



Lisbon School
of Economics
& Management
Universidade de Lisboa

MASTERS IN FINANCE

MASTER'S FINAL WORK DISSERTATION

**AN APPRAISAL OF THE SINGLE RESOLUTION MECHANISM:
THE CASE OF BANCO POPULAR REVISITED**

ANA LUÍSA DA PIEDADE GUERREIRO COVELO

JULHO - 2024



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SUPERVISION:

RICARDO JOÃO NUNES DOS SANTOS CABRAL

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GLOSSARY

Acronym	Description
Banco Popular	Banco Popular Español S.A.
BRRD	Bank Recovery and Resolution Directive (European Parliament and Council Directive 2014/59/EU)
CRD	Capital Requirements Directive
CRR	Capital Requirements Regulation
EBA	European Banking Authority
ECB	European Central Bank
EU	European Union
FOLTF	“Failing or likely to fail”
FROB	Fondo de Reestructuración Ordenada Bancaria
IMF	International Monetary Fund
NCWO	“No creditor worse off “
Santander	Banco Santander S.A.
SMEs	Small and medium-sized enterprises
SRB	Single Resolution Board
SRM	Single Resolution Mechanism
SRM Regulation	Single Resolution Mechanism Regulation (European Parliament and Council Regulation (EU) No 806/2014)
SSM	Single Supervisory Mechanism

ABSTRACT

The global financial crisis and a subsequent sovereign debt crisis within the euro area highlighted the urgent need for improved regulations and oversight of the EU's financial sector. To address these challenges, euro area authorities established a policy framework called the Banking Union which came into effect in 2014, further standardizing rules across the EU and creating new frameworks for supervising and managing banking sector prudential regulation, supervision, and resolution.

The resolution of Banco Popular was the first case of bank resolution managed by the Single Resolution Board (SRB) under the 2014 Banking Union policy framework.

This dissertation aims to assess the effectiveness of the Single Resolution Mechanism (SRM) and in particular, of the Single Resolution Board (SRB) in resolving Banco Popular, the first and the only large bank resolved by the SRB, on June 6, 2017, focusing specifically on adherence to the principles and procedures outlined by the BRRD. Using a single case study, the phenomenon was analyzed within a real-life context, employing both quantitative and qualitative research methods.

We find that the resolution process was generally effective and adhered to BRRD principles and procedures, though the following weaknesses were identified.

First, the ECB inadequately assessed the seriousness of Banco Popular's problems. Although corrective actions were taken, extending the timeline for these measures might have prevented the bank's collapse and resulted in the raising of more equity capital. Moreover, more rigorous stress tests could have anticipated and mitigated the crisis.

Second, the SRB's swift resolution process caused substantial loss of value and stakeholder losses, with Santander obtaining significant gains from the acquisition of Banco Popular. This issue could be addressed through a new mechanism to extend the time frame. Additionally, we found the valuation methods used to be unreliable, resulting in inconsistencies in the bank's evaluation and highlighting the need for improvement.

Keywords: European Banking Union; Banco Popular; Financial Stability; Single Resolution Mechanism; Single Resolution Board; BRRD.

JEL Codes: E58; G20; G21; G28.

RESUMO

A crise financeira global e a subsequente crise das dívidas soberanas da Área do Euro revelaram a necessidade urgente de regulamentação e supervisão do setor financeiro na UE. Para enfrentar esses desafios, as autoridades europeias estabeleceram um enquadramento legal e regulamentar designado União Bancária, que entrou em vigor em 2014, criando um novo enquadramento e uniformizando as regras de supervisão, gestão da regulamentação prudencial, e resolução do setor bancário em toda a UE.

A resolução do Banco Popular foi o primeiro caso de resolução bancária gerido pelo Conselho Único de Resolução no âmbito da União Bancária de 2014.

Esta dissertação tem como objetivo avaliar a eficácia do Mecanismo Único de Resolução e, em particular, do Conselho Único de Resolução (CUR), na resolução do Banco Popular, o primeiro e único grande banco resolvido pelo CUR, em 6 de junho de 2017, com foco específico na adesão aos princípios e procedimentos delineados pela BRRD. Foi utilizado um estudo de caso único empregando métodos de pesquisa quantitativos e qualitativos.

Concluimos que o processo de resolução do Banco Popular foi, no global, eficaz e alinhado com os princípios e procedimentos da BRRD, embora identificadas fragilidades.

Primeiro, o BCE avaliou inadequadamente a gravidade dos problemas do Banco Popular. Embora tenham sido tomadas ações corretivas, a extensão do prazo para essas medidas poderia ter evitado o colapso do banco e resultado no aumento de capital próprio. Além disso, testes de stress mais rigorosos poderiam ter antecipado e mitigado a crise.

Segundo, o rápido processo de resolução do CUR causou uma perda substancial de valor e perdas para as partes interessadas, beneficiando o Santander com ganhos significativos provenientes da aquisição do Banco Popular. Esta questão poderia ser abordada através de um novo mecanismo para prorrogar o prazo de aplicação da medida de resolução. Além disso, constata-se que os métodos de avaliação utilizados foram pouco confiáveis, resultando em inconsistências na avaliação do banco e destacando a necessidade de melhorias.

Palavras-Chave: União Bancária Europeia; Banco Popular; Estabilidade Financeira; Mecanismo Único de Resolução; Conselho Único de Resolução; BRRD.

Códigos JEL: E58; G20; G21; G28.

TABLE OF CONTENTS

Glossary	i
Abstract	ii
Table of Contents.....	iv
List of Figures	v
List of Tables.....	v
Acknowledgments.....	vi
1. Introduction	1
2. Overview of Relevant Studies, Key Question and Purpose.....	3
3. Methodology.....	6
4. The Case of Banco Popular.....	8
4.1. Background.....	8
4.1.1. The Spanish banking sector.....	8
4.1.2. Banco Popular.....	9
4.2. Resolution Process.....	13
4.3. Valuations conducted throughout the Process.....	15
4.4. Legal and Economic issues in the aftermath of Resolution	20
5. Effectiveness of the Single Resolution Mechanism in Responding to Banco Popular's Crisis under the BRRD	22
5.1. Evaluating the ECB's Oversight Prior to Resolution.....	22
5.2. Examining the SRB's Approach to Resolution Process and Mechanisms ...	24
5.3. Analyzing the Effectiveness of Valuations and Implications for Shareholders Throughout the Process	29
6. Critical Lessons from the Banco Popular Resolution Experience.....	34
7. Conclusion	35
References.....	36
Appendices	41

LIST OF FIGURES

FIGURE 1 – Outcome for Banco Popular legal entity (Creditor Losses) -----	19
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LIST OF TABLES

TABLE I - Banco Popular-Total Assets and Consolidated Results 2008-2017-----	9
TABLE II - Banco Popular - Solvency -----	10
TABLE III - Outcome of the economic valuation -----	17
TABLE IV - Outcome of the alternative outcome scenario -----	17

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AN APPRAISAL OF THE SINGLE RESOLUTION MECHANISM:

THE CASE OF BANCO POPULAR REVISITED

By Ana Guerreiro

1. INTRODUCTION

The 2007-2009 global financial crisis and the 2010-2012 sovereign debt crisis revealed that the European Union lacked adequate policy tools to effectively respond and intervene in weak or insolvent banks. During these crises, these challenges were a key factor that forced Member States to bail out institutions using taxpayer money. In order to minimize the need for such interventions, it became necessary to harmonize the resolution processes for these institutions ('European Parliament and Council Directive 2014/59/EU', 2014).

The Bank Recovery and Resolution Directive (BRRD) was established in May 2014 and became effective in July 2014, providing a unified framework for swiftly and efficiently resolving failing banks and investment firms in Europe. The main objective of the new system was to protect taxpayer funds and prevent expensive state-funded bailouts while ensuring market discipline (Pancotto et al, 2019). It entailed the creation of a single supervisory authority – the SSM/ECB – which assumed supervisory authority over the Euro Area significant banks from November 2014.

Later, in July 2014, the SRM Regulation was published, furthering the harmonization process in the field of resolution and creating a centralized resolution authority entrusted to the SRB ('European Parliament and Council Regulation (EU) No 806/2014', 2014). The SRB thus became the entity responsible for managing the SRM, becoming operational on January 1, 2015, and fully assuming its resolution authority on January 1, 2016.

The resolution of Banco Popular was the first case of bank resolution managed by the SRB under the BRRD and the SRM Regulation.

Banco Popular, founded in 1926, emerged as one of Spain's major banks by 2016, ranking sixth in terms of market capitalization. However, the bank encountered growing financial challenges following the global financial crisis and the sovereign debt crisis, namely those stemming from the impact of those crises and their economic repercussions

on its operations as well as bank-specific issues, which resulted in a substantial volume of non-performing loans and a deteriorating capital position. Despite concerted efforts aimed at recovery and profitability under the oversight of the Bank of Spain and European institutions, the bank's situation progressively deteriorated, culminating in its failure in 2017.

On June 6, 2017, the ECB determined that Banco Popular was "failing or likely to fail" (European Central Bank, 2017) as a result of the lack of liquidity to fund withdrawal requests, even though the ECB acknowledged that Banco Popular complied with capital requirements. The SRB, in coordination with the ECB and other relevant authorities, decided to apply a resolution measure to Banco Popular, determining that the sale of a business tool for transferring shares to a purchaser aligned with resolution objectives and protected the financial stability of both the Spanish and Euro Area financial markets. The resolution process involved executing the write-down and conversion of capital instruments immediately before the application of the sale of business tool. Additionally, a recovery plan was not adopted because the directive does not permit it once a bank has been declared FOLTF.

Banco Popular was put into an expedited sale process conducted by the Spanish resolution authority (FROB), with only one bank (Santander) submitting an offer of one euro, coinciding with the minimum price stipulated by the SRB, which was accepted by the relevant authorities as an alternative to ensure the continuity of critical functions and to protect depositors and financial stability.

Shareholders and subordinated creditors incurred accounting losses of EUR 11.4 billion as a result of the resolution of Banco Popular. This has led to divergences in the interpretation of the case and to numerous legal proceedings regarding the decisions made by Spanish and European authorities, challenging the performance of the SRM and compliance with the BRRD and SRM Regulation.

In this context, this thesis aims to assess the effectiveness of the SRM, under the responsibility of the SRB, in managing the Banco Popular crisis. It seeks to evaluate whether Banco Popular was successfully resolved under the architecture of the SRM by examining the compliance of the entire process with the principles and procedures outlined by the BRRD.

With this objective in mind, our analysis will be based on Banco Popular as a unique case study. The methodological approach we will use to collect and analyse the empirical information will be both qualitative and quantitative, utilizing information available in the literature, procedures and official documents of the European Union, reports from independent auditors, recent legal documents regarding controversies surrounding the case, and an interview with a representative of the interested parties.

The paper is structured as follows. Section 2 provides an overview of existing studies, the objectives of the work, and the question we intend to address. Section 3 discusses the methodology that will be used. Section 4 provides a literature review, detailing the events that triggered the resolution of Banco Popular, the specific steps of the resolution process, and the economic and legal issues that arose following the conclusion of the process. Section 5 analyses, evaluates, and discusses the adherence to the principles and procedures outlined by the BRRD in the case study under analysis. Section 6 presents a critical overview of the Banco Popular resolution process. Section 7 concludes the study by answering the starting question and giving some notes for further research.

2. OVERVIEW OF RELEVANT STUDIES, KEY QUESTION AND PURPOSE

Even though seven years have passed since the resolution of Banco Popular on June 6, 2017, it remains a relevant topic due to its ongoing controversy. From the distance, the resolution is perceived as a success, as it achieved closure resolving a bank that had faced financial difficulties for a number of years prior to its resolution. However, Banco Popular's stakeholders and several academics contend that the resolution of Banco Popular was highly problematic.

The resolution of Banco Popular has inspired an already relatively large body of literature and analyses (Fonts and Sabaté, 2018; Bogen and Pelli, 2018; Reffet, 2020; Urbaneja Cillán, 2022).

The existing literature focuses on various aspects, such as the legal framework of the SRM, the decision-making process of the SRB, the implications for shareholders and creditors, the effectiveness of the resolution in maintaining financial stability, and comparisons with other bank resolution cases.

Fonts and Sabaté (2018) compare the Banco Popular bail-in case with the bail-out cases of Veneto Banks and Monte dei Paschi di Siena, using a methodology based on Stock Prices and CDS Spreads.

Bogen and Pelli (2018) examine the effects of the implementation of the BRRD on the process for failing financial institutions, with Banco Popular as a case study, focusing their analysis on the effectiveness of key ratios imposed by regulators to evaluate early warning signals for the bank.

Reffet (2020) explores the wider implications of the resolution of Banco Popular on the subordinate debt market and regulatory authorities, suggesting that the broader implications of the event regarding the structuring of contingent convertible bonds (CoCos), valuation of capital structures, and trigger levels contradict the recent shift in approach by the ECB following the consequences of the Covid-19 crisis.

More recently, Urbaneja Cillán (2022) focuses on the Banco Popular case with the aim of analyzing the legality of the SRM under European Union law.

Other researchers present articles whose focus is not Banco Popular as a case study but make reference to it due to its relevance and visibility as a pioneer in the application of the SRM by the SRB in the field of the European Banking Union.

Among other scientific papers, Ghibellini (2021) focuses on examining how the interaction between resolution rules BRRD and State aid rules can mitigate potential distortions of competition during bank failures, integrating concerns related to various aspects of banking regulation and competition policy.

Donnelly and Pometto (2024) provides insights into the comparative analysis of varieties of financial capitalism, economic nationalism, and bank resolution, focusing on Spain and Italy's approaches to managing bank insolvency and resolution from 2008 to 2018.

Given the significance and prominence of the event in a world where banks play a key role in the economy, we will analyse, in the case study of Banco Popular, the implementation of the SRM carried out by the SRB. Although this study is not groundbreaking, it offers a new approach by aiming to determine whether the SRM was

effective in resolving Banco Popular, focusing specifically on adherence to the principles and alignment with the procedures outlined by the BRRD.

As a more recent work, it provides a much more comprehensive level of detail and incorporates subsequent developments. Specifically, it offers a much deeper analysis of the historical events and the resolution process itself compared to all previous existing studies. It also encompasses the more recent position disclosed by the General Court in response to the legal proceedings initiated against the European institutions involved in the process, which were made public in June 2022 and November 2023.

To evaluate the effectiveness of the SRM in addressing the Banco Popular crisis, we gathered information from various sources including literature, procedures and official documents of the European Union, independent auditors' reports, and judgements from the General Court related to cases against the SRB submitted to the court (Case No. T-481/17 and Cases no. T-302/20, T-303/20 and T-307/20). Additionally, we conducted an interview with a representative of the interested parties.

The aim of the research was to address the following question:

- Were the procedures outlined in the BRRD followed effectively in the resolution of Banco Popular? How and why?

To address the mentioned question, the following objectives were pursued in the study:

- I. The first aim was to sequentially analyse the series of events since the 2008 crisis that led to the decision to resolve Banco Popular.
- II. The second aim was to further explore the resolution process conducted by national and European entities, which ultimately resulted in the sale of Banco Popular to Santander.
- III. The third aim was to examine in detail certain post-resolution issues and their economic and legal context.
- IV. The fourth aim was to determine, based on all compiled information, whether the resolution of the Banco Popular crisis was effectively managed in line with the European banking framework, particularly the BRRD.

3. METHODOLOGY

“A case study is an empirical inquiry that investigates a contemporary phenomenon within its real-life context; when the boundaries between phenomenon and context are not clearly evident; and in which multiple sources of evidence are used.”

In Yin, R. K. (2009), p. 23.

We consider the Case Study design appropriate for this investigation given that it is the first case of bank resolution in the European Union under the responsibility of the SRB and because it is, *de facto*, the only case where the SRB has adopted a resolution measure to a large bank.

As a single case study, the phenomenon was analysed within a real-life context and the research adopted a simultaneous approach of quantitative and qualitative analysis, typical of which included the utilization of multiple data sources such as direct detailed observations, interviews, and documents (Rowley, 2002).

As highlighted by Larrinaga (2017), widely used tests in empirical research to ensure the rigor and quality of the research were taken into consideration:

- Construct validity: The analysis of multiple sources of information (data triangulation) strives to create analytical standards and generate explanations about the phenomenon under study.
- Internal validity: The data collection process utilizes various sources and aims to establish evidence chains.
- Reliability: Regarding data collection, it adheres to the case study protocol and will organize, integrate and synthesize the information obtained from the different sources of evidence.
- Theoretical-interpretative consistency: A prior understanding of the perspectives related to the phenomenon and its context based on evidence sources, followed by a systematic and critical analysis.

In our research process, we followed the data triangulation methodology by gathering data from multiple sources and using various pieces of evidence. We also ensured a simultaneous quantitative and qualitative approach as we considered not only Banco

Popular financial reports and reports from independent auditors, but also information available in the literature, procedures and official documents of the European Union, as well as legal documents regarding the case.

Additionally, in order to incorporate true-to-life information about facts and enrich our empirical material, two interview scripts were created with relevant questions for this dissertation. Various participants in the Banco Popular's resolution process were contacted to participate either via MS Teams or, alternatively, by responding to the interview guide in writing via e-mail.

Out of the 15 individuals we reached out to, the majority declined to participate because the subject matter is sensitive and currently under legal scrutiny. The two interview guides, along with the contacts made and the responses received from the participants, are available in Appendix A.

Only the law firm Ramón C. Pelayo Abogados, represented by its managing partner, Mr. Ramón C. Pelayo, agreed to participate in this project through an interview, which was conducted via MS Teams on May 7th. The transcription of this interview is available in Appendix B, and its contribution has been included in section 5 of this dissertation.

4. THE CASE OF BANCO POPULAR

4.1. Background

4.1.1. The Spanish banking sector

The cumulative effects of the 2007-2009 financial crisis, sparked by the subprime mortgage crisis, the real estate collapse in Spain and the Euro Area sovereign debt crisis of 2010-2012 resulted in large and losses and brought to light vulnerabilities in the capitalization of Spanish financial institutions.

Indeed, factors such as the burst of the real estate bubble, increased non-performing loans, falling house prices, excessive leveraging, and risk-taking by financial institutions heightened the need for capital and provisions in banks. Regulatory requirements were strengthened to mitigate systemic risk and ensure more realistic valuation of real estate assets.

The crisis affected mainly savings banks, the so called ("Cajas"), leading to the creation of the Fund for Orderly Bank Restructuring (FROB) in 2009, a state-owned agency responsible for managing restructuring processes and channeling public aid to financial institutions.

Between 2009 and 2012, EUR 15 billion was injected into eight savings banks by the FROB, with an additional EUR 7.9 billion provided by the Deposit Guarantee Fund. In July 2012, the European Union approved up to EUR 100 billion in financial support to recapitalize the Spanish financial sector, with EUR 55.9 billion used for direct recapitalization of banks through the FROB (World Bank Group, 2016). Only two banks met their capital requirements without resorting to state aid, which were Banco Popular and Ibercaja.

As part of this process of restructuring and recapitalizing the banking sector, Spanish authorities forced a significant consolidation of the sector with stronger banks absorbing weaker ones. The number of savings banks ("Cajas") decreased by two-thirds, from 45 in 2008 to 15 in 2012.

4.1.2. Banco Popular

Banco Popular was founded in 1926 and operated primarily as a domestic bank, with a particular focus on SMEs, groups, and families. Its business model centered around SMEs, holding a market share of 16.7% in Spain (Single Resolution Board, 2016).

TABLE I - BANCO POPULAR-TOTAL ASSETS AND CONSOLIDATED RESULTS 2008-2017

(MILLIONS OF €)

	31.12.2008	31.12.2012	31.12.2015	31.12.2016	31.03.2017
Total Assets	101 583	157 618	158 650	147 926	147 114
Consolidated Results	892	(-) 2 461	106	(-) 3 485	(-)137

Sources: PricewaterhouseCoopers, 2009; Banco Popular Español S.A.,2013;

Banco Popular Español S.A., 2017a; Banco Popular Español S.A.,2017b.

Following the financial crisis, the bank had survived previous restructurings and mergers by assimilating smaller competitors, securing foreign investment from Varde Partners, Citibank, Bx+, and Dexia, selling off assets and divisions to raise capital, and using the proceeds to address the financial challenges of the savings banks ("cajas") it acquired (Donnelly and Pometto, 2024).

Indeed, in 2008, the bank decided to improve their liquid positions by consolidating the regional banks (among others, Banco de Castilla). Subsequently, in 2011, Banco Popular acquired Banco Pastor, the oldest Spanish bank, after Banco Pastor failed the EBA stress test.

Banco Popular had been recording a high exposure to real estate assets which it maintained to avoid recognizing losses, further worsening its situation, and putting it in difficulty. In addition, Banco Popular continued to face problems concerning the escalating levels of non-performing loans.

As part of the accompanying restructuring of the Spanish financial system in 2012, independent experts on behalf of the ECB and IMF determined the solvency needs of Spanish entities, revealing in September 2012 that Banco Popular had a capital deficit of EUR 3.2 billion in the most adverse scenario. This led to a capital increase in November 2012 of EUR 2.5 billion without recourse to state aid but through an emergency issuance, thus ensuring compliance with regulatory requirements (Urbaneja Cillán, 2022).

However, shareholders reacted negatively to the news, especially since dividends were also reduced in October as part of an effort to build up capital.

The capital increase was used foremost to recognize impairments and to constitute provisions on non-performing loans. As a result, Banco Popular reported a net loss of EUR 2.46 billion for 2012, exacerbated by the ongoing rise in non-performing loans, which reached 8.98% in the last quarter of 2012 and then surged to 14.5% by July 2013. This increase was attributed to the Bank of Spain's new policy, which criticized domestic banks for being overly optimistic in their treatment of restructured debt, failing to make adequate provisions for potential future losses, and not accurately valuing their bad loans (Guillem and Fonts, 2018).

Despite that, Banco Popular passed the 2014 ECB stress test of Euro Area significant banks.

TABLE II - BANCO POPULAR – SOLVENCY

(MILLIONS OF € AND %)

	31.12.2015	31.12.2016	31.03.2017
CET1 Capital	9 827	7 808	6 100
CET1 Ratio (%)	13,14%	12,13%	10,02%
TIER 1 Capital	9 828	7 808	6 616
TIER 1 Ratio (%)	13,14%	12,13%	10,87%
TIER 2 Capital	494	655	636
TIER 2 Ratio (%)	0,66%	1,02%	1,04%
Total Capital	10 322	8 463	7 252
Total Capital Ratio (%)	13,80%	13,15%	11,91%
Risk Weighted Assets (RWA) total	74 778	64 372	60 886

Source: Banco Popular Español S.A., 2017a; Banco Popular Español S.A., 2017b.

Later, in May 2016, banks in Southern Europe began to face pressure from the SSM (ECB) to reduce their bad debts and increase provisions for non-performing loan ratios. Supervisory authorities asked Banco Popular to raise capital, which it did through another capital increase of EUR 2.5 billion, covered with a 36% oversubscription of newly issued shares by private sector investors. In July 2016, the results of stress tests were released by the EBA, indicating that the CET1 ratio would reach 13.45% in 2016 in the baseline scenario, dropping to 7.01% in 2018 in the adverse scenario (Mesnard et al, 2017).

However, despite the bank's compliance with capital regulatory requirements, it was one of the weakest banks in the 2016 ECB-EBA stress tests (Pérez-Rodríguez et al, 2022), and there was an evident trend of capital deterioration between 2015 and 2017 (see Table II), as the bank restructured reducing risk weighted assets and total assets.

Note that in 2016, Banco Popular ranked as the sixth-largest bank in Spain in terms of market capitalization. With total assets of EUR 147.9 billion, it served 4.6 million customers through 1,739 branches and employed 11,948 workers (Banco Popular Español, S.A., 2016).

On December 5, 2016, the SRB approved a first resolution plan for Banco Popular, in which it determined that a liquidation under normal insolvency proceedings would not be effective, as it could impact not only the real economy but also the stability of the Spanish financial system. In the 2016 version, it was determined that the most appropriate resolution strategy would be the application of the bail-in, and the strategy would be divided into two phases: a stabilization phase, in which “the bail-in tool would be applied at the level of the parent entity of the group (Banco Popular Español S.A.)”; and, a restructuring phase, “in which the management of the entity or group in resolution must submit a business reorganization plan within one month” after the application of the bail-in tool (Single Resolution Board, 2016, p. 23).

In 2016 and 2017, the SSM (ECB) conducted on-site inspections of Banco Popular. The 2016-2017 inspections resulted in the ECB requiring at the beginning of 2017 that Banco Popular acknowledge EUR 5.7 billion of additional provisions on its real estate portfolio. Consequently, even though Banco Popular's results before provisions were positive, it ended the year with losses of EUR 3.5 billion (as can be seen in table I), after provisions of EUR 5.7 billion in 2016, consuming the capital increase made months earlier (Banco Popular Español S.A., 2016). The publication of these financial challenges on February 3, 2017, resulted in ratings downgrades and an increase in deposit outflows.

On February 10, 2017, DBRS Morningstar (then known as DBRS Ratings Limited) downgraded Banco Popular's rating due to its weakened situation.

Later, on February 20, 2017, following a year of poor performance attributed to bad loans, Mr. Emilio Saracho replaced Mr. Angel Ron and became the new Chairman of Banco Popular.

In April 2017, CEO Pedro Larena resigned following the publication of an audit revealing that the bank had under-provisioned of bad loans portfolio for EUR 600 million and had also revealed unreported loans to clients to buy shares in the 2016 capital increase (Mesnard et al, 2017). Therefore, it announced corrections would be necessary in the financial report for the first quarter of 2017.

Following Banco Popular's announcement regarding the need for result adjustments, DBRS downgraded Banco Popular's rating again on April 6, a move followed by Moody's and Standard & Poor's on April 7.

In the same month, Banco Popular initiated a sales process to a competitor with a first deadline of June 10, 2017, later delayed to the end of June, aiming to restore its stability.

On 5 May 2017, Banco Popular released its financial report for the first quarter of 2017 with provisions of EUR 500 million and net losses of EUR 137 million. Banco Popular would have positive results without the provisions.

On May 12, 2017, because of the continuing and growing pressure on funding, Banco Popular fell below the minimum threshold of 80% of the Liquidity Coverage Requirement, as outlined in Regulation (EU) No 575/2013 of the European Parliament and of the Council, dated June 26, 2013.

Following the sale process announced by Banco Popular, Santander formally informed, by letter dated May 16, that, despite their interest, the conditions for submitting a final proposal were not yet met.

The bank was now facing not only credit risk but also increasing reputational risk.

On May 23, 2017, the chair of the SRB, Elke König, was interviewed on Bloomberg TV and, when questioned about the situation of Banco Popular, she declined to comment on specific cases but mentioned that Banco Popular was one of the banks they were monitoring, thus exacerbating the situation (Bloomberg, 2017).

It's worth noting that in the same month, a Reuters article dated May 31, 2017, revealed that the chair of the SRB warned EU officials that Banco Popular could be closed if a buyer was not found, with this statement negatively contributing to the run-on deposits (Reuters, 2017a).

Due to the news and rumors circulating in the media, market pressures intensified, and Banco Popular's stock price plummeted due to significant withdrawals of liquidity. Additionally, national government authorities also made massive withdrawals of their deposits from the institution, leaving the bank quickly without liquidity.

On June 5, 2017, in the morning, Banco Popular found itself in need of requesting EUR 2.0 billion of Emergency Liquidity Assistance from the Bank of Spain. During the afternoon of the same day, it requested an additional EUR 1.6 billion of Emergency Liquidity Assistance as an extension of the initial amount requested, due to significant deposit withdrawals. Banco Popular reportedly provided collateral worth EUR 40.0 billion to the Bank of Spain, suggesting that the Bank of Spain imposed a 90%+ haircut on collateral (Mesnard et al, 2017; Cabral, 2022), precipitating Banco Popular's failure. On June 6, 2017, the Board of Directors of Banco Popular informed the ECB that the bank would be unable to meet withdrawal requests, as it lacked liquidity and acceptable collateral to obtain further Emergency Liquidity Assistance from the Bank of Spain.

On June 6, 2017, Banco Popular's rating was once again lowered by Moody's and DBRS.

A summary of the events leading up to the fall of Banco Popular is outlined in Appendix C.

4.2. Resolution Process

The ECB determined that Banco Popular "was failing or likely to fail" (FOLTF) on June 6, 2017, according to Article 18, paragraph 1, of the SRM Regulation, stating that "the significant deterioration of the liquidity situation of the bank in recent days led to a determination that the entity would have, in the near future, been unable to pay its debts or other liabilities as they fell due," and informing the SRB accordingly (European Central Bank, 2017). Nonetheless, the ECB stated that Banco Popular fully complied with capital requirements.

The next day, the SRB promptly adopted a resolution program, bailed in existing shares and Additional Tier 1 instrument and Tier 2 instruments, and "transferring all (resulting) shares and capital instruments of Banco Popular Español S.A. (Banco Popular) to Banco Santander S.A (Santander)" (Single Resolution Board, 2017c) for one euro, thus

allowing Banco Popular to “operate under normal business conditions as a solvent and liquid member of the Santander Group with immediate effect” (Single Resolution Board, 2017c).

The SRB grounded its decision on the need to protect Banco Popular's depositors and its critical functions, avoiding impact on financial stability and the real economy, without using public funds (Single Resolution Board, 2017c) in accordance with the objectives of resolution, as outlined in Article 14, paragraph 2, of SRM Regulation.

The resolution scheme was submitted to the European Commission at 5:13 am on June 7.

On the same day, at 6:30 am, the European Commission approved the resolution scheme, based on the SRB's proposal and in accordance with the EU's bank recovery and resolution rules. It was considered that the conditions for the resolution of Banco Popular were met, namely "the bank was failing, there were no private sector solutions outside of resolution, and there were no supervisory actions that would have prevented its failure." In the specific case, "losses were fully absorbed by shares and subordinated debt" (European Commission, 2017).

The entire decision-making and approval process was achieved quickly and with agility, adhering to the resolution procedure and timelines established in detail in Article 18 of the SRM Regulation. According to this article, the resolution program adopted by the SRB only takes effect if, within 24 hours of its adoption, no objections are raised by the Council or the European Commission, or if the resolution program is approved by the European Commission.

“The decision taken today safeguards the depositors and critical functions of Banco Popular. This shows that the tools given to resolution authorities after the crisis are effective to protect taxpayers’ money from bailing out banks.”

Elke König, Chair of the SRB.

In Single Resolution Board (2017c).

4.3. Valuations conducted throughout the Process

In the context of resolution, and with the goal of supporting and validating the decisions made by resolution authorities, Directive 2014/59/EU and SRM Regulation (EU) No 806/2014 stipulate three types of valuations, each serving a distinct purpose.

Valuations 1 and 2 are provisional and take place before a resolution, whereas Valuation 3 is definitive and occurs after a resolution. Furthermore, both Valuations 2 and 3 must be conducted by an independent entity.

i. Valuation 1

In the case of Banco Popular, valuation 1 is dated June 5, 2017.

Drafted by the SRB, its purpose was to determine whether Banco Popular was in a situation or at risk of insolvency and to assess whether the conditions for triggering a resolution procedure were met, as provided for in Article 20, paragraph 5, of the SRM Regulation and in accordance with Article 18, paragraph 1, of the same Regulation.

As mentioned in valuation 1 (Single Resolution Board, 2017a), the objective was to confirm whether Banco Popular met the requirements to be considered "failing or likely to fail" by meeting the criteria defined in Article 18, paragraph 4, of the SRM Regulation, which we cite:

“(a) the entity infringes, or there are objective elements to support a determination that the institution will, in the near future, infringe the requirements for continuing authorisation in a way that would justify the withdrawal of the authorisation by the ECB, including but not limited to the fact that the institution has incurred or is likely to incur losses that will deplete all or a significant amount of its own funds;

(b) the assets of the entity are, or there are objective elements to support a determination that the assets of the entity will, in the near future, be less than its liabilities;

(c) the entity is, or there are objective elements to support a determination that the entity will, in the near future, be unable to pay its debts or other liabilities as they fall due.”

The present valuation had a provisional and urgent nature considering the deterioration and deposit outflows that had been observed in recent days, based on the last March 31 quarter report on a consolidated basis.

The method of this valuation was to determine if the total value of the entity's assets exceeded that of its liabilities. Valuation 1 concluded that as of the valuation date (31.03.2017), Banco Popular was solvent, with net assets valued at 8.4 billion euros, and that the conditions for being considered FOLTF were not met.

It is noteworthy that, according to the SRB, valuation 1 became obsolete on June 6, 2017, as a consequence of the FOLTF assessment by the ECB on that date.

ii. Valuation 2

Valuation 2 regarding Banco Popular is dated June 6, 2017.

Drafted by Deloitte, acting as an independent expert, its objective was to assess the value of the entity's assets and liabilities in a sale of business scenario, estimate the treatment that shareholders and creditors would have received if it were a normal insolvency process, and provide data to enable the SRB to define the conditions for the application of the activity disposal tool, in accordance with Article 20, paragraph 10, of the SRM Regulation.

The independent valuation by Deloitte (requested in May 2017, prior to the decision on the resolution scheme) adopted a category-by-category approach and most of the information used was as of 31 March 2017 and conducted on a consolidated basis.

Their provisional economic valuation focused on the areas below and estimated that the value of the bank would reach EUR -8.2 billion in a stressed scenario, EUR -2 billion in a base scenario and EUR 1.3 billion in a best scenario.

TABLE III - OUTCOME OF THE ECONOMIC VALUATION

Area	Adjustments (*) (€ billion)		
	Best case	Worst case	Best estimate
Loans and receivables	-2,7	-7,0	-3,5
Real estate assets	-2,6	-3,4	-3,1
Deferred tax assets	-2,7	-3,0	-2,7
Legal contingencies			
Intangible assets	-2,2	-2,6	-2,2
Equity and Fixed Income	-0,4	-0,5	-0,5
Joint ventures, associates and subsidiaries	0,1	-0,6	-0,3
Total adjustments	-18,8	-20,6	-14,7
Consolidated equity as of March 2017	10,8	10,8	10,8
Subtotal	-1,0	-9,8	-3,9
Cost savings **	2,3	1,6	1,9
Other sources of valuations adjustments ***	Not quantified	Not quantified	Not quantified
Adjusted equity	1,3	-8,2	-2

(*) Adjustments are not reflective of an accounting basis

(**) Including restructuring costs

(***) Including potential contractual adjustments, upsides regarding Hippocrates' market position

Source: Valuation 2 Report (Deloitte, 2017)

On the other hand, the table below details the best and worst-case scenarios for creditors regarding potential total recovery and implied losses.

TABLE IV- OUTCOME OF THE ALTERNATIVE OUTCOME SCENARIO

(€ billion)	Worst	Best
Total recovery available for creditors	107,7	111,6
Implied losses (for consolidated liabilities and equity as of March 2017)	-31,1	-27,2

Source: Valuation 2 Report (Deloitte, 2017)

Following valuation 2, the SRB issued Decision SRB/EES/2017/08 regarding the adoption of the resolution scheme for Banco Popular (Single Resolution Board, 2017b).

The SRB utilized the sale of business tool in the resolution scheme of Banco Popular, by transferring shares to a purchaser.

As detailed in Article 6.1 of the resolution scheme (Single Resolution Board, 2017b), the SRB decided:

- Firstly, to write down the nominal amount of Banco Popular's share capital in an amount of EUR 2.098.429.046, resulting in the cancellation of 100% of Banco Popular's share capital.

- b) Secondly, to convert all the principal amount of the additional Tier 1 instruments issued by Banco Popular and outstanding as at the date of the decision relating to the resolution scheme into newly issued shares of Banco Popular ('the New Shares I'),
- c) Thirdly, to write down to zero the nominal amount of the 'New Shares I', resulting in the cancellation of 100% of those 'New Shares I'.
- d) Lastly, to convert all the principal amount of the Tier 2 capital instruments issued by Banco Popular and outstanding as at the date of the resolution decision into newly issued shares of Banco Popular ('the New Shares II').

The sale of business tool was expedited by the fact that in the weeks prior, a buyer for Banco Popular was already being sought, and thus, the bank's accounts had already been duly analyzed.

Indeed, on June 6, 2017, the Spanish resolution authority (FROB), to whom the SRM addressed the execution of the resolution instrument of Banco Popular (as per Articles 18, paragraph 9 and Article 29 of the SRM Regulation), had set the deadline for proposal submissions until midnight of the same day.

Among the initial five potential bidders, one was excluded by the ECB and two declared they had no interest. Of the remaining two, BBVA and Santander, the first one communicated its decision not to submit a proposal on June 6, 2017, thus making Santander the sole bidder.

Consequently, the FROB indicated that Santander would be the only bank meeting the requirements to proceed with the purchase of Banco Popular and the sole interested party, having submitted the purchase offer for the defined minimum value.

All the shares and debt of Banco Popular were transferred to Santander for the symbolic value of one euro.

iii. Valuation 3

The Valuation 3 of Banco Popular, a valuation of the bank in a liquidation scenario, was drafted by Deloitte acting as an independent expert. It commenced in June 2017 and was made available on June 14, 2018, with an addendum dated July 31, 2018, correcting certain clerical errors in the report.

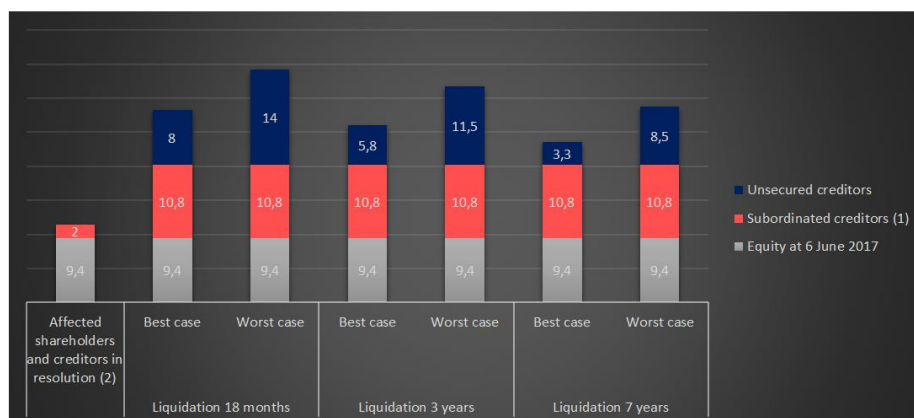
As stipulated in SRM Regulation (Article 20, paragraph 16), after the conclusion of the resolution process of Banco Popular, the SRB requested a valuation from an independent entity (Deloitte) to "evaluate whether shareholders and creditors would have received more favorable treatment if the institution subject to resolution had entered into a normal insolvency process." If so, the SRB would have to compensate shareholders for having "suffered greater losses than they would have suffered in the event of liquidation in accordance with normal insolvency proceedings" (Article 76, paragraph 1, subparagraph e, of SRM Regulation). Thus, valuation 3 is key to verifying that the resolution measure complies with the NCWO principle.

Valuation 3 concluded that the opening of a normal insolvency proceeding would be destructive, for reasons including: the abrupt cessation of business; customer attrition; an inefficient asset realization process; and additional (often significant) costs and claims (Single Resolution Board, 2018).

As a method of analysis, Deloitte considered three alternative time scenarios for a liquidation under normal insolvency proceedings, and for each scenario, the report presented the best and worst-case outcomes as detailed below.

FIGURE 1 – OUTCOME FOR BANCO POPULAR LEGAL ENTITY (CREDITOR LOSSES)

(BILLIONS OF €)



(1) This includes €2.0bn of subordinated debt and €8.6bn of intra-group debt, totaling 10.8bn.

(2) All creditor's losses in resolution (€11.4bn) were suffered by the shareholders and subordinated creditors of Banco Popular legal entity.

Source: Valuation 3 Report (Deloitte, 2018)

The 18 month scenario reflects the Spanish Insolvency Act, and was deemed by Deloitte as extremely unlikely considering the size and complexity of the Bank. The 3 years scenario was considered by Deloitte as the minimum period to liquidate assets in an efficient way. And, the 7 years scenario was considered by Deloitte as a longer-term work out of assets to obtain higher recoveries.

In all three scenarios, the losses would always exceed those recorded in the resolution scheme used. Additionally, in the resolution scheme, only the affected shareholders and creditors of the Bank were impacted, whereas here, unsecured creditors would also bear losses.

As mentioned in the “Explanatory Note on the Valuation 3 Report” (Single Resolution Board, 2018), the most important factors driving Deloitte’s conclusions were: a) a significant reduction in the valuation of the Bank’s loan portfolio, driven by estimated prepayment behaviour on the performing loan portfolio and discounts required to achieve disposal of the nonperforming and ‘rump’ performing loan portfolios, b) reductions in the value of securities, real estate, intangible assets, and tax assets, and c) liquidation costs (remuneration costs, cost arising from the termination of contracts, employee costs including the process for collective dismissal and operating costs), and estimates of legal contingencies.

On March 17, 2020, following valuation 3, the SRB published the final Decision SRB/EES/2020/52 (Single Resolution Board, 2020), in which it determined that shareholders and creditors were not entitled to compensation. As stated in the document accompanying the Final Decision, the evaluator concluded in valuation 3 that no recoveries would have been expected in a normal insolvency proceeding, and consequently, affected shareholders and creditors would not have received better treatment if the institution had entered normal insolvency proceedings compared to the actual treatment received in resolution.

4.4. Legal and Economic issues in the aftermath of Resolution

After the resolution of Banco Popular, various opinions emerged regarding the effectiveness of the resolution process in the case of Banco Popular.

While regulators considered the first test of the Single Resolution Mechanism carried out by the SRB to be a success, questions began to arise from aggrieved parties regarding the process. Indeed, it was the first time that losses were borne by shareholders and bondholders without the use of public funds.

As argued by Guillem and Fonts (2018), although Santander established a compensation scheme of EUR 1 billion in an attempt to dissuade claimants from suing not only Santander but also the former management of Banco Popular and the supervisory institutions, this proved to be unsuccessful.

In fact, more than 300,000 bondholders and shareholders initiated litigation processes against European institutions in an attempt to overturn the resolution decision, which resulted in losses of around EUR 4 billion (Reuters, 2017b).

A Judgment of the General Court dated June 1, 2022, was made public and contributed to establishing the General Court's jurisprudence on the resolution of Banco Popular (Urbaneja Cillán, 2022), concluding that the process respectfully complied with European regulations. Subsequent Judgments of the General Court, made public on November 22, 2023, further clarified positions regarding Valuation 3, with the General Court also concluding that the entire process complied with European regulations.

Following the mentioned Judgments of the General Court, it becomes important to highlight and detail some issues raised in the post-resolution phase in the specific case study of Banco Popular, contrasting, on one hand, the raised claims, and on the other hand, the position of European institutions regarding the application of the Single Resolution Mechanism, which are detailed in the table in Appendix D. It is important to highlight that the table contains the topics raised that we consider most relevant to this study.

In fact, the General Court concluded “the actions seeking annulment of the resolution scheme in respect of Banco Popular and/or the Commission decision endorsing that scheme are dismissed in their entirety” (Court of Justice of the European Union, 2022) and that the affected shareholders and creditors “would not have received better treatment in the event of the liquidation of the bank than that resulting from its resolution” (Court of Justice of the European Union, 2023).

5. EFFECTIVENESS OF THE SINGLE RESOLUTION MECHANISM IN RESPONDING TO BANCO POPULAR'S CRISIS UNDER THE BRRD

This Section aims to evaluate the effectiveness of the resolution process applied to the case study of Banco Popular, particularly the compliance with the principles and alignment with the procedures determined by the BRRD. This assessment will also consider not only the positions taken by the Court in judgments dated June 1, 2022 (Case No T-481/17), and November 22, 2023 (Cases No T 302/20, T 303/20, and T 307/20), but also insights provided by the interview conducted with Mr. Ramón C. Pelayo, as managing partner of the law firm Ramón C. Pelayo Abogados, which represented various shareholders of Banco Popular in Case No T-481/17. From these inputs, we will draw our conclusions and propose improvements.

5.1. Evaluating the ECB's Oversight Prior to Resolution

In accordance with Article 4 of the BRRD, paragraph 10, subparagraph a, Banco Popular was considered a significant financial institution within the financial system since the total value of its assets exceeded EUR 30 billion, thus meeting one of the requirements for direct supervision by the ECB to be triggered.

For this reason, it was subject to direct supervision by the ECB from the official start of the single supervisory mechanism, in November 2014, throughout the period leading up to the determination of its resolution, which formally consisted in a FOLTF assessment by the ECB on June 6, 2017, due to the significant deterioration of liquidity situation of the Bank, and a resolution decision by the SRB on June 7, 2017.

Banco Popular faced significant challenges stemming from its high exposure to real estate assets, which it refrained from recognizing as losses, exacerbating its financial difficulties. This situation was compounded by escalating levels of non-performing loans.

An assessment on behalf of ECB and IMF in September 2012 revealed a capital deficit of EUR 3.2 billion in an adverse scenario, leading to a capital increase of EUR 2.5 billion

in November 2012. Despite these efforts, Banco Popular reported a net loss of EUR 2.46 billion for 2012, aggravated by the continuous rise in non-performing loans¹.

In 2014, the ECB and the EBA conducted a stress test of all significant Euro Area banks including Banco Popular. Even though it passed the 2014 ECB-EBA stress test, Banco Popular faced increased pressure from supervisory authorities in May 2016 to address bad debts and raise capital. Another capital increase of EUR 2.5 billion followed, but despite regulatory compliance, the bank remained one of the weakest in the 2016 ECB-EBA stress tests. Subsequent ECB on-site inspections in late 2016 and earlier 2017 revealed the need for additional provisions in the amount of EUR 5.7 billion on its real estate portfolio, leading to significant losses and ratings downgrades.

Market pressures intensified in 2017, exacerbated by rumors and media speculation, leading to significant withdrawals of liquidity by both depositors and national government authorities. Banco Popular's stock price plummeted. Further, while Banco Popular formally complied with capital requirements throughout the entire period including during its resolution, from May 12, 2017, onwards, it entered a stage of non-compliance with CRD and CRR liquidity requirements, namely the “Liquidity Coverage Requirement”. Despite efforts to sell the bank to restore stability and requests for emergency liquidity assistance, conditions for further injections were considered as not met². On June 6, 2017, Banco Popular informed the market and supervisory and resolution authorities that it would be unable to meet liquidity obligations.

According to the viewpoint of the interviewee, the collapse of Banco Popular was a result of the ECB's absolute passivity, which he believes should have intervened much earlier with proactive measures.

He added that access to emergency liquidity assistance on June 5, 2017, could have allowed Banco Popular to resist for a few more days, but it became irrelevant because, in his view, Banco Popular was already doomed on the 3rd, 4th, and 5th due to liquidity fluctuations.

¹ Further details on this topic can be found in Section 4.1.2.

² Further details on this topic can be found in Section 4.1.2.

Finally, he mentioned that the ECB should have acted differently in response to the internal struggles within the Board of Directors and felt that the changes in executive management contributed to the bank's instability and market distrust.

In fact, competent authorities must be able to monitor and address the economic and financial deterioration of an institution, preventing it from progressing to resolution.

It is our understanding that the corrective measures imposed by the ECB, namely the successive capital increases and the need for additional provisions under ECB supervision, ensured a consistent application of regulations and policies in matters of supervision but proved ineffective in altering the outcome of Banco Popular.

Plus, Banco Popular's request on June 5, 2017, for emergency liquidity assistance totaling EUR 3.6 billion, for which the national supervisory authority, the Bank of Spain, demanded collateral of EUR 40 billion (Mesnard et al, 2017; Cabral, 2022), if correct, seems to us not to have facilitated, but rather precipitated, the bank's downfall and resolution.

We also argue that the use of more detailed stress tests by the ECB and EBA could have provided a more assertive view of Banco Popular's problems, anticipated or contained the situation earlier, and eventually prevented the triggering of the resolution.

Finally, the passive conduct of the ECB in the face of the increasing media coverage that contributed to the deterioration of the bank's situation further complicates matters.

5.2. Examining the SRB's Approach to Resolution Process and Mechanisms

As defined in Article 32 of the BRRD, paragraph 1, subparagraphs a and b, the resolution process should be initiated when a competent authority, after consulting a resolution authority, determines that an institution is in a situation or at risk of insolvency and that the adoption of alternative measures cannot prevent such insolvency situation within a reasonable time frame.

According to paragraph 4 of the same article, an institution shall be considered to be in a situation or at risk of insolvency when it fails, or is at imminent risk of failing, to meet one or more of the following requirements:

- a) the institution has ceased to comply, or there are objective elements indicating that the institution will cease to comply within a short period, with the requirements necessary for the continuation of its authorization, to such an extent that withdrawal of that authorization by the competent authority would be justified, notably, but not exclusively, because the institution has incurred or is likely to incur losses that will lead to the total exhaustion, or significant reduction, of its own funds;
- b) the assets of the institution are, or there are objective elements indicating that they will be, within a short period, less than its liabilities;
- c) the institution is unable, or there are objective elements indicating that it will be unable, within a short period, to pay its debts and other obligations as they fall due;
- d) extraordinary public financial support is required to maintain authorization, when the assets of the institution are or are at risk of becoming, within a short period, less than its liabilities, when the institution is unable or is at risk of becoming, within a short period, unable to pay its debts as they fall due, or when the institution requires extraordinary public financial support.

Additionally, according to paragraph 1, subparagraph c of the same article, a resolution measure is considered to be in the public interest if it is necessary and proportionate to achieve one or more of the resolution objectives referred to in Article 31, and if a liquidation process of the institution under normal insolvency proceedings would not achieve the same outcome.

The resolution objectives outlined in Article 31 of the BRRD are as follows:

- a) to ensure the continuity of critical functions;
- b) to avoid significant adverse effects on financial stability, in particular by preventing contagion, including to market infrastructures, and by maintaining market discipline;
- c) to protect public funds by minimising reliance on extraordinary public financial support;
- d) to protect depositors and investors;
- e) to protect client funds and client assets.

It is also stated in the BRRD that an institution in insolvency should be kept in operation through the use of resolution tools, utilizing private funds whenever possible.

The resolution tools, which may be used singly or in combination, are established and defined in the BRRD, Article 37, paragraph 3, which we quote: (a) the sale of business tool; (b) the bridge institution tool; (c) the asset separation tool; (d) the bail-in tool.

Finally, as also referred to in the BRRD, it is necessary to ensure the confidentiality of information obtained by resolution authorities throughout the resolution process and until the resolution decision is disclosed. In fact, information about recovery plans and assessment results may have far-reaching effects not only on the markets in general but also on private interests impacted by specific actions. Furthermore, considering that negotiations with potential acquirers and information regarding the disposal of an institution may have systemic repercussions, it is important that their public disclosure be postponed for the necessary time to ensure financial stability.

In compliance with Article 32, the ECB, as a competent authority, declared Banco Popular as FOLTF on June 6, 2017, due to the significant deterioration in its liquidity situation, using the requirement referred to in paragraph 4, subparagraph c., although it acknowledged that Banco Popular fully complied with capital requirements. The ECB also mentioned that, even with the emergency liquidity injection, whose losses would fall to the Bank of Spain's Treasury, and to which it had not raised objections on June 5, 2017, the liquidity on that date would not be sufficient to meet its commitments on June 7, 2017, given the significant liquidity movements.

“The significant deterioration of the liquidity situation of the bank in recent days led to a determination that the entity would have, in the near future, been unable to pay its debts or other liabilities as they fell due.”

Press Release dated 07.06.2017.

In European Central Bank (2017).

This triggered the SRB to promptly adopt a resolution plan, using the sale of business as the chosen resolution tool, transferring all shares and capital instruments of Banco Popular to Santander³, thus also complying with Article 37, paragraph 3 of the BRRD.

This was facilitated by the prior search for a buyer for Banco Popular in the weeks leading up to the resolution, which allowed for a thorough analysis of the bank's accounts beforehand. This also expedited the sale process and ensured a smooth transition of Banco Popular's operations to the acquiring entity.

The action taken aimed to maintain normal business operations for Banco Popular within the Santander Group, safeguarding depositors and critical functions while avoiding disruptions to financial stability and the real economy. Importantly, this resolution was achieved without the use of public funds and aligned with all objectives of resolution set out in Article 31 of the BRRD.

“The SRB has decided that the sale of business tool for transferring shares to a purchaser meets the resolution objectives and ensures the financial stability in Spain and Portugal, where Banco Popular owns a subsidiary. As a result, the shares, including the entire business of Banco Popular and its subsidiaries, have been transferred to Santander Group as of 7 June 2017. The SRB, by its decision, effectively protects the depositors of Banco Popular and its critical functions to avoid adverse effects on financial stability and the real economy, without using any public funds.”

Press Release dated 07.06.2017.

In Single Resolution Board (2017c).

The General Court's position on this matter was that Banco Popular was indeed at risk of insolvency, considering not only the analysis by the ECB dated June 6, 2017, but also the fact that the Board of Directors themselves had informed that Banco Popular was at risk of insolvency. It was also noted that financial indicators indicated solvency problems, not just liquidity issues, considering significant losses and failures in liquidity coverage

³ This topic is discussed in greater detail in Section 4.3.

requirements. The Court determined that the emergency liquidity injection would be insufficient for the bank to meet its commitments on June 7, 2017, thus it couldn't have been considered an alternative to resolution. Additionally, the interest shown by Barclays Bank and Deutsche Bank in securing a capital increase of EUR 4 billion was not a formal commitment but only discussions at an early stage, so it couldn't be considered an alternative measure to avoid the adoption of resolution.

Furthermore, regarding the proposal by the claimants to replace the members of Banco Popular's management bodies, it was also considered ineffective in restoring market confidence and containing deposit outflows.

Finally, the General Court argued that while the bank's sales process was transparent, it was also intentionally limited and delayed. This limitation and delay were necessary to prevent adverse effects on financial stability, as public disclosure of the sale could have triggered panic among shareholders and depositors. Plus, conducting a prior consultation with all depositors and shareholders before adopting the resolution mechanism would have further delayed the process and weakened its effectiveness.

On the other hand, the interviewee believes that the negligence on the part of the SRB, especially its Chair, Mrs. Elke König, in adopting statements and contributing to rumors, was the cause of the abrupt drop in Banco Popular's liquidity in the last days of May and early June 2017. He also highlighted the evidence of e-mails published in the media, sent by the Chairman of FROB at the time, Mr. Jaime Ponce, to the Chair of the SRB, alerting and expressing his disagreement with the statements she made, as he believed that the damage it would cause to Banco Popular would be terrible.

Regarding the possibility of there being an alternative resolution tool, he pointed out that, as many experts argued, a "bad bank" could have been created, where all insufficiently provisioned real estate assets would have been transferred, thus allowing the restoration of confidence in Banco Popular.

Based on the information provided, we agree that the European authorities' activation of the resolution process for Banco Popular, along with the attainment of resolution objectives and the application of the resolution tool, aligns with the BRRD's stipulations. Given Banco Popular's circumstances, the swift resolution process and the chosen tool

likely represented the most effective and expedient approach to fulfilling the directive's resolution objectives, thereby preventing market destabilization and restoring confidence.

Plus, by finding a private sector buyer, the resolution process sought to limit the need for taxpayer-funded bailouts and ensure that losses were borne by shareholders and creditors rather than taxpayers, while also aiming to protect jobs and minimize the impact on workers.

Indeed, the European institutions involved in the process ensured that information remained confidential throughout the resolution process, delaying its disclosure only until after the resolution decision, considering the inherent systemic risk. Despite being in line with what is envisaged in the directive to prevent systemic risk, the perceived lack of transparency in the process was one of the issues raised in the post-resolution period by shareholders.

However, we believe that the statements made on May 23, 2017, by the Chair of the SRB, Elke König, on Bloomberg TV, and also the Reuters article dated May 31, 2017, which stated that the Chair of the SRB warned that Banco Popular could be closed if it did not find a buyer, contributed to the run on withdrawals and violated what is provided for in the BRRD when it stated that merely disclosing that the resolution authority is monitoring a specific institution is sufficient to have negative effects on that institution.

5.3. Analyzing the Effectiveness of Valuations and Implications for Shareholders Throughout the Process

According to Article 34 of the BRRD, authorities must ensure that resolution measures are governed by the following principles: shareholders should be the first to bear losses, followed by creditors and in accordance with the priority ranking of claims prescribed in normal insolvency proceedings. Additionally, the losses borne by both should not exceed those they would have incurred if the institution had been liquidated under normal insolvency proceedings.

To ensure the protection of shareholders and creditors, both should be entitled to compensation for their claims if it is estimated that they would have incurred a lower loss had the institution been liquidated under a normal insolvency process.

Before any resolution measure is defined, as stipulated in Article 36 of the BRRD, a preliminary, fair, and realistic valuation of the institution's assets and liabilities must be conducted by an independent entity.

According to Article 74 of the BRRD, following the implementation of resolution measures, a new valuation should be carried out as soon as possible, now definitive, and also by an independent entity, to determine whether shareholders would have received more favorable treatment if the institution had entered into a normal insolvency process.

In the case of Banco Popular, three valuations were conducted.

Firstly, the SRB conducted a provisional valuation of Banco Popular on June 5, 2017, called Valuation 1, to assess its solvency and determine if conditions warranted initiating a resolution process. The valuation, based on a comparison of assets and liabilities, concluded that Banco Popular was solvent as of the valuation date with assets valued at 8.4 billion euros, and for this reason, it did not meet the conditions to be considered FOLTF. However, this assessment became outdated on June 6, 2017, when the ECB conducted its own analysis, considering events occurring after March 31, 2017, which led the determination that Banco Popular was in a situation or at risk of insolvency.

Secondly, according to Article 36 of the BRRD, a provisional valuation, called Valuation 2, dated June 6, 2017, was conducted by Deloitte, acting as an independent expert. The objective of this valuation was mainly to assess the bank's assets and liabilities. The valuation, requested prior to the resolution scheme decision in May 2017, utilized data mainly as of March 31, 2017, on a consolidated basis. The preliminary economic valuation indicated a negative value for the bank, estimating it to be EUR -8.2 billion in a stressed scenario and EUR -2 billion in a base scenario, but +1.3 billion in a best-case scenario.

After the completion of Valuation 2, the SRB issued Decision SRB/EES/2017/08 (Single Resolution Board, 2017b), concerning the adoption of the resolution scheme for Banco Popular.

Thirdly, according to Article 74 of the BRRD, a definitive valuation, called Valuation 3, was conducted by Deloitte as an independent expert, which began in June 2017 and was finalized on June 14, 2018, with an addendum dated July 31, 2018, to assess whether shareholders and creditors would have fared better in a normal insolvency process.

Deloitte was once again the entity chosen to conduct Valuation 3, in accordance with Article 36, paragraph 10, which states that this valuation may be carried out by the same independent entity that performed Valuation 2. Valuation 3 concluded that the losses incurred in a normal insolvency proceeding would consistently surpass those recorded in the utilized resolution scheme. Furthermore, while the resolution scheme only affected shareholders and creditors directly associated with the bank, in a normal insolvency scenario, unsecured creditors would also suffer losses.

Subsequently, on March 17, 2020, the SRB published Final Decision SRB/EES/2020/52 (Single Resolution Board, 2020), determining that shareholders and creditors were not entitled to compensation, highlighting no expected recoveries in a normal insolvency proceeding, indicating that shareholders and creditors received no better treatment compared to the resolution process.

According to the General Court, and in response to the complaints that arose regarding the discrepancy between the conclusions of the first and second valuations, it agreed that the two valuations utilized different analysis dates, leading to necessarily different conclusions. This was because the second valuation considered information after March 31, 2017, including significant deposit withdrawals and the bank's inability to meet its debts, which led to insolvency. Additionally, it concurred that the objectives of the two valuations differed, with valuation 1 aiming to assess if the bank's assets exceeded liabilities, while valuation 2 focused on the economic value rather than the accounting value of Banco Popular. Regarding the method used in valuation 2, which included a simulation of a liquidation scenario rather than viewing the bank as a going concern, it was clarified that the first part of valuation 2 was used for the adoption of the resolution program, while a later valuation (valuation 3) replaced the second part.

Another issue related to the impact on shareholders was the fact that the sales process only included five institutions and the perceived lack of efforts to maximize the sale price. The General Court justified the limitation of the sales process to only five institutions, citing the risk of expanding it to a broader group of potential buyers, which could lead to increased uncertainty and loss of market confidence. It's noteworthy that Banco Popular's private sales process was open to all Spanish and international institutions, but interest was only shown by the five mentioned ones. The General Court concluded that there was

no unfair advantage given to Santander, as it was the only bank to formally propose purchasing Banco Popular. Regarding the claim of non-maximization of the sale price, the General Court determined that the FROB had set the minimum bid price at one euro, and since there was only one proposal, it cannot be considered as a lack of real competition in the bidding process.

According to the interviewee, valuation 2 was highly unviable and ineffective because Deloitte, as an independent expert, admitted in the document itself the lack of sufficient time, information, and documentation to support the valuation.

As for valuation 3, he argued it was scandalous for using a fictitious scenario by assuming that the bank would have lost its banking license, its customers, and would have enormous resolution and sales costs. However, Banco Popular never ceased operations, having been sold to Santander with its banking license, its customers, and functioning assets. Further, excluding provisions for the recognition of the lower value of assets the bank was profitable in 2016 and in the first quarter of 2017.

After analyzing the obtained information, we agree that the SRB complied with the provisions of the directive by conducting valuations as legally stipulated and ensuring that through the analysis of the independent entity, shareholders and creditors bore the losses, which were not greater than those they would have incurred in a normal insolvency process.

However, the Banco Popular case study showed that the valuations are not reliable, based on assumptions that depend on multiple factors, leading to significant discrepancies in the bank's valuation. Indeed, valuations with such intervals is highly questionable, as pointed out by interviewee.

Firstly, it is factual that valuation 1 presented conclusions contradictory to valuation 2, with the valuation 1 determining that the bank was solvent and the valuation 2 determining it was insolvent, although justified by the fact that they were based on different valuation criteria.

Secondly, the SRB considered valuation 2 as a valid basis for deciding the resolution measures for Banco Popular, even though it included Deloitte's caveat that they had 12 days to prepare it, when it would normally take 6 weeks, and that it should be considered uncertain and provisional.

It should be noted that, on June 7, 2017, in a presentation to analysts, Santander shared partial information about its valuation of Banco Popular after acquiring it. This valuation differed from the SRB resolution decision and the Deloitte valuation reports, as Santander revealed that it decided to create provisions totaling EUR 7.9 billion, with EUR 7.2 billion allocated specifically for its portfolio of real estate assets and loans. Santander claimed that this resulted in a 'provision and capital deficit' of EUR 9.1 billion, arguing that these additional provisions left Banco Popular's real estate assets "well provisioned" (Banco Santander, 2017a, 2017b; Cabral, 2024).

Thirdly, regarding Valuation 3, Spanish legislation stipulates that the determination of the difference in treatment should be based on a liquidation scenario, which was used by Deloitte. In fact, given Banco Popular's inability to meet its obligations on the due date, and in light of Law 22/2003 (General Insolvency Law), the initiation of insolvency proceedings would have led to its liquidation, involving an accelerated realization of assets, without a minimum price, and the payment of the net proceeds to the creditors. Nevertheless, we reiterate that the possibility of using different scenarios makes the conclusions fluctuate, rendering the conclusions of the said valuation questionable.

Further, it is our understanding that Banco Popular's shareholders may have been disadvantaged and Santander benefited from the fact that the sale of Banco Popular was concluded for the value of one euro. In practice, this was justified by the minimum price set by the FROB for proposal submissions, but we believe that, considering it was an absolutely limited sale process with only one bidder, Santander may have capitalized on the situation in an urgent sale scenario and, as mentioned, conducted a valuation of Banco Popular much higher than the acquisition price.

Finally, we emphasize the destruction of value incurred by Banco Popular stakeholders that occurred as a result of the resolution procedure: EUR 11.4 billion from an accounting perspective; EUR 8.4 billion according to valuation 1 of the SRB; EUR 1.3 billion in the best-case sale of business scenario, according to valuation 2 by Deloitte. In addition, there are unaccounted losses incurred by other stakeholders such as Banco Popular staff, managers, depositors and creditors. Plus, the Spanish Treasury likely supported additional resolution costs in the form of tax credits to the acquirer, Santander, as well as other losses in tax revenues.

6. CRITICAL LESSONS FROM THE BANCO POPULAR RESOLUTION EXPERIENCE

Considering the succession of events leading up to the resolution decision of Banco Popular, from our perspective, the ECB, as the entity responsible for ensuring banking supervision, demonstrated a certain inefficiency in accurately characterizing the magnitude of the problems at Banco Popular, which were continuously deteriorating, ultimately leading to its downfall.

Although the ECB implemented corrective measures, such as capital increases and additional provisions, perhaps if the time frame for their execution had been extended, it could have prevented the successive declines in the value of the bank's shares, and Banco Popular might have continued to operate without the need for resolution. Additionally, the use of more rigorous stress tests by the ECB and EBA could have anticipated and managed the situation sooner.

Thus, the question arises whether the bank would be able to turn-around if given more time and monitored with a more assertive approach, i.e., if the crisis could have been resolved through greater regulatory forbearance.

Regarding the performance of the SRM, under the responsibility of the SRB, we believe that, overall, the resolution process was effective, particularly in its compliance with the principles and alignment with the procedures determined by the BRRD. However, we consider that some errors were made when the process is analyzed in detail.

The 24-hour period stipulated for the resolution scheme to enter into force, although intended to prevent financial instability, resulted in Banco Popular being sold for just one euro in a *de facto* fire-sale scenario, despite widely varying valuations of the bank and despite the fact that, excluding provisions, the bank was operating profitably. We believe that an additional mechanism could be implemented to extend the time frame for the sale process, thereby reducing value destruction and losses to stakeholders, and avoiding potential bias towards the acquiring bank. Moreover, we consider that the valuations are unreliable, since they are based in different scenarios and depend on many factors which lead to discrepancies in the bank's assessment. We believe that the methodological approach should be revised to minimize fluctuations in the analysis.

Thus, there may exist grounds for improvements to the current resolution process to make it more efficient.

7. CONCLUSION

This study aimed to analyse whether the procedures outlined in the BRRD were effectively followed in the resolution of Banco Popular, examining how and why these procedures were implemented as specified by the starting question.

From the conducted study, we can conclude that the resolution process overseen by the SRB was generally effective, adhering to the BRRD principles and procedures, but we also highlight some weaknesses during the process.

On the one hand, the SSM did not adequately evaluated the seriousness of Banco Popular's problems between November 2014 and February 2017. Although corrective actions were taken, extending the time frame for these measures could potentially have prevented the bank's collapse. Additionally, more rigorous stress tests accompanied by more significant capital increases might have anticipated and mitigated the crisis.

On the other hand, concerning the SRM's effectiveness, we can conclude that the swift resolution process caused substantial loss of value and stakeholder losses, with Santander obtaining significant gains from the acquisition of Banco Popular. This issue could be addressed through a new mechanism to extend the time frame. Additionally, we found the valuation methods used to be unreliable, resulting in inconsistencies in the bank's evaluation and highlighting the need for improvement.

These conclusions should be interpreted with some caveats. As a single case study, it provided detailed insights into the resolution of Banco Popular but should be complemented by broader methodologies or comparative analyses to enhance the robustness and applicability of findings. Additionally, due to the sensitive nature of Banco Popular's resolution and ongoing legal scrutiny, this study could only include a single interview, offering only one perspective on the merit of the resolution procedure.

For future research, we propose a deeper examination into the valuation approaches used in the resolution of Banco Popular, aiming to identify improvements or alternative methods. Furthermore, we recommend an investigation into the long-term performance and integration challenges of Banco Popular's acquirer (Santander), assessing how well the acquisition strategy aligned with initial expectations.

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APPENDICES

APPENDIX A - PARTICIPANTS IN THE RESOLUTION PROCESS OF BANCO POPULAR
CONTACTED FOR INTERVIEW PURPOSES AND INTERVIEW GUIDES

Interview guide	Participants in the resolution process	Position	Response received regarding the request to participate in an interview
1	Fundación Tatiana Pérez de Guzmán el Bueno	Claimant shareholder who initiated legal proceedings after resolution	Unanswered interview invitation
	Stiftung für Forschung und Lehre (SFL)	Claimant shareholder who initiated legal proceedings after resolution	Unanswered interview invitation
	RAMÓN C. PELAYO ABOGADOS	Law firm which represented important shareholders of Banco Popular	Interview conducted with the managing partner of the law firm, Mr. Ramón C. Pelayo, on May 7, 2024
	Mr. Pedro Larena	Former CEO of Banco Popular	Unanswered interview invitation
	Mr. Angel Ron	Former Chairman of Banco Popular	Although interest in participating was expressed in writing, no response was sent to the questions outlined in the interview script.
	Mr. Vítor Constâncio	Former Vice-President of the ECB (2010-2018)	Unanswered interview invitation
Interview guide	Participants in the resolution process	Response received regarding the request to participate in an interview	
2	FROB	Received response indicating impossibility to comment on matters under judicial review, referring to the public appearance made by the president of the FROB at the time, Mr. Jaime Ponce, in the Congress of Deputies, where information on the topic can be found. (FROB, 2017)	
	Bank of Spain	Received response stating it is not possible to accept the invitation, as matters related to the supervision of specific entities are subject to confidentiality.	
	Single Resolution Board	Received response informing that there are ongoing legal proceedings regarding the matter, and therefore, any public information available about the Banco Popular resolution can be found on their website.	
	European Central Bank	Received response indicating a lack of availability in the schedule.	
		Received response indicating that participation in the interview is not possible due to the sensitivity of the matter and its sub judice status.	
		It was clarified that non-confidential versions of the relevant documents can be consulted, such as the resolution decision, the resolution scheme and the valuations in SRB website.	
		It was also mentioned that responses to the questions can be found in the various judgments of the European Courts in the Banco Popular case, which are public in CURIA website.	
	European Commission		
	Banco Santander	Received response citing unavailability.	
	Deloitte	Received response informing that they cannot discuss their professional activities due to contractual clauses with their clients and Deloitte's internal policy.	
	BBVA	Received response citing unavailability.	
	Deutsche Bank	Unanswered interview invitation	

The interview guides provided to participants when contacted by e-mail can be accessed through the following links:

[Interview guide 1 - English Version](#)

[Interview guide 2 - English Version](#)

APPENDIX B - INTERVIEW TRANSCRIPT (INTERVIEWEE MR. RAMÓN C. PELAYO) - ENGLISH VERSION

The full transcription of the interview with Mr. Ramón C. Pelayo, conducted on May 7th via MS Teams, can be accessed through the following link: [Full Interview Transcription](#). This document provides additional insights and details referenced in section 5 of this dissertation.

APPENDIX C - BANCO POPULAR: TIMELINE OF EVENTS LEADING TO RESOLUTION PROCESS

Date	Event
September 2012	In September 2012, as part of Spain's financial system restructuring, independent experts for the ECB and IMF found that Banco Popular had a EUR 3.2 billion capital deficit in the worst-case scenario. This led to a capital increase in November 2012 of EUR 2,5 billion in order to ensure compliance with regulatory requirements.
December 2012	Banco Popular reported a net loss of EUR 2.46 billion for 2012, exacerbated by the ongoing rise in non-performing loans, which reached 8.98% in the last quarter of 2012 and then surged to 14.5% by July 2013.
26.05.2016	Under pressure from the ECB to reduce its bad debts and increase provisions for non-performing loan ratios, the bank encountered the need for another capital increase of EUR 2.5 billion.
29.07.2016	Publication of Stress Test results by EBA in which the CET1 ratio would reach 13.45% in 2016 in the baseline scenario, dropping to 7.01% in 2018 in the adverse scenario.
05.12.2016	Resolution Plan approved by the SRB: “a stabilization phase, in which the bail-in tool would be applied at the level of the institution; and, a restructuring phase, in which the management of the entity or group in resolution would submit a business reorganization plan within one month after the application of the bail-in tool” (SRB, 2016).
03.02.2017	Banco Popular announces that 2016 ended with losses of EUR 3.5 billion, after provisions of EUR 5.7 billion, predominantly related to impairments on its real estate portfolio (made public in February 2017).
10.02.2017	DBRS Morningstar downgraded Banco Popular's rating due to its weakened situation.
20.02.2017	Mr. Emilio Saracho replaced Mr. Angel Ron and became the new Chairman of Banco Popular.
03.04.2017	Resignation of CEO Pedro Larena following the publication of an audit revealing that the bank had under-provisioned of bad loans portfolio for EUR 600 million and had also revealed unreported loans to clients to buy shares in the 2016 capital increase.
06.04.2017	DBRS Morningstar has once again downgraded Banco Popular's credit rating.
07.04.2017	Moody's and Standard & Poor's downgraded Banco Popular's credit rating.
April 2017	Banco Popular initiated a sales process to a competitor with a first deadline of June 10, 2017, later delayed to the end of June.
05.05.2017	Banco Popular released its financial report for the first quarter of 2017, with new provisions of EUR 500 million and new losses of EUR 137 million (worse than expected).
12.05.2017	Banco Popular falls below the minimum 80% of Liquidity Coverage Requirement.
16.05.2017	Following the sales process initiated in April, Banco Popular announces that multiple potential buyers have reached out to them. Santander formally informed via letter that it is not in a position to present a final proposal.
23.05.2017	The chair of the SRB was interviewed on Bloomberg TV and mentioned that Banco Popular was one of the cases they were monitoring, thus exacerbating the situation.
31.05.2017	A Reuters Article revealed that the chair of the SRB warned EU officials that Banco Popular could be closed if a buyer was not found (although on the same day it was refuted by the SRB).
05.06.2017	Banco Popular found itself in need of requesting EUR 3.6 billion of Emergency Liquidity Assistance.
06.06.2017	Moody's and DBRS downgraded Banco Popular's credit rating once again.
06.06.2017	The ECB determined that Banco Popular "was failing or likely to fail" (FOLTF).

Source: Own creation based on the literature reviewed in Section 4.1.2.

APPENDIX D - RAISED CLAIMS VS. POSITIONS OF EUROPEAN INSTITUTIONS ON THE SINGLE
RESOLUTION MECHANISM APPLICATION

Raised Claims	Position of the European Institutions
Lack of transparency throughout the process	<input type="checkbox"/> The sales process was transparent, albeit limited and delayed, as any public disclosure of the sale of the bank could have adverse effects on financial stability.
Limitation of access to information by shareholders	<input type="checkbox"/> Given the short deadlines provided in Article 18 of the SRM Regulation, and to prevent financial stability from being threatened, the resolution measure had to be adopted swiftly. This prevented the risk of contagion and ensured the stability of the financial system. <input type="checkbox"/> If a prior consultation with all depositors and shareholders had been conducted before the adoption of the resolution mechanism, it would have delayed the process and undermined its effectiveness. <input type="checkbox"/> Informing shareholders and depositors of the Bank about details of the resolution process would inevitably lead to the selling of securities and the withdrawal of deposits, compromising the defined objectives.
Non-communication of valuation 2 during the process	<input type="checkbox"/> In accordance to Article 90, paragraph 4, of the SRM Regulation, the right of access was limited to the entity in question, which in this case was Banco Popular, and not to its creditors or shareholders. It was also mentioned that certain data could be protected if deemed confidential.
Early intervention and restructuring measures could have been adopted	<input type="checkbox"/> As provided for in Article 18, paragraph 1, subparagraph a, and paragraph 4, subparagraph c, of the SRM Regulation, the ECB determined that Banco Popular was in a "situation or risk of insolvency", the reasons for which had been enumerated in the ECB's valuation and mirrored in Article 2 of the resolution scheme, indicating that Banco Popular would not be able, in the short term, to pay its debts and fulfill its obligations. <input type="checkbox"/> There were no visible early intervention or supervisory measures that would ensure the immediate restoration of the bank's liquidity.
Compliance with with Article 18, paragraph 1 of the SRM Regulation, alleging that the requirements for adopting a resolution process were not met:	<input type="checkbox"/> According to Article 18, nr.1 of the SRM Regulation, the SRB adopts a resolution program if the following conditions are met: "a) The entity is in a situation or at risk of insolvency; b) Taking into account the deadlines and other relevant circumstances, there is no reasonable prospect that an alternative action by the private sector, including measures taken by an institutional protection scheme (IPS), or supervisory action, including early intervention measures or the reduction or conversion of relevant capital instruments, under Article 21, adopted in relation to the entity, would prevent its insolvency within a reasonable timeframe; c) A resolution measure is necessary to protect the public interest in accordance with paragraph 5."
a) The program would not apply to Banco Popular because it was a liquidity problem rather than solvency	<input type="checkbox"/> Regarding subparagraph a: 1. not only did the ECB conduct an analysis on June 6, determining that there were objective reasons to classify Banco Popular as being in a situation or at risk of insolvency in the near future, but also the Board of Directors itself had communicated to the ECB on the same day that Banco Popular was at risk of insolvency. 2. concerning the claim that Banco Popular only had liquidity problems and not solvency issues, it was highlighted the losses of EUR 3.5 billion and the need for exceptional provisions of EUR 5.7 billion, as stated in the 2016 Annual Report; the financial report for the first quarter with results worse than expected; the appointment of a new chairman; the downgrades in ratings in February, April, and June; and the media reports that contributed to the deposit run. 3. Banco Popular failed to meet the liquidity coverage requirement, falling below the 80% threshold on May 12, 2017, a situation that, according to EBA guidelines, determines that an institution should be considered to be in a situation or at risk of insolvency.
b) Insolvency could have been avoided through emergency liquidity injection; another private measure could have allowed to solve Banco Popular's problems; the ECB could have replaced the members of Banco Popular's management bodies and thus regained market confidence	<input type="checkbox"/> Regarding subparagraph b: 1. the ECB determined that, although an injection was approved on June 5, 2017, and partially released on June 6, 2017, it would not be sufficient for Banco Popular to meet its commitments until June 7, 2017, so it would not be an effective alternative to resolution. Furthermore, although the claimants argue that if the full liquidity injection had been granted, it would have allowed time for other measures such as asset sales, the truth is that this sales process would take several weeks, time that Banco Popular no longer had considering the continuous withdrawal of deposits and lack of market confidence in the institution. 2. about the issue raised that another private measure could have allowed to solve Banco Popular's problems, namely the interest of Barclays Bank and Deutsche Bank in securing a capital increase of EUR 4 million, so the resolution program could have been postponed to the following week and in the meantime the SRB could have released a loan through the SRF, it was mentioned that the interest shown by the two banks was communicated by letter on June 3 and 5, in which there was no formal commitment, but mere discussions at an early stage. Furthermore, resorting to the SRF can only be considered within the scope of an adopted resolution measure and not an alternative to that measure. 3. the hypothesis that the ECB replaced the members of Banco Popular's management bodies and thus regained market confidence was also not an accepted argument, as it would not provide the liquidity that Banco Popular needed and would hardly stop the deposit outflow the Bank was experiencing.
c) There could have been other measures that would have allowed to solve Banco Popular's liquidity crisis	<input type="checkbox"/> Regarding subparagraph c, it was determined that the sale of the business tool would be necessary to fulfill the said subparagraph, arguing that in a normal insolvency process, it would not have been possible to achieve this objective in the same way. This is because Banco Popular, given its size and importance, as well as the nature of its commercial banking activity, whose business model was similar to that of other Spanish banks, could have led to the indirect contagion of these banks and caused widespread adverse effects on financial stability in Spain.

Discrepancy of conclusions between valuations 1 and 2	<p>□ Valuation 1 became obsolete on June 6, 2017, after the valuation conducted by the ECB on that date, which determined that the Banco Popular would be in a situation or at risk of insolvency.</p> <p>□ Valuation 1 referred to the data of March 31, 2017, a time when Banco Popular was solvent. However, the ECB, in its valuation, considered events that occurred after that date, including significant withdrawals of deposits in the months of April, May, and June, and the fact that the Bank no longer had liquidity, being unable to pay its debts on the due dates.</p> <p>□ The different conclusions between evaluations 1 and 2 were also justified by the fact that they had different objectives. The first aimed to determine if the total value of assets exceeded that of its liabilities, that is, if it was solvent on the balance sheet, while the second was based on the economic value rather than the accounting value of Banco Popular.</p>
The method used in valuation 2, considering that the market value analysis should have been viewed as a going concern rather than a liquidation scenario	<p>□ Valuation 2 had two parts: a first part with the provisional valuation of assets and liabilities to conclude the economic value of the Bank, and a second part with the simulation of a Banco Popular liquidation scenario to determine if, in the case of a normal insolvency process under Spanish law, shareholders and creditors would benefit.</p> <p>□ For the adoption of the resolution program, the information contained in the first part of valuation 2 was used. The second part of valuation 2 was replaced by valuation 3, conducted later and with a definitive character.</p> <p>□ The liquidation value was only used by Deloitte in the second part of valuation 2. In the first part, the Bank's going concern value was considered.</p>
Limitation of the sales process only to banks that had participated in the process	<p>□ Limiting the process to only five institutions was justified by the risk of expanding it to a broader circle of potential buyers, which could imply additional uncertainty and a loss of market confidence.</p> <p>□ The private sales process initiated by Banco Popular had been open to all Spanish and international institutions, and interest was only demonstrated by the aforementioned ones.</p>
Favoritism toward Banco Santander	<p>□ Among the initial five interested parties, only Santander and BBVA decided to participate in the sales process.</p> <p>□ Considering that on June 6, BBVA communicated its decision not to submit a proposal, there was no unfair advantage conferred on Santander since it was the only bank to submit a formal purchase proposal for the bank.</p>
Lack of efforts to maximize the sale price	<p>□ The FROB had set the price in the bids to be equal to or greater than one euro and considering that there was only one purchase proposal, the SRB could not be held responsible for the lack of real competition in the sales process through prices.</p> <p>□ The fact that 4 out of 5 participants withdrew and there was only one proposal for one euro were circumstances beyond the control of the SRB.</p>
Valuation 3: - The appealed decision did not determine whether the former shareholders of Banco Popular would have benefited from better treatment in a normal insolvency process since it was equated to a liquidation - According to Spanish law, a concordat is the priority outcome of the insolvency process	<p>□ According to the provisions of Law 22/2003 (General Insolvency Law), concordat and liquidation constitute two mutually exclusive solutions.</p> <p>□ The SRB stated that, according to valuation 3, in light of the circumstances of the case and particularly the inability of Banco Popular to pay its debts on the due date, the opening of a normal insolvency process would have led to a liquidation of Banco Popular, which would have entailed an accelerated realization of assets without a binding minimum price, and the payment of the net realization to creditors in accordance with the hierarchy established by Law 22/2003.</p> <p>□ In assessing the difference in treatment following a resolution decided by the FROB, Spanish law stipulates that the counterfactual scenario is a liquidation scenario of the entity, taking into account the provisions of Law 22/2003 regarding liquidation.</p> <p>□ Deloitte explained in the clarification document for valuation 3 the reasons why it was not possible, in the case of Banco Popular, to carry out a sale as a going concern or to organize a concordat: on the one hand, given the liquidity situation of Banco Popular at the time of resolution and the ECB's assessment of Banco Popular's situation or risk of insolvency, it could not continue to operate while negotiations were carried out, causing significant value destruction; on the other hand, the evaluator had considered that Banco Popular's banking license would have been revoked, as the conditions for its revocation provided for in Spanish law were met.</p>
The applicable national law authorized a "good bank/bad bank" strategy and it was considered the best strategy for applying the principle that no creditor would be worse off	<p>□ The creation of a "good bank" and a "bad bank" was not foreseen in Law 22/2003, and in any case, its execution would require time that was not available at that time.</p> <p>□ The SRB considers this argument irrelevant since the expert report presented by the claimants assumes an evaluation of Banco Popular as a going concern, based on the mistaken assumption that Banco Popular could continue its activities.</p>
Lack of objectivity and impartiality on the part of the evaluator when conducting valuation 3 and being influenced by the fact of having conducted valuation 2 (again using a liquidation scenario methodology)	<p>□ The assessment of the treatment that shareholders and affected creditors would have received if Banco Popular had been subject to a normal insolvency process could only be carried out under a liquidation scenario, and it was not possible to evaluate it as a going concern.</p> <p>□ Another evaluator appointed by the SRB to conduct valuation 3 could only have used the same method.</p>

Source: Own creation based on data from the Judgments of the General Court

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June 28, 2024

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