---It does.

And ASIC would not expect to win every case that it takes to court?---No, we don't.

And even with a very strong case, there are uncertainties that are inherent in litigation?---Correct.

There may be cases where ASIC loses a case on the facts, perhaps because a witness changed their account from prior to trial to during trial?---Huge amounts of variables. You're absolutely right.

And there might be cases where the court doesn't agree with ASICs view of the law?---I certainly have experience of that, yes.

But in that situation, the court makes a pronouncement on what the law requires?---It certainly does.

And ASIC can use that pronouncement as a basis to consider whether it ought to press government to change the law?---It certainly does.

There are also uncertainties in other remedial outcomes, aren't there, Mr Shipton? You don't know, unless you ask them, whether an entity who has been served with an infringement notice will accept it and pay it. You don't know whether an entity that has agreed to an enforceable undertaking will abide by that undertaking. There is a level of uncertainty in many of your remedial outcomes, is there not?---There's many uncertainties in everything that we do. I totally agree. Although I would make the observation that that degree of uncertainty is resolved at a earlier, arguably less expensive, point in time in the system than court-based enforcement actions. I am not saying for one second that we are reticent about moving forward. And I will highlight that the points that we went through in – in our interim response was merely what are militating factors. I want to make it crystal clear we will be undertaking more court-based actions. We will be more adventurous, as it were, in pushing points of law. We will be taking more – let's call it risks, because we now have, through my direct engagement with the government, more funding to do exactly that.

What about the public interest in bringing proceedings, Mr Shipton? You agree that there is one?---Totally. And that's why I wanted – I just reinforced my commitment to bringing more actions, because I firmly believe that there is a public interest in using court-based admonishment – admonishment and deterrence and punishment, particularly with larger financial institutions who have disappointed us and disappointed Australia so much.

ASIC intends to conduct more test litigation moving forward. Is that the impost of what you've just said, and ASICs interim submissions – interim report submissions?---Yes. I – my observation is that we should be testing the limits of the law more because the case that is made in the interim report of the Royal Commission is a very strong one, that if we do hit, at the end of a court process, a roadblock, then that is a very clear, very strong argument to go to the government and say that we do not have the penalties and powers that we need to. Because my observation, in the nine months that I've been in this role, is that we don't have right now – right now – sufficient penalties. We don't have right now sufficient powers. And what we need to do is have those sufficient powers, have those sufficient penalties, and if there's any doubt or any weakness as regards our powers or penalties, then a very good place to display and realise that deficiency is a court judgment.

When you say you don't have sufficient powers, Mr Shipton, what powers do you not have that are not pending?---Not pending? Maybe we can get on to this later but I am a – I am a very strong advocate of the BEAR regime being extended across to our areas of responsibility and jurisdiction. I mentioned earlier that I believe that we should be having far more deterrent effect on business leaders in financial institutions and to better enable the efficiency of that deterrent effect having a BEAR regime that would apply to them would make a direct linkage and make that wish more effective.

Do you accept that there needs to be a fundamental change of mindset at ASIC towards the pursuit of court-based outcomes?---I believe there needs to be a very strong change in approach, procedures, and guidance. I use the expression – and deliberately use the expression we made mistakes in relation to the case studies that you have raised today and yesterday. I like the word "mistake" because it includes the concept of being misguided. We could and will be doing a better job at providing guidance and direction to our people so that their mindset, their approach, their starting point, their starting proposition will be very different. We have a program of change and program of reform that I fundamentally believe in. And, in fact, I remember saying when I first accepted this role, coming back from Cambridge, Massachusetts for a couple of days I made public comments about the need for strategic change at ASIC. I had that belief in October of last year. I had that belief when I arrived on 1 February. And I firmly believe in its implementation right now.

Can I ask you about criminal proceedings, Mr Shipton. What do you see – what does ASIC see as the purpose of criminal court-based outcomes?---Well, that is – that is, again, going up the – the – using the scale analogy, going to the most serious of extremes. I've been alluding to the enforcement pyramid of Professor Ayres and Braithwaite. To use that analogy, the criminal action is at very much towards the apex of that for the most serious of matters, the most egregious of matters and reacting and responding accordingly.

Do you accept that ASIC should pursue criminal action against larger financial institutions more frequently than it has?---Most definitely.

And how would you characterise ASICs major failings in respect of pursuit of criminal court outcomes?---At the risk of – at the risk of getting into a debate again about failings, I prefer "mistakes". Again, I use the expression "mistakes" because failings to me, at least – this is my own understanding of the word – means there has been no success, there has been no functioning which, in my understanding of the word, means that we haven't been doing it at all. And we have. So, yes, we have made mistakes. Yes there are case studies that you may want to take me to where, in my view, we should have, if the case was before us today, pursued criminal sanctions. And so in answer to your question, yes, we need to do it more often. And now we have a process and procedure and a – a program of change that I am expecting that that mindset, that approach will be embedded.

ASIC has not given sufficient attention to whether it should pursue criminal proceedings, has it?---We could have done much better.

I want to ask you a few questions about this by reference to the ClearView life insurance case study that was dealt with in the sixth round of public hearings. You've also dealt with it in your statement. You know that ASIC engaged with ClearView about two distinct issues: breaches of the anti-hawking provision in the Corporations Act and concerns about mis-selling?---Yes, that's right.

And breach of the anti-hawking provision is a criminal offence?---It is, yes.

And the evidence in the Commission's hearings was that ASIC and ClearView began engaging about potential breaches of the anti-hawking provision in April 2016?---Yes.

And early on, ASIC formed the view that the matter was unlikely to, in the words used in the documents, go criminal. Have you seen those references, Mr Shipton?---I don't recollect seeing those references at this point in time, but it is consistent with my understanding of the – of the facts.

But over time, ASIC received further information about the potential criminal breaches and built up a picture of their significant scale. Do you agree with that?---Yes.

And by early May 2017, ClearView had told ASIC that it may have breached the anti-hawking provision up to 303,000 times over a three-year period?---I understand that to be the case, but I want to be clear in this. I'm not – I'm not sure whether ClearView have been so direct in their admission. But there certainly was a strong indication of – of that.

And despite that strong indication, ASIC did not seriously revisit its view that it had earlier formed that this was not a criminal matter?---That's right. That was a mistake.

And why was that mistake made?---I understand – and, again, I wasn't involved, and I'm just – my response – and I want to be very clear – my response now is just to give you context of what was going on at the time. That the focus was to stop the pressure tactics which were regarded – and I – I do have empathy with this view as being egregious. There was also industry-wide concerns as regards pressure sales tactics. ClearView was not the only firm that was engaging in pressure sales. I understand that there were two other cases at that particular point in time, Select being one, Freedom being another one, which were far more egregious by terms of volume of – of pressure sales and also that that pressure selling was continuing. Given that we have, in limited resources, I've mentioned the limitations of both – and the size of resource of our enforcement team which is about 240 people. The other team involved in this is our DCI team, that only has 80 people. So given that context, given what was going on, that is why a decision was made to focus in on stopping the pressure sales, stop this – this misconduct, focus in – enforcement attention on more egregious pressure selling at Freedom and Select. And this is unfortunate and I think it was a mistake not to pursue the anti-hawking aspects of this matter.

Isn't the purpose of the anti-hawking provision to try to eliminate situations where customers are subjected to sales processes whether they involve poor sales practices or otherwise without particular statutory requirements being met?---I personally agree with that assessment, yes.

So noncompliance with that provision is a very serious matter?---It is, yes.

And that's reflected in Parliament's decision to make breach of the anti-hawking provision a criminal offence?---I certainly agree with that and I've made that point to the team. The fact that the Parliament of Australia has determined this to be a criminal matter means that we need to give it – any criminal matter extremely serious weight and attention. I agree with that.

So you now accept that ASIC should have given consideration to criminal action against ClearView?---Absolutely, yes.

And it should have escalated the matter to the enforcement committee?---Most definitely, yes.

But neither of those things happened?---No, they did not.

Now - - -?---That was a mistake.

Was there anything new about the evidence that was given in the sixth round of public hearings?---I'm not aware of anything being new, no.

But ASIC has, in light of those public hearings, reconsidered whether or not it will take criminal action against ClearView. Is that right?---Yes. I want to be very careful because there is – I want to be very careful here because there is criminal investigation and I – I need to be careful in my responses. So I will be as helpful as I can.

Well before the hearings, ASIC had agreed terms with ClearView by which it resolved its concerns, hadn't it?---It did.

So ASIC has had to consider the effect of that agreement on its ability to pursue a criminal outcome now against ClearView.

MR COLLINSON: Could I raise this – it's really up to the Commission, your Honour, but it's ASICs position that for the chair to answer that question is potentially unhelpful to the prospect of those criminal proceedings.

THE COMMISSIONER: I just don't follow, Mr Collinson. You will need to take me more slowly through the proposition you're putting.

MR COLLINSON: Well, if I were to unpack it, which I can, I think I will probably expose it too much. But perhaps I better just say it briefly. More that is said might expose and assist an argument by potentially charged parties that the initiation of criminal proceedings might involve an abuse of process because of prior events.

THE COMMISSIONER: Well, if there were an abuse of process, and, of course, I simply don't know, but if there were an abuse of process, that would be reason, would it not, to in fact expose the difficulty rather than to keep it private. Isn't the – aren't you on the horns of a dilemma, the dilemma being this: there's consideration

of whether or not to prosecute someone criminally. There may or may not be a bar or difficulty lying in the way of that prosecution. The bar – the difficulty or bar in the way of prosecution concerns the conduct of a public agency in its dealings with that person who may be the subject of prosecution. I must say, my immediate reaction is to think that those factors point towards exposure than they point towards keeping confidential the considerations that bear upon whether a prosecution can or cannot go ahead. But that's the problem - - -

MR COLLINSON: Well, submissions might be made that would assist a person under investigation presently and a question for the Commission is whether it needs to explore at this level of particularity in order to complete its work and that that should overpower the prospect of that criminal investigation going forward.

THE COMMISSIONER: Yes. Ms Orr, what do you say?

MS ORR: All I had asked and all I wished to hear an answer to was whether ASIC had had to consider the effect of the agreement on its ability to pursue criminal action. I was not proposing to explore conclusions based on that consideration. So I don't know if that assists my friend - - -

MR COLLINSON: If it's confined in that way.

THE COMMISSIONER: No difficulty. Very well. Put the question again, please.

MS ORR: So my - - -

MR .....: Mr Hayne, why are you concealing the greatest fraud in this country which is variable interest rate loans.

THE COMMISSIONER: Could I ask you to sit down, sir.

MR .....: Variable interest rate loans render a contract void for uncertainty - - -

THE COMMISSIONER: Would you be good enough please, sir, to sit down.

MR .....: - - - and yet we have kangaroo courts in this country who are conspiring with the banks to conceal this great fraud.

THE COMMISSIONER: I'm sorry, sir, I think that you are interfering with the work of the Commission.

MR .....: I put in a submission to this Commission which included a transcript of the High Court showing the corruption of the judiciary in concealing this fraud. Variable interest rates render a contract void – I will get my bag – void for uncertainty. You are concealing – this is a corrupt Commission. You are concealing fraud.

THE COMMISSIONER: Yes, Ms Orr.

MS ORR: Mr Shipton, my question was whether ASIC has had to consider the effect of that agreement on its ability to now pursue criminal action against ClearView?---I'm going to respond with one word, yes.

Thank you. And do you think it was appropriate for ASIC to resolve the matter with ClearView on the terms that it did?---No, I do not.

Thank you. Now, what does the ClearView case say to you about ASICs attitude to and pursuit of criminal action against larger financial entities?---May I respond by saying what it says at that particular point in time about the decisions was that it was a mistake not to pursue a action of this seriousness in relation to a financial institution. That is yesterday's mindset. That is not the mindset that exists today – of the ASIC of today.

Mr Shipton, I want to turn now away from your enforcement measures towards other initiatives at ASIC. And I would like to ask you some questions about what has been referred to as the CCM program?---Please.

Now, earlier this year ASIC announced that it was going to begin putting ASIC staff on site at five financial institutions, ANZ, CBA, NAB, Westpac and AMP?---Yes, that's right.

And that is the close and continuous monitoring program, or the CCM program?---That is that program, yes.

So I want to ask you some questions about the aims of that program and how it's going to work in practice. Now, in your second statement you said that in your experience in Hong Kong, you saw how extended onsite supervision approaches applied to individual institutions worked to identify and address the risk of harm from misconduct?---That's correct. And, in fact, I believe I reference some of the work that we did or I did – my team did in Hong Kong whereby we were able to – or the SFC team was able to identify thousands of breaches through – I think, 1500 breaches through 300 onsite inspections. So that speaks statistically to these types of programs. I can also speak to being a regulated person, being the subject of both onsite supervision in Hong Kong and being subject of the American equivalent – the American equivalent through the New York Federal Reserve. So I can speak to the subject matter both as a regulator but also a regulated person.

When you arrived back in Australia earlier this year to take up your position at ASIC, were you surprised that ASIC didn't already have a similar program?---Yes, I was. And I understand that one of the reasons being was resource constraints. I will quickly add that my colleague, Commissioner Armour, has been utilising this very effective tool in the market space during her tenure as a Commissioner.

Did you think when you got to ASIC that ASIC was doing enough to proactively address the causes or drivers of misconduct as opposed to responding to misconduct that had occurred?---I think we could have done better. And the sequencing of my thinking was after a number of months in the role and after a number of months of returning back to Australia, I realised, essentially, two things that we needed to do very quickly, and that was accelerate our enforcement outcomes, and embark upon new supervisory approaches, including but not limited to the CCM, and that is a conversation that I had with the government and then resulted in August for funding for those two programs, amongst others.

So that – that funding which we referred to earlier in your evidence was given after Treasury invited ASIC to submit a funding proposal for new strategic initiatives. Is that right?---Correct. There had been some correspondence before that invitation. There had also been representations by me to the very most – the very most senior members of the government on these matters.

And the CCM program was one of the strategic initiatives that ASIC proposed in response to that invitation?---Yes, that's right. I think I referred to yesterday as this being a surge approach or a mid-year approach or out-of-cycle approach. It was not only an out-of-cycle approach for us but to give context to the government, it was also an out-of-cycle funding for them.

Could I take you to the letter that you wrote to the Treasurer and the Minister for Revenue and Financial Services when submitting your funding proposal. ASIC.0076.0001.4411. We see in the last paragraph of that page – this is your letter, I'm sorry, Mr Shipton?---Yes, I recognise this letter.

Yes. From 28 May this year to the Treasurer and the Minister for Revenue and Financial Services. We see in the last paragraph on this first page that you explained that you wanted to make significant changes to the direction of ASIC and the way it does its regulatory work. And that your key changes were:

> *... accelerating and expanding enforcement activities and embedding new supervisory approaches which involve more dedicated and intensive supervision for our most important financial institutions.*

?---Yes.

And then if we turn to 4415 in this letter we see some more detail at the bottom of the page about the CCM program. You said:

> *ASIC has traditionally taken a risk-based approach to surveillance. This means the surveillances are focused on a specific incident or transaction or involve reviewing a thematic systemic issues across multiple institutions. This contrasts with risk-based supervision which involves ongoing monitoring of an institution.*

?---Yes, that's right.

And over the page at 4416 you referred to the new approach that you considered was required – this is in the first paragraph:

> *... involving dedicated staff assigned to supervision or close and continuous monitoring of the entities.*

Do you see that?---Yes, I do.

Now, you didn't give any information in this letter about the type of supervision you wanted your staff to conduct or provide further details about how you thought the program would work. And I want to come to that later. But at this point, those details were not provided?---That's correct. This was a framework or an outline of the ideas. Of course, pending – pending funding and pending support to enable that, yes.

And we see in the third paragraph on this page that you described this as one of – a number of initiatives that would:

> *Require coordination with APRA.*

Do you see that?---Yes, most definitely.

And APRA has conducted prudential supervision of ANZ, CBA, NAB, Westpac and AMP for many years hasn't it?---That's right. The prudential supervisory team has been operating for quite some time. Their supervisory approach as I understand it is slightly different and, of course, their focus being prudential is distinct from our role.

What do you hope the CCM program can achieve that is different to what the APRA supervisory work does?---Well, at the – the starting point for APRA is the safety and soundness of financial institutions, and that is an absolutely fundamentally important role. Our starting point is the good conduct – the adherence – the good conduct to financial institutions, the adherence to the laws and regulations of the land and what we think should be better outcomes and better awareness of the fact that there are consumers involved, consumer conduct matters involved when it comes to financial institutions. So that is the different starting points. There is degrees of overlap and coordination necessary but we both, under the twin peaks model, come from different ends of the twin peaks spectrum.

Did you consult with APRA before you put this proposal to Treasury?---Yes, I – I made Chairman Byres aware of this approach and sought his support and understanding that we would be working together. Chairman Byres and I have a number of initiatives that we would like to do more of, including – and it's not included in these documents – the greater utilisation of supervisory colleges for the larger financial institutions so that we look at large financial institutions from

different angles, from the prudential angle, the conduct angle and we would include other regulators as well.

And what was APRAs view of ASIC conducting supervisory work alongside APRAs supervisory work?---I remember Chairman Byres being extremely supportive and encouraging.

Could I tender this document Commissioner.

THE COMMISSIONER: Letter from the chair of ASIC to the Treasurer, 28 May '18, ASIC.0076.0001.4411, exhibit 7.76.

EXHIBIT #7.76 LETTER FROM THE CHAIR OF ASIC TO THE TREASURER DATED 28/05/2018 (ASIC.0076.0001.4411)

MS ORR: So in August of this year, Mr Shipton, the money came through and ASIC was given about $8 million in funding for the CCM program?---That's right. I think it was 7.8 million to be exact.

Yes?---Over two years.

And the first onsite supervision began at the end of October when a team of ASIC staff went to CBAs offices in Sydney?---That's right. And that is what I would call a rapid response.

Yes. ASIC had about three months between finding out that this program would be funded and deploying its staff to the first entity?---Correct. Not only deploying staff to the first entity but – and this is crucial to, I think, the effectiveness of the role – securing senior staff members to lead these teams. We're calling these senior staff members senior supervisory officers, because we needed to have senior people who could have direct, robust and frank conversations and provide feedback to the senior-most officers of a financial institution. So part of the difficulty in getting the rapid response is to take two people, two very fine professionals, out of existing important roles and transition them across to the SSO role, the senior supervisory officer roles.

So ASIC didn't hire new staff with experience in supervising financial services entities for the program?---That's very – in my observation as being a regulator over different jurisdictions, it is very difficult to find people with direct demonstrable regulatory and supervisory experience. We would have to, in my quick observation – and I did think about this – but unfortunately, it was discounted as impractical – I thought about the possibility of bringing in people from overseas, particularly the United States or Hong Kong, who I knew, but that was impractical. And I have faith in the – in the team that we have – have – have now sort of assigned to these roles.

So, instead, you redeployed existing staff at ASIC. And do they have experience in onsite supervision of financial services entities?---One of them has, I believe – yes, one of them certainly does. And both of them, though, I will – I will quickly add, both of them have many years – many, many years of what I think are very important leadership roles in regulation and supervisory-type functionality. And I have every faith and confidence in the two leaders of this project and the men and women who work with them.

My questions were not just directed to the leaders, Mr Shipton. As I understand it, those two people – the two chief supervisory officers have two teams of people working under them. So do the people working in those teams have experience in onsite supervision of financial services entities?---They wouldn't have – not many of them would have that much direct experience as – yes, because just of the nature of – of – of the work that has been conducted at ASIC over many years. So that was part of the challenge – and there's undoubtedly challenges to this – of building a team and responding rapidly in those few months that we had.

Will the teams be assigned to particular entities or are they going to rotate between the entities?---Ultimately, they will rotate between the entities. We've got some guidelines – I believe I have attached them to my witness statement – some protocols around professional behaviour onsite, professional behaviour during the conducts of these onsite supervisory functions. And there will be a program of rotation, which is important, I think, for best practice, but also important for benchmarking and comparison, and it's good regulatory practice.

Why is it best practice to rotate them?---In part, as I said, so that there is a greater degree of benchmarking, so that a supervisory officer will understand across the spectrum of financial institutions as opposed to only seeing a small number of them. That is one operational advantage. The other issue that we are very highly attuned to is the risk of regulatory capture. And there has been some case studies out of the United States that we have used for training purposes, so that the supervisory officers involved are attuned to some of those regulatory capture risks before they start their work.

Now, you said earlier that the first team went to CBAs offices at the end of October. And Mr Comyn gave evidence earlier this week that CBA had volunteered to go first in the CCM program. Was that taken into account by ASIC?---That was a – that was not taken into account, but their readiness was acknowledged.

And have – has there been any feedback from your team at CBA about how they're progressing?---There has been some very clear feedback from – from our team as to – as to the system structure of CBA, and there will be more feedback. And from what I understand from the chief supervisory officer involved in CBA, that feedback will be very powerful, very important. And this goes to the ultimate aim of the CCM and onsite supervisory project will improve, we think, the systems, processes and mindset of that particular institution and hopefully the other institutions very soon and very quickly.

Did I hear correctly you said you had had feedback as to the system structure. Is that what you said?---Yes. What we had started to do and this is – let's call it an entry point – we have started the entry point into financial – these five financial institutions is to start by looking at their breach reporting processes and procedures. This builds on the body of work that you and I discussed yesterday on our breach reporting compliance report. We have a body of information that is a baseline and a starting point to be applied and reviewed by the team, and the feedback, as I understand it, as this has been interrogated and explored, even – even though only over a short period of time, is very powerful. And being able to have a chief supervisory officer give direct feedback on some of the system failings inside the financial institutions in this – in this case in relation to breach reporting – is very powerful. And if I may quickly add, one of the concerns that we have found is that we worry about the raw, real message getting through to the senior-most leaders of an organisation, the CEO and the boards of directors. We worry that the message is being filtered as it goes up that hierarchical chain. Senior – sorry, chief supervisory officers will disintermediate that filtering and late give raw, frank, blunt but very real feedback to the people who need to hear it.

You have mentioned a number of times in that answer that this is powerful. What is powerful about it? What is it that is being described to you as powerful from the feedback so far?---The fact that – the reason why it's powerful is motivated not only from my feedback and my understanding of the very short weeks of the operation of this role – of this initiative with CBA, but it's also a personal experience. And starting with my own personal experience I was working at a financial institution before it had onsite supervisory oversight by the New York Federal Reserve. And then over a weekend during the financial crisis, it had onsite supervisory oversight by the Federal Reserve. Even though I was sitting in Hong Kong half a world away from the supervisors, I sensed a change in approach by the leaders of the financial services firm that I was working for. I also was the subject matter – and this is quite paradoxical, I was also a business leader subject of an onsite supervision by the Hong Kong Securities and Futures Commission when I worked in a business called the Prime Brokerage business. And I remember my mindset changing when I had my own interaction, probably for the first time as a regulated person, with a regulator. My mindset and the mindset of my senior colleagues beside me changed. Because even though we were middle management, as it were, we had, for the first time, direct engagement and interaction with a regulator. That changed my mindset. That changed my colleagues' mindset. So I took these personal experiences which are in my mind very powerful, and then I'm seeing it play out through the prism of the interactions between the chief supervisory officer and Mr Comyn and I am seeing very clearly the same feedback that my colleagues and I had when I was subject of these types of supervisory approaches. Hearing the message in terms which aren't couched. Hearing something directly in detail from a regulator is very powerful and very meaningful.

Well - - -?---And I think that it will have a big impact over time if we can expand it.

I want to understand a bit more about the CBA experience, Mr Shipton. What is the message that CBA is hearing from those conducting the CCM at CBA?---Well, it's – it's very short, because we've only been in there for a very short period of time but the initial feedback is is that we are not confident that the messages that we're seeing when we look at individual case studies, the concerns as to the way those case studies were handled, how they were escalated, we are – we are – we are not confident that that raw message, that clear important message is being escalated in direct and frank and clear terms to the senior-most leaders.

I just want to – I want to make sure I'm understanding this answer. I'm asking you about the message being conveyed by those who are conducting the close and continuous monitoring?---Yes.

What is the message that they are conveying to CBA?---Well, you mean, more broadly?

No. No. What are they doing there, Mr Shipton?---They are, as I said, they are looking at the processing, the systems, the reporting, the escalation, the dealing with of breach reports. We have a body of cases which we became aware of through the breach reporting compliance project that you and I discussed yesterday. So we have a starting baseline. We have a body of knowledge.

Yes?---What we are now doing is a deeper dive into some of those case studies. And by doing a deeper dive into some of those case studies we are diagnosing these issues and concerns. In other words, we're getting to a level of detail and passing on that detailed message to a CEO and potentially to the board that they probably haven't heard before. And that level of raw detail is important.

I want to understand more about how that works. They're conducting a deeper dive into those issues, those systems and reporting issues based on a number of cases that you identified in the work that was the subject of report 594. Is that right?---That's right.

So what do they do? Do they get there, call for documents about those cases and read those documents?---Yes, they're – they're looking at those documents, they're – they're now speaking directly to the business leaders who are involved in those case studies.

So - - -?---And they – legal and compliance officers who are directly involved in these case studies, as opposed to, which is a more traditional approach, things being filtered through, you know, the general office of compliance or the general office of reform. We're going directly to the people involved in those case studies.

Yes. You are sitting in the premises of that entity. You are reviewing documents – which you could pull into your own premises under your compulsory information gathering powers – but you are reviewing those documents at the premises of the entity and you are then having conversations at those premises with representatives

of the entity about what you are seeing in those documents. Is that right?---Yes. There is – I will add that probably a large part of the document review will be taking place at our offices.

I see?---A large part of that.

So what exactly happens at the offices of CBA?---We will be doing a tremendous amount – we will be reviewing documents there and we do review documents because we will ask for a document and if that document will – if a document comes – it is apparent that a document would be useful to have a look at, we will ask for that document and it's entirely possible that that document could be produced onsite and reviewed onsite.

Right?---We will also be asking and spending time, we – in the case of CBA, we've been assigned a meeting room which is for our dedicated use which is sequestered and away so we can keep our own material confidential but we will be interrogating and speaking and discussing and asking questions and finding out more information with those individuals who were involved in these particular case studies. Onsite supervision is essentially, in my experience both as a recipient of it and as an executor of it, it is a matter of sitting in a room and starting to ask questions, getting to know the business, drilling down into detail, following leads, being inquisitive, asking questions and really delving into a particular matter so that we can diagnose the issue and the problem very precisely.

So you have your meeting room within CBA and you have the documents you've called for which you can read in that meeting room. And can you then invite people in and ask them questions in that meeting room about what you've seen?---Yes. And that – that's my experience. And, again, we mustn't – we've only been in CBA for a short period of time. So we only have a handful of – of days of operation to – to work from. What I'm now describing is my intention and my experience of how it has worked having run programs of this nature before. How it works. So, yes, we will be calling in, we will be asking. It seems as if it would be useful if we could speak to person X because person X seems to be referenced in this document or in this process. So to better understand what person X does, we will ask to speak to him or her.

And apart from inviting people into your meeting room to speak with them there, is it intended that you will, your representatives, will sit in on meetings that are going on within CBA and observe those meetings?---Possible, although we are cognisant and aware that trying to be a fly on the wall is extremely difficult because, of course, behaviours will change. There's an experience – this is – this is an experience from overseas. So I doubt there will be much effectiveness of doing that. What I do think, though, is very powerful – and, again, I've had this on both sides – is having long, detailed question and answer sessions with middle management business leaders, that is incredibly powerful. And may I also talk about a secondary derivative – a derivative of this which actually is a very powerful one. The more people we interact with in the body of the organisation, the more the message gets out as to

what our real motivators and drivers are. People's attitude inside a financial institution can, will and do change once they have been interrogated and interacted with a regulator. That is a very powerful tool. Because, as I said, we are now speaking to people who have probably never been spoken to by a regulator in their career, in – in a – a – an environment which is not a formal investigation but is a supervisory one in nature which better allows, you know, better allows what I think an understanding of the broader business and how a business is conducted with the mindset of good governance, adherence to the law and ultimately good conduct for consumers.

So Mr Shipton, how many people are you sending in to occupy the meeting room at CBA?---We would – I think at the moment our teams are very limited because we're resource constrained. I think our teams are probably half a dozen or so.

How long will they be there for?---They will be coming and going hopefully forever but we only have funding for two years.

And coming and going with what sort of frequency?---We hope that they will be coming and going with at least bi-weekly frequency. At least bi-weekly frequency. You must remember we're only funded to about 16 to 20 head count. We're covering five institutions. These institutions are all over the country. So this is just a starting point. This is a launching pad. And those folks in our supervisory team, they will be expected as they rotate and move around to be spending as much time as possible onsite gathering information as they can. As I said, there's going to be back and forth. I think that's very good practice. I don't think being embedded – being embedded or being permanently onsite is good practice. But by having frequent onsite physical presence, in my experience and observations over the globe is a very good regulatory tool.

And what is the work product, from your point of view that the people in the meeting room will produce. At the end of intervals do they produce some sort of report that they bring back to ASIC about CBA containing recommendations or proposals that will be passed back to CBA? What happens?---Yes, so there will be – so this – this body of work in relation to breach reporting will ultimately end up with a series of ongoing reports to CBA on what we believe are the system faults, the system failings, where we believe there could be improvements, where we believe there are deficiency. That feedback will take place. Equally, the other output is that this feedback will be given to other members of our own team, and, indeed, to APRA so that other members of our team who interface with CBA in this case will have knowledge and understanding of what we're finding inside that institution. And then broadening it out – and I mentioned this before – we want to utilise what's called supervisory colleges more often which is working with APRA, working, perhaps, with the New Zealand regulators, and sharing all of these knowledges, presentations, feedback amongst our regulatory peers so that all of us in Australia, New Zealand, prudential, conduct regulators have a much better understanding of an organisation like CBA. That means that we can better – we can better supervise and regulate. And another by-product is – and this is my experience in Hong Kong – we will often

– I expect that we will often come across misconduct and that misconduct will then be escalated and referred to the enforcement teams as appropriate.

The ongoing reports that you're going to provide to CBA, will they be made publicly available?---We would consider making them publicly available. But some of the – we could consider that. I – I haven't turned my mind to that particular question. My observation of seeing this in practice in the United States and seeing this in practice in – in Hong Kong is that the – the most powerful – a very powerful weapon is that direct feedback. I've personally been involved when I was in Hong Kong of providing direct feedback to senior-most leaders of financial institutions at the end of our project, and that is very powerful. I think we would reserve the rights – again, subject – subject to the protocols that I understand we have in place – about the – making public of information because I do understand that there are protocols and restrictions on information that we can make public, but subject to that, that is certainly the – something we would keep in mind.

And do you anticipate that those reports will contain recommendations to CBA about changes that they ought to make?---Yes, I mean, we – we can certainly highlight. But I do want to – I do want to clarify. This is not an onsite compliance department. This is not an onsite strategic guidance firm. What we will be doing is making observations in relation to what we believe are deficiencies or areas for improvement. Our role is not to be their compliance department. Our role is not to be their strategy department. Our role is to give frank, honest, blunt and very important feedback as to where we see potential deficiencies, where we see room for improvement, and where we see that the leadership, system, structure and, importantly, culture of financial institutions can improve.

That's a convenient time, Commissioner.

THE COMMISSIONER: Yes. Just before we adjourn, Ms Orr, you may step down, Mr Shipton. The solicitor for the Commission has received the following communication from Gilbert & Tobin, solicitors for Westpac:

> *Westpac wishes to clarify a matter that arose during Mr Hartzer's oral testimony yesterday morning. From around transcript 6850, line 30 Mr Hodge asked Mr Hartzer questions in relation to arrangements concerning BTGL authorised representatives and the issuing of fee disclosure statements (FDSs) and opt-in arrangements for ongoing advice services. By way of clarification, BTGL authorised representative are not required to provide opt-in notices from pre-FOFA clients on a biennial basis. By way of further detail we note the following. BTFA employed advisers: renewal notices referred to as opt-in notices are required to be issued biennially for all ongoing advice customers. FDSs are required to be issued annually for all ongoing advice customers.*
>
> *BTGL authorised representative: opt-in notices are required biennially for all post-FOFA ongoing advice customers. Opt-in notices are not required for any pre-FOFA ongoing advice customers remaining. FDSs are required to be*

issued annually for all ongoing advice customers. Westpac apologises to the Commission for any inconvenience caused.

That letter having been received this morning I thought it right that I should read it publicly so that there should be no doubt about what has been communicated to us about those matters.

MS ORR: Thank you, Commissioner.

THE COMMISSIONER: Now, Ms Orr, 2 pm.

MS ORR: Yes, thank you, Commissioner.

ADJOURNED **[1.05 pm]**

RESUMED **[2.00 pm]**

THE COMMISSIONER: Yes, Ms Orr.

MS ORR: Mr Shipton, you mentioned earlier, BEAR, the Banking Executive Accountability Regime. Now, I want to ask you some questions about that, but I want to summarise a few propositions first. BEAR currently applies to the largest banks in Australia?---Yes.

And it imposes a series of obligations on those banks. There are the notification obligations which require the bank to identify the accountable persons who are responsible for the bank's operations?---Yes.

And there are the key personnel obligations, which require the bank to make sure that the responsibilities of the accountable persons cover all the operations of the bank?---Yes.

And there are the deferred remuneration obligations which require the bank to defer a particular proportion of the variable remuneration of accountable persons for four years?---Yes.

And the accountability obligations. Each accountable person has three accountability obligations. Do you agree?---Yes.

They need to conduct the responsibilities of their position as an accountable person, firstly, by acting with honesty and integrity and with due skill, care and diligence. Secondly, by dealing with APRA in an open, constructive and cooperative way, and thirdly, by taking reasonable steps in conducting those responsibilities to prevent

matters from arising that would adversely affect the prudential standing or prudential reputation of the bank?---Yes.

And the bank itself, as well as the accountable persons, has similar accountability obligations?---Yes.

But in the case of the individual accountable persons and in the case of the bank, the obligation to take reasonable steps to prevent matters from arising relates to matters affecting the prudential standing or reputation of the bank?---Yes.

And that is why BEAR, in its current form, is administered by APRA?---Correct.

Now, the BEAR is based on a similar regime in the UK called the Senior Managers Regime?---Yes.

Are you familiar with the Senior Managers Regime, Mr Shipton?---I am familiar, yes.

It's broader than BEAR in a number of ways. It firstly applies to a broader range of entities, do you agree?---Yes.

Not just to banks but also to insurers and other financial services firms?---Yes, that's my understanding.

And in the UK the Senior Managers Regime is jointly administered by the conduct regulator, which is the Financial Conduct Authority and the prudential regulator, the Prudential Regulation Authority?---Yes.

And the obligations that the Senior Managers Regime imposes on individuals – this is the other aspect of the greater breadth – aren't limited to matters affecting the prudential standing or reputation of the firm?---Yes.

They extend to the conduct of individuals more broadly?---Yes.

Now, there are two sets of conduct obligations imposed on individuals by the Senior Managers Regime. Could I ask you to look at RCD.0006.0016.0746. Now, this is a document produced by the Financial Conduct Authority about the Senior Managers Regime. And could we turn to 0789 where we see the two tiers of conduct rules under the Senior Managers Regime. Do you see in the table, if we could, perhaps – thank you. The first tier, the individual conduct rules, apply to almost all employees of financial services firms. Is that right?---Pardon me?

The first tier, the individual conduct rules, are you aware that they apply to almost all employees of financial services firms?---Yes, I am. I believe that there is a – a pyramid of, as it were, of different degrees of application, but yes.

And the first tier is the tier that applies to most of the employees?---That's my understanding, yes.

And so the conduct rules for those employees are:

> *You must act with integrity, you must act with due care, skill and diligence, you must be open and cooperative with the FCA, the PRA and other regulators; you must pay due regard to the interests of customers and treat them fairly; and you must observe proper standards of market conduct.*

?---Yes.

And the second tier of conduct rules apply to senior managers of financial services firms. And they require senior managers to:

> *Take reasonable steps to ensure that the business of the firm for which you are responsible is controlled effectively; to take reasonable steps to ensure that the business of the firm for which you are responsible complies with the relevant requirements and standards of the regulatory system; take reasonable steps to ensure that any delegation of your responsibilities is to an appropriate person and you oversee the discharge of the delegated responsibility effectively; and you must disclose appropriately any information of which the FCR or PRA would reasonably expect notice.*

?---Yes, the FCA, yes.

That's right. Now, what I want to ask you, Mr Shipton, is whether ASIC supports expanding the BEAR so that it is administered by ASIC in relation to conduct, as well as APRA in relation to prudential issues?---We support the extension wholeheartedly of the BEAR regime to cover conduct, and we would work – we would propose to work collaboratively with APRA who would be – continue to have oversight on the prudential aspects.

So you don't think that you should move to joint administration of the regime. You would leave administration of the regime with APRA?---That is something that we are open to. I understand from the UK regime that there is joint administration. I'm not ruling it out. My earlier response was just to say that I wholeheartedly support the current regime whereby APRA has ownership and carriage of the oversight in relation to prudential matters. I will quickly make an observation, as I understand it, with the UK regime is slightly different – their twin peaks is slightly different because the FCA does have, in certain cases, prudential oversight responsibilities.

So you said that you supported the extension to cover conduct. Do you think that the accountability obligations imposed by BEAR should mirror the sorts of conduct obligations that are imposed by the senior managers regime?---Most definitely, yes. And if I remember correctly, there is quite a long list of conduct-related responsibility – responsibilities under the UK regime, including – including more

detail as to these conduct responsibilities. And I believe that is a very good starting point for us to consider here in Australia.

We see from the explanatory memorandum for the BEAR amendments that one of the reasons why the BEAR was restricted to matters affecting the prudential standing and reputation of banks was to avoid potential confusion of regulatory roles. Do you have any comments about that?---My only comment to be made would be that, in my observations in different jurisdictions, we need – regulatory agencies need to be working very collaboratively, cooperatively across a range of issues, and that requires management leadership attention. And it is a – an ongoing challenge. But I do not see it as an impediment for the extension of a BEAR-type regime here in Australia.

And if the BEAR obligations were extended to the sorts of conduct rules that are on the screen at the moment, then in what kinds of circumstances would you envisage ASIC commencing enforcement action against an accountable person for failing to comply with those obligations?---It's – again, it's difficult to respond in the abstract, but I was alluding to this earlier. These types of structures provide a direct linkage and a direct responsibility so that it can be clearly established in the event of a failure to adhere this, that person X was responsible for the oversight of that particular area, and if there's a failure in that particular area, then enforcement actions could ensue. So I think these types of regimes and models are very important for enforcement accountability, but equally – and I was involved in the formulation of a similar regime in Hong Kong which is called the Manager-In-Charge regime, and my practical observation was that one of the first steps was just merely mapping out who is accountable for conduct oversight is incredibly important and powerful.

Can you give an example of how ASIC might have dealt differently with one of the matters that I've asked you questions about in your evidence, if you had had additional powers under an expanded BEAR regime?---Well, again, it's difficult for me – it's difficult for me to generalise. And it's difficult for me to answer that question in relation to the case studies, because I do not know the responsibility map or the accountability map that would have – would exist in a scenario if it were to occur under this type of regime. But each and probably every one of the case studies that we have discussed today would clearly point to, as a part of that responsibility map, part of that accountability map, and in the UK they have responsibility statements which clearly articulate what type of responsibilities each individual manager and leader has, then you could clearly delineate which person, which senior manager was responsible for the conduct and the conduct failures. So you could likely in most if not all cases draw a direct line between the misconduct and who was responsible in the leadership and management of that financial institution for that not to happen.

I tender that document, Commissioner.

THE COMMISSIONER: Senior Managers and Certification Regime RCD.0006.0016.0746, exhibit 7.77.

EXHIBIT #7.77 SENIOR MANAGERS AND CERTIFICATION REGIME (RCD.0006.0016.0746)

MS ORR: Now, Mr Shipton, I would like to take you to another document about the Senior Managers Regime published by the Financial Conduct Authority. RCD.0006.0016.0032. This is a document published this year by the FCA about the Senior Managers Regime. And if I could direct your attention to 0034 which contains the foreword from the chair of the FCA. We see in the second paragraph of the first column the chair says, speaking of FCAs responsibility for ensuring that financial markets work well by protecting consumers, protecting and enhancing the integrity of the financial system and promoting effective competition, he says:

> *These important responsibilities are supported by a robust framework of accountability and transparency. We are accountable to the Treasury and to Parliament with detailed public scrutiny exercised by the Treasury Select Committee. We are open and accountable to the public through the publication of our annual report and our annual public meeting. We are subject to examination and certification by the National Audit Office.*

Now, that accountability framework is broadly analogous to ASICs save that the Parliamentary committee here is the Parliamentary Joint Committee on Financial Services?---We also have additional Parliamentary committees.

Yes?---House of Representatives and Senate Economics. But broadly similar, yes.

Yes. Now moving to the second column in the second paragraph the chair said – the chair says:

> *We want all those involved in financial services to be able to trust that their regulator and the firms it regulates have their best interests at heart. That is why we believe our senior management should meet standards of professional conduct as exacting as those we require from regulated firms.*

He then speaks about the Senior Managers Regime in the last column, describing it as:

> *A formal expression of the commonsense, good governance practice that any organisation should adhere to. It was created against the backdrop of a clear and shared understanding that a culture of personal responsibility must be embedded at the heart of financial services. This is true of firms and regulators alike. We are not formally subject to the regime but we uphold the highest professional values and our stakeholders, including Parliament and the Treasury Select Committee rightly expect us to do so. In line with this, we have decided to apply the fundamental principles of the regime to our senior staff.*

You see that?---Yes, I do.

Now, does ASIC propose to apply the principles of BEAR to its senior staff as the FCA has done with the Senior Managers Regime?---I – I think it's an excellent suggestion and I have looked at this paper in reasonable detail. And I think it provides a good governance framework for regulatory agencies. As I was mentioning before, in my own personal experience in designing a similar regime in Hong Kong, I found that that first step of that accountability map was just plain good – good practice of good governance. I've looked at this and I am – I am minded to apply this form of rigour to our own organisation, because I also have – and this has been an agenda throughout my time, because as a part of my reform agenda – I am very mindful of what I call hypocritical risks of a regulator. If we expect something of the regulated community, we must be holding that – that standard to ourselves. And I have asked our team, well before – well before I came here today, to undertake what I – what is a review across our organisation of making sure that we are holding ourselves to the highest standard of account using as a benchmark the standards we expect of others.

So do I take from that answer, Mr Shipton, that you do propose to apply the principles of BEAR to your senior staff?---Yes, as I said, I am minded to it. I would like to have more – I would like to get into the more – into this in a more detail. I would like to share this idea more broadly with my Commissioners. But I am going to propose it to my fellow Commissioners. And we are, at the moment, embarking upon a transition of our structure whereby we are delineating roles – new roles and responsibilities, and I think the model that is provided by this document is an excellent model.

And if obligations analogous to those in BEAR were to be applied to ASIC, do you think that should be done by ASIC publicly undertaking to be bound by those obligations in the way the FCA has done, or by a separate statutory accountability regime established either specifically for ASIC or for regulators?---Well, we're getting – we're getting into a – a lot of sort of potential detail, but I think the starting point – the starting point is, as I mentioned before, to propose to my fellow Commissioners that we should be holding ourselves to this account, and should be presenting to Parliament and the public what – what is – what I think an excellent model here.

And you don't have any views at present about how, if that proposal is accepted, you ought then execute that?---Well, I think – again, I haven't had time or the ability to workshop this idea with experts. I would, for instance – I would, for instance, like to speak to my peers and colleagues in the FCA, who I know very well, about their experience and what works and what their experiences are in relation to this. But I am certainly very open-minded about ways that we can better ensure our accountability by using different frameworks. And I mentioned in my witness statement – and I believe this is also in the interim – response to the interim report – we want to work with Parliamentary committees about better assessment frameworks of what we do, and I see this as an excellent example of – of such a framework.

I tender that document, Commissioner.

THE COMMISSIONER: Senior Management Regime, RCD.0006.0016.0032, exhibit 7.78.

EXHIBIT #7.78 SENIOR MANAGEMENT REGIME (RCD.0006.0016.0032)

MS ORR: Now, Mr Shipton, I want to turn to ASICs organisational structure. As you indicated in answer to one of my questions earlier, ASICs current members are you as the chair, two Deputy Chairs, and four Commissioners?---Yes, that's right.

So ASICs governing body is comprised entirely of executive members?---We – it – the current – currently we are structured as executive Commissioners or Commissioners with executive responsibilities, is probably the best way of putting it.

Well, there are no non-executive members of your governing body, is there?---Sorry, that's exactly right. We – we do – we do not have non-executive members of our Commission.

And that's in contrast to the Financial Conduct Authority which we've just been speaking of. That entity has both executive and non-executive members of its governing body?---It's in contrast to the FCA and also in contrast to the Securities and Futures Commission in Hong Kong in which I was an executive director and board member of – or Commission member of.

And in contrast to the ACCC and the Competition and Markets Authority in the UK and the Reserve Bank?---Yes, in contrast to – to those, or – to the – as I understand it, yes.

So do you think there are risks in ASIC having a governing body, unlike all of those organisations, that is comprised entirely of executive members?---There are concerns that I have when – when I look at the current operational framework and operational responsibilities of the ASIC Commission. And that is why I am the firm – I am of the firm belief that our current structure should move to one whereby Commissioners of ASIC do not have day-to-day executive responsibility, and that executive responsibility, that day-to-day executive operational responsibility should be moved to another class or strata of leaders and managers. And I believe that that is the optimal structure. I will quickly observe that in my – in the last three or four years, both as a regulator in Hong Kong under one structure and then spending some time thinking about this when I was at Harvard University, I actually believe that the optimal model is full-time Commissioners with relevant experience providing strategic oversight, strategic challenge and strategic direction, because that, I think, is the optimal model for a regulatory agency.

It would be regarded as poor governance practice for a large listed entity to have a board comprised entirely of executive directors, wouldn't it?---It would be, yes.

Why wouldn't the inclusion of eminent non-executive members on ASICs governing body assist in the good governance of ASIC?---I'm not ruling that out. What I am saying is that I believe – and my own observations, having thought about this for a number of years from a number of different angles, and having looked very closely, actually, at the models in the United States, the SEC and the CFTC, that the optimal model is full-time Commissioners who do not have executive responsibilities, but are providing full-time strategic oversight, strategic direction, strategic guidance, and challenge to the executive group.

In 2015, Mr Shipton, a capability review of ASIC was undertaken by an expert panel, wasn't it?---It was.

And that review resulted in a report being provided to government in December 2015?---Yes.

And you've annexed a copy of that report to your statement. The expert panel made a large number of recommendations and they included recommendations in relation to internal governance?---Yes, they did.

And one recommendation was that ASIC realign internal governance arrangements by elevating the current Commission role to that of a full-time non-executive function with a commensurate strategic focus and external accountability free from executive line management responsibilities. These are the sorts of things you've just been raising with me?---Yes. And I remember reading that at my desk in Hong Kong in 2016 and it resonating then and it resonates with me now.

The expert panel also recommended that a new role of head of office be established with delegated responsibility and accountability for executive line management functions. Do you recall that?---Yes, I do.

And both those recommendations flowed from the expert panel's view of the dual roles of the Commissioner. Do you agree?---I – I understand that to be the case.

And the panel said that it believed that a dual governance and executive line management role inherently undermined accountability?---I believe that was words to that effect, yes.

And it also referred to this as creating insufficient bandwidth for strategic decision-making?---Yes, I remember that line.

And the panel concluded that there would be a number of significant benefits from the governance model that it proposed, including clearer lines of accountability and oversight, and allowing the Commissioners to focus on strategy matters?---Yes. I am – I am clearly influenced by – by those sentiments.

But ASIC responded to the capability review in April 2016 and did not embrace those proposals?---I understand that to be the case.

And ASIC expressed the view that the new model would tend to undermine rather than enhance its strategic focus and accountability. Have you seen that?---I have seen that, yes.

And what observations do you make about that response by ASIC?---I would take a different view to the – that response at that particular point in time.

You've spoken publicly about the capability review?---Yes, I think I've spoken very – very publicly about how I wish to embrace it.

And in your assessment, was ASICs response to the internal governance recommendations capable of addressing the issues identified by the panel?---I think we needed to go further and we are going further.

In your statement you identify a number of changes arising from the capability review that ASIC has made since you took over as chair?---Yes. They have been my first order of priority in the nine months that I've been here.

And they include a very recent step of creating a new level of senior management known as executive directors?---That's correct, yes.

And the Commission approved, on 5 November – so a very short time ago – that commencing on 1 January next year your Commissioners would cease to have day-to-day operational and executive responsibilities and they would adopt a strategic oversight review and external engagement role with the 10 executive director roles established to sit between the Commission and the senior executive leaders?---Correct. And I would only add that there will be additional senior executive leaders to add increasing – increased bandwidth at the operational and executive level as well.

And this resulted from a reconsideration of the recommendations of the capability review?---Well, at least in my part, yes, and by my fellow Commissioners as well, yes.

And which responsibilities will the executive directors take over from the members of the Commission?---Well, that is, essentially, all of the executive responsibilities currently undertaken, day-to-day executive responsibilities of a Commissioner will transition away from a Commissioner to the executive director. We've seen in a number of case studies, by way of example, the engagement by a Commissioner. That type of engagement will cease.

Why did ASIC choose – why did you choose to respond to the capability review findings and recommendations by creating an entirely new layer of senior managers rather than adopting their suggestion of appointing a head of office who would, in effect, act as the CEO of ASIC?---Because of my own personal experience having been a regulator, and reflecting for over – over two or three years on what I personally believe is the optimal structure for a financial regulatory agency, and I

believe that the structure, which is not – the structure that we're proposing which is not dissimilar to the US SECs is the optimal model. There are – let me be also very quick I don't think the US SEC with due respect to them is a perfect model but I do believe – and that model has highly influenced me in my thinking over many years as to what I believe is the optimal model. I'm not ruling out and have not ruled out some form of head of office functionality. I will also quickly supplement that in addition to the executive director, we are creating a chief of staff role to the Commission which will in part – in part form some of the functionality which is envisioned by the head of office role in the capability review. So there is a partial acceptance of that idea without a full acceptance of that, for the reasons I've just stated.

What functions will the executive directors have in respect of enforcement decisions?---Well, the executive directors – there will be two executive directors in relation to enforcement. They will make key decisions as regards the conduct of a case and – and the procedure of a case, but I will quickly add that all of that process is, of course, under review right now. But pending that review, or, you know, assuming that review to – to sort of go in the direction that I expect it to be, they will be discharging decision-making responsibilities on an executive basis pursuant to, as I've mentioned many times before, better, more structured guidance, strategic guidance in particular, coming from the Commission, so that they are directed and guided in the execution of that decision-making discretion.

So will the two executive directors with enforcement responsibilities have the capacity to approve the commencement of proceedings?---Potentially. Potentially in some cases. But, of course, there will be – what I envision that will come out of the enforcement review is that there will be thresholds for approvals of certain matters to – to go to the enforcement committee for – for decision. Or, perhaps, other forums. But, of course, that is all part of the enforcement review. So there will be some discretion by the executive directors, but they will not have the entirety of the discretion because we do have structures in place, committees and governance groups that will be providing key decisions moving forward.

Well, how does that work, Mr Shipton, because isn't the point of this to free up the Commissioners so that they can engage in strategic roles and governance responsibilities? They're still going to have operational responsibility, are they, for whether or not proceedings will be commenced?---They will have decision-making – decision-making roles when a Commissioner sits as a part of the – the enforcement committee. They will be reviewing papers. They will be objectively reviewing papers and submissions. They will be hearing from the team and then deciding upon, along with other colleagues, deciding upon the – the pursuit of the action. As I understand it – as I understand it that is not dissimilar to the structure that is in place by the US SEC.

I may have misunderstood but I thought that you said that they were going to cease to have operational and executive responsibility for regulatory work?---That's

correct. I – but they will still have oversight responsibility and decision-making responsibility - - -

It's more than oversight. You're explaining that they remain the decision-makers?---They – they remain the – because we are structured – the way we are structured, the Commission is the ultimate authority for – for ASIC. We are not a corporate body. We are not structured as a corporate body. So there is only so far we can take the analogy of a board and the executive leadership team. We can only take that analogy so far. What – what I envisioned by this is that decision-making will still be made, because that is our statutory responsibility, final decision-making and sign-off on key matters, on key items will be decided by the full-time Commissioners, and others. And when I use strategic oversight and governance, I am using that expression not so much in a corporate sense but very much in a regulatory agency – government agency sense.

So exactly what it is – what is it that you are freeing them up from doing by creating these 10 new executive directors?---Because right now, on a range of different matters, the Commissioners – or a number of the Commissioners, not all of them because we are already, in effect, transitioning out, a lot of them are actually having – or two or three of them are actually having operational day-to-day responsibility. And that is why I keep on using the expression "day-to-day", because that is – that is where the distinction between the corporate world and a government agency world comes in. A Commissioner under the proposed regime will not have day-to-day operational responsibility. He or she will not be making day-to-day decisions. Yes, there will be decisions that will come to Commissioners on a regular basis. But we are designed by statute to be a decision-making body. And we will remain a decision-making body as a Commission. What I am saying is that we need to be more strategic. We need to be less involved in day-to-day executive responsibilities and operational matters to free up time so that when those decisions come to us, we have an objective mindset, not a subjective one, and that we can, when we are reaching those decisions, align them with our strategic thinking.

The 10 executive directors, the new position, they have now been appointed, have they, Mr Shipton?---They've been appointed but they have not yet commenced because we will be shortly transitioning.

And did you appoint external candidates?---No, we did not.

Did you have an external recruitment process?---No, we did not.

So how did you fill the positions?---We filled the positions internally.

Why did ASIC decide to limit the pool of candidates to internal candidates and, on my read of the documents, to a very limited category of internal candidates?---We decided because of a number of reasons. Firstly, we wanted this transition to take place as quickly as possible. Secondly, there was a realisation that we had a – essentially, a majority of new external outside Commissioners coming on board, who

were providing that external reference point and external experience. Thirdly, there was a recognition that we needed to retain institutional knowledge and regulatory experience. And then finally – and this is my own personal observation – it is a – having – having experienced this through the recruitment process for the Commissioners, the additional Commissioners of which I was a panel member of, and through my own experience globally, it is extremely difficult to find, outside of a regulatory agency, people with demonstrably referable regulatory experience. So with that experience in mind, we opted to recruit from internally, but, yes, we also only referenced or had a category of, essentially, the senior executive leadership pool, which is practically speaking, the pool of talent within our organisation that is – that – that would be qualified for these roles.

Wasn't this a prime opportunity to bring in at a day-to-day operational level some external people with different ideas and different skill sets?---Yes. And that's exactly why that was achieved, by bringing in a number of Commissioners with exactly that external mindset.

My question was about the day-to-day operational level, Mr Shipton?---And I was going to go on and say that I, in my own experience, over many years, it is difficult to find, externally, people with day-to-day relevant experience at that senior level – that regulatory senior level. May I also add something, that it – it is very difficult – we perceived it would be very difficult to recruit into ASIC people at a senior leadership level if there was any doubt as to potential restructures. And I would also emphasise that speed was a part – was – speed of change and action was a key driver. And we have also – and we are writing into the contracts that these are – these are two year contracts. And if people do not perform at this level, then we are – we are clearly minded to make changes.

Well, Mr Shipton, we will never know if you're right about how difficult it is to find these people externally, because you didn't try, did you? You didn't open this to external applicants?---Ms Orr, we will never know, but all I can do is speak from my own professional experience over many years, and from my own experience and professional judgment, that it is extremely difficult to find at this senior level people with demonstrably relevant experience, regulatory experience. It's – because we are talking about a regulatory professional mindset.

And they might have come across from other regulators, mightn't they?---They may have. But, again, my professional judgment and the judgment of my peers – and we did think about it, and – and your – your questioning and your – the premise on which you are presenting is not without merit. I certainly understand. But we decided for the reasons I mentioned before, particularly because we have new fresh perspectives coming from excellent new Commissioners that we wanted to balance the internal institutional regulatory knowledge with this new mindset and approach coming from the new majority of – of Commissioners.

Mr Shipton, I want to ask you some questions about the arrangements for oversight of ASIC. ASIC is subject to ministerial oversight?---Yes.

And it's overseen by the three Parliamentary committees that you referred to earlier?---Yes.

Now, do you consider that the arrangements for external oversight of ASIC could be improved?---Most certainly.

In what ways, Mr Shipton?---Well, I believe that we should be thinking and working with the – particularly the Parliamentary committees about developing frameworks and metrics and methodologies whereby, over time – not in the short term, but over time – they can measure, comment and assess our performance. I have spoken to a number of chairs of Parliamentary committees about this idea. And I hope to – to take it further. I am also minded to try and find out more from our UK equivalents how they best utilise their Parliamentary oversight, because I understand that they have – and I may be wrong – and this is why I want to find out – they have dedicated oversight hearings. I believe that dedicated oversight hearings which go to assessing us – this is Parliamentary hearings – that go to assessing us with reference to that framework would be very, very, very useful.

Who would be responsible under this idea for developing the frameworks or metrics or methodologies that you've referred to?---Well, I think the starting point – and I was alluding to this before because this is a body of work – the starting point is better thinking around the qualitative and quantitative assessments that you were questioning me earlier about. I think that very same exercise needs to be broadened – as I said, broadened out and included in these frameworks. One – and as I said before, the start – one of the starting points is metrics, quantitative metrics that measure the hopeful improvement in the performance and the culture and the outcomes in the financial services sector. That's one of the starting points. And then working back from there is assessing how our tools, approaches and strategy is helping to move those metrics and the performance of the financial sector more broadly in the right direction. This is – this is – and I – this is a very difficult undertaking, and I've spent a lot of time with regulatory experts globally on this, including Professor Sparrow at Harvard University who I worked closely with at Harvard, developing metrics is a challenge for every single regulator around the world in almost every single sector.

And my question, Mr Shipton, was about who would be responsible for engaging with that task? Would it be ASIC who would design the framework metrics or methodologies or would it be the Parliamentary committees?---So we would start by developing these metrics. And then we would propose it to the – to the Parliamentary committees. And we would work with the Parliamentary committees to ensure that they are comfortable and agree with that methodology.

The Financial Systems Inquiry recommended the establishment of a regulatory assessment board to undertake reviews of the performance of Australia's financial service regulators. What's ASICs position on that recommendation?---Our position is we would like to explore making the current accountability and review mechanisms work better than they currently do. And my personal position is that if

that does not have the outcome that we would like it to be, then we should consider alternatives, and that could very well be one of those alternatives. But my proposal is to try and make the current system work better.

THE COMMISSIONER: An essential element of this proposal to make the current system work better is to attempt to measure behaviour in the financial sector. Is that right?---That's the starting point, Commissioner.

And how do you measure behaviour in the financial sector except through the regulator?---You would measure – the starting proposal is to measure using some baseline proxies. Now, I've mentioned quite a bit - - -

Well, just stay with my question. How do you measure performance in the financial sector except through the regulator?---I – I - - -

Who else knows whether the financial sector is behaving or misbehaving - - -?---Pardon me.

- - - other than the regulator?---Yes. So, yes, we would be conducting these metrics. That's exactly right, sir.

So ASIC itself would have to determine and develop what you describe as a baseline about behaviour in the financial sector. Is that right?---What I would say is proxies for behaviour in the financial sector.

Yes. See, what I suggest to you is that it all just becomes self-referential. ASIC determines the base, judges itself against the base. What I want to ask of you is where is the intellectual rigour in that process?---Well, I would submit that the intellectual rigour is that that baseline would be for everybody to see. So if I may use the example of breach reporting, which I have spoken a lot about, we have now a baseline as to the performance of financial institutions. Their poor performance. If we can see those baselines and we – and the world can see those baselines improving, then that must mean that both the financial institutions themselves are improving, and it also must mean that the regulator is improving, and that is, I believe, an objective assessment. So I would submit, very, very, very clearly that what we would be developing is not subjective assessments, of which you would be rightly concerned about, but what we are developing is objective assessments for the world to see and that we would use that as a benchmark.

Yes.

MS ORR: One of the suggestions ASIC made in its submissions in response to the interim report was that reviews could be undertaken of ASICs work by the Council of Financial Regulators. Why would that body be appropriate for that function, Mr Shipton?---Because I am, again, influenced by my international experience that I found reviews – peer reviews by fellow regulators coming from different perspectives to be extremely useful. And the peer review mechanism exists under

IOSCO. So that the idea that I had was to explore with peer regulators here in Australia utilising their expertise to conduct a peer review of each other, and that the coordinating body for that could very well be the Council of Financial Regulators who would also provide some level of oversight and inputs to these – the metrics we were talking about and the measurements we were talking about. I do not for one minute say that it's an exclusive. I believe that we should be thinking about complementary oversight mechanisms and exploring peer regulatory reviews domestically, exploring these metrics and frameworks with the Parliament and exploring some other ideas that I have mentioned and we have mentioned in our submissions.

Well, why wouldn't it be preferable, Mr Shipton, instead of having the heads of other regulators assess the performance of your regulator for an independent assessment to take place by a body designed for that purpose?---Again, I'm not ruling that out. What I'm saying is that we should be working to make existing mechanisms that exist better and see if we can improve the existing frameworks and, you know, I'm hopeful – I can't guarantee it but I'm hopeful that those existing frameworks and existing systems would work better. And I – all I'm saying is that we can be making more of the Council of Financial Regulators and we should be making more of Parliamentary committees. But just one point of correction on your question, if I may. It would not be the heads of the agencies who would be conducting assessments of the others, but the way I envision it is that a team would conduct a peer review. This is a common practice in IOSCO where a team from a foreign regulator would go and assess a peer regulator from across the seas. What I am essentially proposing here with this construct – and it's only a proposal – I haven't had the opportunity to speak to my colleagues on the council yet – that is to basically provide an Australian version of that.

Well, if there was an independent body with that function, it could, in consultation with ASIC, and perhaps even with the Council of Financial Regulators, design the criteria against which to assess ASICs performance. Do you agree?---Yes, I – I see your point, yes.

And if an oversight body was created, would it be beneficial to have it assess ASICs compliance with any BEAR-like obligations that you are prepared to adopt?---That is – as I was saying before, I think it's a very good proposal to have those BEAR-like structures as a framework for Parliamentary committees, or should, you know, the government of the day decide for another oversight mechanism, yes.

An independent body could develop performance benchmarks against which to assess ASICs work, couldn't it?---They could. Most definitely.

And they could prepare a report of their findings against those benchmarks?---They very well could, yes.

And do you think the availability of a report like that would assist the joint Parliamentary committee in the discharge of its oversight responsibilities?---Yes, I –

I would agree that it would. But I would also add that my suggestion to the Parliamentary committees is for their secretariats to provide that sort of – that sort of expertise, so that their – the Parliamentary secretariats would have that. So, again, this is why I have given a great deal of thought to this subject matter, and I believe that many of your very fine suggestions can be achieved within the existing frameworks.

I have no further questions, Mr Shipton.

THE COMMISSIONER: Yes.

MR COLLINSON: No re-examination.

THE COMMISSIONER: Yes. Thank you very much, Mr Shipton. You may step down.

<THE WITNESS WITHDREW [2.52 pm]

MS ORR: Commissioner, that concludes our witnesses for today. And we will pick up again with a new witness on Monday in Melbourne.

THE COMMISSIONER: Yes. We will adjourn until 10 am Monday next in Melbourne.

MS ORR: Thank you, Commissioner.

MATTER ADJOURNED at 2.52 pm UNTIL MONDAY, 26 NOVEMBER 2018

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