Clarification Document of valuation of difference in treatment
Banco Popular Español
18 December 2019
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1. Executive Summary

Resolution Action

On 7 June 2017, following the endorsement of the resolution scheme in respect of Banco Popular Español SA (“BPE”) by the European Commission, the Single Resolution Board (“the SRB”) notified its decision to the Spanish Fund for Orderly Bank Restructuring (“FROB”), which, on the same day, adopted the necessary measures to implement the Resolution Decision of BPE.

Following the implementation of the Resolution Decision, Deloitte (“we” or “Deloitte”) acting as independent valuer appointed by the SRB, commenced a Valuation of Difference in Treatment Process as referred to in Article 20(16) and (17) of Regulation (EU) No 806/2014 (“the SRMR”). Deloitte issued the Report on 12 June 2018 (“the Report”). The scope of the Report was to provide a valuation of the difference in treatment of shareholders and creditors in the resolution of BPE, as compared to a normal insolvency proceeding.

On 6 August 2018 SRB published its preliminary decision that it was not required to pay compensation to the Affected Shareholders and Creditors (“ASCs”) of BPE pursuant to Article 76.1.e) of Regulation (EU) No 806/2014. At the same time, a non-confidential version of the Report was published as an annex to the decision. Thereafter, the SRB commenced a Right to be Heard process for ASCs regarding the SRB’s preliminary decision and the underlying reasoning. Specifically, the process wants “to allow eligible registered parties, or their representative, to submit their written comments in respect of the preliminary decision not to grant them compensation and its underlying reasoning”.

The Right to be Heard

The role of Deloitte

The SRB has requested that Deloitte review and respond to the comments collected in the Right to be Heard process identified by the SRB in so far as they relate to the Report (“the Comments”). Deloitte has considered whether the Report remains valid in light of the Comments. Deloitte has developed this Clarification Document at the request of the SRB and in order to provide answers and clarifications to the Comments received from the SRB, regarding the Report. Deloitte will not advise SRB on the content of its decision under Article 76(1) (e) of Regulation (EU) No 806/2014. This Clarification Document is not a new valuation report. It does not consider new additional information apart from any that is contained within the Comments.

Methodology

In June 2019, the SRB provided Deloitte with a number of documents with the Comments. We understand this was a subset of comments received that the SRB determined pertained to the Report. The SRB provided the Comments on an anonymous basis, so Deloitte was not aware of the identity of the ASCs. The documents consist of the following:

- The excel file provided by the SRB included 1,095 comments.
- Seven word documents also included comments deemed by the SRB to be directly related to the Report.

A number of the Comments related to similar topics on the Report and we therefore grouped the Comments into topics and as necessary grouped remarks. Thereafter, the Comments were reviewed by the appropriate subject matter experts who worked on the Report. As an additional quality check, analysis and challenge was provided by Deloitte individuals not previously involved in the preparation of the Report.

Purpose of this document

The purpose of this Clarification Document is to review and respond to the Comments identified by the SRB in so far as they relate to the Report, considering whether the Report remains valid in light of the Comments.
This Clarification Document is addressed exclusively to the SRB however, it does not provide
the SRB with any type of recommendation as to the content of its decision under Article
76(1)(e) of Regulation (EU) No 806/2014.

The purpose of the Clarification Document is to consider all the Comments with respect to
the Report, and therefore this document should be read in conjunction with the Report. We
have not been required to answer individually all the Comments; however all of the
Comments provided have been considered in preparing this Clarification Document. This
Clarification Document does not consider new additional information apart from any that is
contained within the Comments.

Conclusions

The majority of the Comments revolved around the following topics: criteria behind the
methodologies used, requests for additional information, challenges regarding the
assumptions used, and the lack of additional and/or detailed explanations regarding our
sources of information and/or methodologies used.

After reviewing the Comments we consider, to the best of our judgement, that both the
strategy and various hypothetical liquidation scenarios detailed in the Report, as well as the
methodologies followed and analyses used in the Report, remain valid.

The conclusions in the present Clarification Document are divided up into 13 different sub-
sections, into which the Comments have been classified:

1. Specific Context of the Report
2. Macroeconomic Scenario
3. Liquidation Strategy
4. Loans and Receivables
5. Real Estate
6. Tax Assets
7. JVs and Subsidiaries
8. Intangible Assets
9. Fixed Income and Derivatives
10. Other Assets
11. Legal Contingencies
12. Liquidation Costs
13. Shareholders, Creditors and Deposit Guarantee Scheme Hierarchy

The Executive Summary enumerates the topics found in the Comments and provides a
summary of both the questions received and the answers provided, the details of which can
be found in section 5 of the Clarification Document.

1. Specific context of the Report

The Comments relating to the specific context of the Report covered the following topics:

- The methodology used being based on regulatory frameworks which had not
  been finally approved at the Valuation Date and/or the rationale for the use of
  hypothetical scenarios when preparing the Report.
- Whether we adopted a dynamic scenario for the valuation of BPE.
- The comparison of the balance sheet used in the Report to figures reported to
  Asociación Española de Banca
• A request for clarification of the source of the information, on the loan portfolio assets with a net book value of €4,000m, which were not included in the loans data tape.

• The exclusive development of a liquidation scenario among all the possible scenarios for a “normal” insolvency proceeding.

• The rationale around our assumption of the removal of BPE’s banking licence following the SSM’s FOLTF decision.

• The comparison between the hypothetical liquidation scenario developed for BPE to other (actual) bank insolvencies/failures.

Our answers regarding the context of the Report are summarised below:

• All the Comments regarding the regulatory framework adopted are fully explained in section 1.2 of the Report.

• Valuation of difference in treatment underpins the No Creditor Worse Off (“NCWO”) safeguard that no creditor or shareholder written down because of resolution actions should incur greater losses than they would have incurred if an institution had wound up under a normal insolvency proceeding. As such, and in line with the requirements of the SRMR, we use hypothetical scenarios to estimate recoveries for creditors and shareholders in a counterfactual (hypothetical) insolvency scenario, i.e. liquidation, as set out in the Report, which can be compared to the actual treatment in resolution.

• In the Comments we have been asked if a dynamic scenario was adopted in the Report and if not, whether this might not have been appropriate. The scenario being modelled is the hypothetical liquidation of BPE, which would see a cessation of operations and realisation of assets over the liquidation period. Based on our understanding of the Comment, we consider that we did adopt a dynamic scenario. We considered three scenarios: 18 months, 3-year and 7-year scenarios. Within each scenario we considered the optimal strategy and disposal period to maximise realisations for the different asset classes reflecting their underlying nature and liquidity. In performing our analysis we considered the macroeconomic forecasts for the Spanish economy as at the Valuation Date (i.e. the date of resolution) so as to evaluate how asset values and realisations would evolve over the liquidation period.

• The Report was created using the latest available financial information as at the date of resolution. Differences observed between the balance sheet used in the Report and figures reported to Asociación Española de Banca primarily reflect a restructuring of BPE’s Real Estate subsidiaries in the period between 31 May and 6 June 2017, converting more than €6.6bn from loans to equity.

• The detail of the €4,000m in loans missing in the loans data tape was obtained from other records and data tapes and we included them in the Report.

• When defining the insolvency counterfactual as required under the SRMR, alternative scenarios were assessed but only the liquidation scenario was deemed appropriate to meet the requirements for Valuation of Difference in Treatment, as explained in section 5.1 of this Clarification Document.

• Removal of BPE’s banking licence would be driven by BPE’s inability to pay funds to depositors following SSM’s Failing or Likely to Fail (“FOLTF”) decision.

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1 A dynamic scenario is understood as a method that sets different moments of realisation during the liquidation and subsequently establishes a value of the asset based, among others, on the realisation time.
or the judicial decision to open a liquidation phase² which we consider the directors would be forced to apply for. This would be consistent with the case of Banco de Madrid.

- As set out in the Report, the liquidation of a bank such as BPE would be unprecedented; we considered whether other previous insolvencies could provide useful insight in defining the liquidation scenario. The Banco de Madrid case provided evidence of the impact of an insolvency on the banking licence. Equally we looked to other situations as to the potential liquidation strategy; however it is also the case that insolvencies are governed by national law which differs by jurisdiction (there have also been significant changes in the Spanish Insolvency Act which affect the comparison to previous Spanish cases) and that the macroeconomic context may also differ. Moreover, the nature of an entity’s operations, business and assets will also be a relevant factor.

2. Macroeconomic scenario

A number of Comments were submitted on the validity of the macroeconomic forecasts used to develop the Report, including whether reference should have been made to alternative sources and later versions which showed higher rates of recovery in the Spanish economy.

Our answers regarding this sub-section are summarised below:

- The principal economic forecasts on which the Report was based on and from which our hypotheses and assumptions are derived, is the report on the Spanish economic forecasts published by the European Commission during spring of 2017³, this being the most recent in time prior to the date on which BPE was resolved and therefore the most relevant for the hypothetical insolvency scenario. We considered other economic forecasts during our valuation, from both public and private institutions, and decided to use the European Commission’s forecasts based on their timing and independence.

- Any differences between the forecast for the Spanish Economy produced by the European Commission and forecasts produced by other public institutions as at the Resolution Date were not considered significant to modify the result of the Report.

- In terms of later revisions to the forecasts, we note that we looked at the forecasts closest to the Resolution Date which is consistent with the requirement set out under the regulations for the Report⁴. Moreover, we note that the scenario being modelled, was the hypothetical insolvency of one of the largest banks in Spain at the time. This is likely to have had a significant negative impact on the Spanish economy and on subsequent forecasts.

3. Liquidation strategy

The Report explains the 3 proposed scenarios for the duration of the liquidation (section 2.2.2) and the liquidation strategy for the realisation of BPE’s assets (section 3.2).

The Comments relating to the liquidation strategy covered the following topics:

- The actions taken by the acquirer after the Resolution Date.

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² Article 8 of the Law 10/2014 on the management, supervision and solvency of credit entities
⁴ Articles 73 y 74 of the BRRD and the Article 20(17) of the SRMR, the Valuation Date is to be the date of resolution, also validated “ex post” (after the Resolution Date) by Commission Delegated Regulation 2018/344 of 14 November 2017
• The view that the established time periods were either too long or too short or the opinion that greater recoveries would have been achieved with a longer insolvency scenario.
• The legal basis for the time limitation established on the Liquidator’s remuneration.
• The disposal strategy assumed for the real estate subsidiaries, specifically the difference to that proposed for foreclosed assets held directly by BPE.
• Comparisons of the asset realisation strategy to that adopted in other failed bank cases.

Our answers regarding this sub-section are summarised below:

• International valuation standards require that we consider events as at the Valuation Date, and do not take into account events occurring after that date as they impact value. Specifically, Commission Delegated Regulation 2018/344 of 14 November 2017 established that our valuation should be based on information about facts and circumstances which existed and could reasonably have been known at the resolution decision date. Moreover, it is important to note that the hypothetical liquidation basis we are required to assume in the Report is entirely different to the going concern basis of the business under ownership of the acquirer, and there are a number of important differences that mean the valuation of assets are not directly comparable between the two scenarios such as the inability of the Liquidator to provide reps and warranties; decline in the value of the business while in liquidation; financing structures; quality of information available to a Liquidator; market conditions, etc..

• Following changes to the Spanish Insolvency Act, the effective legal maximum liquidation period is 18 months (as explained further below where we comment on the liquidator’s remuneration). As set out in the Report we considered two longer scenarios (3-year and 7-year) to reflect a more orderly process (these would enable BPE to naturally amortise a larger portion of its credit portfolio).

• In terms of a longer liquidation period than the 7-year scenario, inevitably this would lead to higher liquidation costs, higher management and maintenance costs and increased uncertainty (i.e. macroeconomic risk) for the Liquidator in terms of the levels of asset realisations. Against this background we considered that a Liquidator would be unwilling to speculate as to possible upsides in the future which are highly uncertain. Moreover, the Liquidator would face pressure from creditors wanting speedy repayment of amounts due to them – particularly in the context that they would not be compensated for the delay since under Spanish law, unsecured creditors do not receive interest on their claims.

• Some comments were raised in the context of the limitation established on the Liquidator’s remuneration. The Comments referenced the proposed time period for the Liquidator to be remunerated. In this respect we note that, following changes in the Spanish Insolvency Act, a Liquidator can only be remunerated for 12 months with a possible 6-month extension.

• In terms of Comments that the disposal strategy assumed for the real estate subsidiaries was different to that proposed for foreclosed assets held directly by BPE and that a longer workout would yield higher recoveries, we assumed going concern sales of the Real Estate subsidiaries within the first 18 months of the liquidation as the optimum realisation strategy. We considered alternative strategies, including (as suggested in the Comments) for BPE to retain the entities and work the assets out itself over a longer period or to phase the disposals over

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5 Article 153 Spanish Insolvency Act and Transitory Provision Third of Law 25/2015
a longer period; however, this would have been a potentially more capital intensive and complex process to manage – in particular considering BPE’s liquidation. Moreover, in the context of BPE’s failure and potential macro-economic impact on asset values such a strategy would expose the Liquidator to additional risk (including from an operational perspective) which, in our opinion, the Liquidator would be reluctant to accept.

- We considered whether other failed bank cases across Europe could provide insight into what a liquidation of BPE might look like. We note that insolvency law is set at national level and different legal frameworks, different macroeconomic contexts and different market dynamics are likely to apply. Moreover, the nature of the institutions in question may vary considerably, which will impact on the nature of the liquidation, including timeframe and realisation strategy. We comment below (under loans and receivables) on observations included in the Comments on the Northern Rock and Bradford & Bingley cases in the UK.

4. **Loans and receivables**

Specific Comments received included comments on the following methodologies and assumptions:

- The run off of the **performing loan portfolio**, specifically with regard to the receipt of interest on the book in the liquidation period.
- Suggestions that the **prepayment assumptions** for performing loans were overly aggressive and resulted in a material understatement in interest received on the book in the liquidation period.
- The **Application of IFRS 9 methodology** to estimate recoveries for the performing loan portfolio, including Comments that this was not an appropriate methodology for estimating liquidation cashflows.
- Requesting greater clarity on the **reclassification of certain loans as non-performing**.
- Our assumptions around the non-performing loan portfolio **disposal timeline** and Comments that a longer or hybrid strategy would yield higher recoveries.
- Our assumptions around the **discount rates** applied in calculating estimated realisations from the sales of i) the non-performing loan portfolio and ii) the remainder of the performing loan portfolio at the end of the run off period.
- Requesting clarification on the treatment of **intragroup/non-intragroup positions**.
- The relationship between the **accounting impairments** surrounding loans and receivables and the realisable value of BPE’s credit portfolio in the hypothetical liquidation scenario.

Our answers regarding loans and receivables Comments are summarised below:

- In terms of Comments requesting clarification of our assumptions for interest receivable on the loan book, we assumed that the **performing loan portfolio** will be run-off until the end of the liquidation period at which point any remaining portion would be sold. We considered 18 month, 3-year and 7-year scenarios and modelled interest on the book continuing to be received during these periods.
- In terms of corporates (including Small Medium Enterprises (“SMEs”)), as noted in the Report, in the event of a liquidation of BPE, entities with transactional banking facilities with BPE will be forced to switch these to another provider. In order to assess the level of corporate loan **prepayments**, we took into account the commercial appetite of third-party entities in relation to the customer (considering the risk profile, segment, accounting qualification, etc.). We also considered the customer’s appetite for change (for example, in relation to any...
potential differences in loan pricing between BPE and alternative providers), taking into account, as noted in the Report, that customers having transactional banking facilities with BPE will be forced to re-bank following the liquidation, and that alternative providers will use the opportunity to capture other banking business.

- We took a similar approach in defining the prepayment assumptions for mortgage customers. We considered the Loan to Value ("LTV") of the loans to exclude those with high LTV's which would be unattractive to an alternative lender. From a borrower’s perspective we took into account the following: (i) the interest rates agreed upon for each transaction to be prepaid (comparing them with market interest rates at the Valuation Date) and (ii) the costs of extinguishing the debt held with BPE and the costs of arranging the new transactions with the destination banks.

- In terms of Comments on the application of IFRS 9 methodologies, for the avoidance of doubt, as set out in the Report, we adopted a Discounted Cash Flow ("DCF") approach when preparing the valuation of the loans and receivables portfolio reflecting the contractual cash flows, including interest and amortisations, over the liquidation period. In the absence of historical default and recovery data and curves, a number of assumptions for rates of defaults and recovery had to be made, which we tested and confirmed to be reasonable and appropriate as set out in the Report.

- Regarding the amount reclassified, the total Non-Performing Loans ("NPL") exposure before the reclassification amounted to €19,055m and €20,200m after this reclassification. After the reclassification, the total Net Book Value ("NBV") of the NPLs, represents 25.3% of Gross Book Value ("GBV") with 87% corresponding to companies and 10% to exposure to mortgage loans. The remaining 3% is composed of consumer and other household loans, as well as general government loans.

- In terms of Comments on the disposal timeline for NPLs, we remain comfortable with the 18 month time horizon. The argument of BPE retaining and working out the NPLs for a longer timeframe (as suggested in the Comments) was considered when preparing the Report. However, it was considered that greater recoveries via this approach would be uncertain, whilst the costs of retaining the work-out team, as well as certain other factors like the reluctance of defaulted borrowers to enter into discussions with an insolvent bank were more certain. Moreover, a longer time frame also increases macro-economic risk; in particular there was an active market for NPL's in H2 2017 and we considered it unlikely that a Liquidator would want to speculate on favourable conditions continuing for a lengthy period of time. It was therefore concluded that a relatively short term sale was ultimately more beneficial and would not result in buyer capacity issues which would impact on the level of realisations achieved.

- Regarding comments on the discount rates applied to NPLs and in particular that these are higher than standard rates observed in the Spanish market, the levels used reflect the lower quality of the processes and information provided to potential buyers, as well as the lack of representations and warranties on a sale out of liquidation.

- When developing our assumptions for the discount rate to apply to a disposal of the rump Performing Loans ("PLs") we considered historical corporate and mortgage securitisations and the average level of yield demanded in the Spanish market in order to set a relevant benchmark.

- As set out in the Report intra-group positions can be with both credit institutions and non-credit institutions. Intragroup positions with credit institutions are
reflected within Loans and Receivables (Credit Institutions)\(^6\) and have an NBV of €4,081m. Intra-group positions with non-credit institutions are reflected within Loans and Advances to Customers\(^7\) and have an NBV of €2,345m.

- Regarding Comments on the level of impairments, the level of accounting impairments made by BPE and included in its financial statements reflect the losses that would result from defaults in a going concern scenario taking into account accepted accounting rules. Whereas, the valuation made and reflected in the Report considers cashflows across the entire lifespan of the individual loans and the additional impairment that would result from a liquidation scenario.

5. **Real estate**

Comments relating to real estate assets covered the following topics:

- Suitability of the Valuation approach – specifically the use of a “statistical” model, haircuts and the effects of using a massive portfolio approach as well as the suitability of the valuation model to estimate realisations in a liquidation scenario.
- Application of macroeconomic forecasts – specifically whether the Report captured the real estate market recovery.
- Disagreement with the assumed disposal period.
- The consideration of the impairment coverage ratio when valuing the real estate assets.

Our answers regarding the Real Estate portfolio are summarised below:

- In terms of Comments on the approach used for the Real Estate valuation, we applied a combination of a statistical approach with a representative asset-by-asset challenge. This incorporates a national database of values and takes into account the heterogeneity of the Spanish regions and specific local real estate conditions as well as the asset’s location, typology, status, and other macroeconomic inputs, such as Consumer Price Index (“CPI”), unemployment rate, disposal income, labour force, etc. This is consistent with the market practice for the valuation of banks’ real estate exposure approach and what a Liquidator would do in the circumstances. Moreover, the size of the portfolio (c512,000 properties) also needs to be considered.
- The employed model (Automatic Valuation Model) has been used in the valuation of a large volume of Spanish Real Estate assets owned by financial entities and Investment Funds, and validated by the representative asset-by-asset challenge previously mentioned.
- In terms of Comments on the application of Macroeconomic forecasts and to reflect real estate market recovery, given the age of some of the valuations, we indexed these to reflect the situation as at the Valuation Date. The Real Estate asset valuation thus included the market recovery registered from 2015 to Jun 2017. When assessing future prospects, consistent with the methodological requirements we took into account the economic forecasts as at Q2 2017\(^8\).
- In terms of comments on the assumed disposal period, as noted in the Report we considered three scenarios for the liquidation of BPE. For own use assets and...

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\(^6\) Page 37 of the Report
\(^7\) Table included in page 38 of the Report that is detailing the line “C. Loans and advances to customers” of page 37 of the Report
foreclosed assets held directly by BPE, realisations were phased over the relevant liquidation period. Based on this valuation exercise, the realisation value (value of an asset when sold) of this portfolio ranged from €2,252m (worst case) to €2,946m (best case) depending on the assumed scenario.

- **Real estate impairment coverages** for Real Estate assets were considered when we prepared the Report.

6. **Tax assets**

The Comments relating to tax assets covered the **scenario of the valuation** of the tax assets and comparison to the post resolution scenario.

Our summarised answer is stated below:

- The scenario modelled and the basis of our valuation was BPE’s liquidation which would include a cessation of operations as opposed to a “sale of business as a going concern” scenario which is fundamentally different.

7. **JVs and subsidiaries**

The Comments relating to Joint Ventures and subsidiaries covered the following topics:

- Our approach to determining the impact of BPE’s liquidation on its Investees and which entities would go into a liquidation proceeding, the completeness of our analysis, and potential capital gains from selling certain Investees.
- Some Comments noted that the “Preferred Securities” in Popular Capital should have received different treatment and been preferred creditors in the liquidation of BPE, as well as questioning if Popular Capital had been considered in the Report.
- How intragroup debt is placed in the hierarchical ranking
- Relative levels of recoveries for the 3 banking entities which would be forced into their own insolvency processes.
- Whether the potential costs of terminating JV agreements had been considered in the Report.
- The sources used for the calculation of the multipliers used in the market value approach.

Our answers regarding Comments on JVs and subsidiaries are summarised below:

- The Banco Popular Group at the Resolution Date, comprised 123 legal entities of which BPE, the parent company, had a direct stake in 79 and the balance were held indirectly. We analysed the impact of BPE’s liquidation on its respective Investees, based on their financial and operational linkages, taking into account subordination of amounts due from BPE under relevant insolvency law, liquidity requirements, etc.. The Report explains in detail which group companies we considered would, in the event of BPE’s liquidation, also enter into an insolvency proceeding or might alternatively continue to operate and be sold as going concern. All group entities were considered as part of our analysis.
- The Report includes recoveries above NBV for several investments (e.g. WiZink, Totalbank, Allianz Popular).
- We note that the Popular Capital SA legal entity was considered in our analysis. In terms of Comments around the treatment of the Preferred Securities, we note that according to article 48.1 a) of the Law 11/2015, the internal recapitalisation will be executed by amortising or reducing the amount of the shares, capital instruments or liabilities following the order stipulated in the aforementioned article, starting with the ordinary capital elements of Tier 1 in proportion to losses and as far as possible. In BPE’s case, the Preferred Securities issued by Popular Capital were recorded as Tier 1 capital instruments by BPE and as set out in
Popular Capital’s prospectus. Moreover, the prospectus sets out that the proceeds would be deposited on a permanent basis with the Bank or with another credit entity of the Group and will be available to absorb losses of the Group once shareholders’ equity has been reduced to zero. In the event that proceedings for the liquidation, dissolution or winding up of BPE are commenced or there is a reduction in the shareholder’s equity of BPE pursuant to Article 343 of the Spanish Corporations Law, the Issuer shall be liquidated by BPE and the holders of Preferred Securities at the time outstanding will be entitled to receive only the Liquidation Distribution in respect of each Preferred Security held by them. At the resolution date, Popular Capital had a balance sheet of €93m, of which €88.1m were loans to BPE, €1.7m were deposits in BPE and €3.3m were non protected DTAs. The total recoverability estimated for Popular Capital’s assets, based on the latest available financial information, was zero.

- We note that intragroup claims are subordinated under the Spanish Insolvency Act - there is a hierarchy within the subordinated class and intragroup claims are at the bottom of this, just one-step above equity. Therefore, if a group entity enters into an insolvency proceeding due to BPE’s liquidation, all of BPE’s rights against these (now) insolvent intra-group companies will be subordinated and its recovery value is likely to be significantly impaired.

- Regarding the relative recoveries within the 3 banking entities, we considered that Banca Privada, Banco Pastor and Banco Popular Portugal would all be forced to enter into their own insolvency proceedings, reflecting asset impairment or liquidity issues. Due to their high level of intragroup positions (on the asset side of the balance sheet), both Banco Pastor and Banca Privada would see their overall level of recoveries substantially reduced. In Banco Popular Portugal’s case, assets predominantly comprise amounts due from 3rd parties, and the recovery range is higher so that overall asset realisations are sufficient to repay part of their intragroup position due to BPE.

- In terms of the potential costs/ claims to BPE associated with terminating existing JV agreements, we note that in some cases JV partners would be able to claim against BPE; however we did not make any adjustment for this in the Report. As such, this represented a conservative assumption from a NCWO perspective. The impact of including these costs/ claims would be to lower recoveries/ increase ordinary creditor claims and would therefore not change the overall conclusion of the analysis.

- The sources used to calculate the multipliers were obtained from generally accepted information providers.

8. Intangible assets

The Comments relating to intangible assets covered the following topics: the assumptions used when preparing the Report and the recovery value of BPE’s intangible assets.

Our answers regarding intangible assets are summarised below:

- The principal assumption was the immediate liquidation of BPE and a cessation of operations, and not the continuity of the business.

- Reflecting the nature of these assets, none of which are readily realisable in their own right, we estimated the recovery value for BPE’s intangible assets to be nil or very low, in the scenario where BPE was not a going concern.

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9. **Fixed income and derivatives**

The Comments relating to fixed income assets and derivatives covered the following topics:

- The methodology applied in our analysis, including whether any downward **adjustments** had been made to fixed income assets within the loans and receivables portfolio.
- Comments around the methodologies applied to “**level 3 assets**”, including the suggestion that these would lead to an underestimation of realisations.
- Comments suggesting the undervaluation of BPE’s **derivatives**.

Our answers regarding fixed income and derivatives are summarised below:

- The principal adjustments between book value and the amount estimated to be realised in liquidation (using fair value as a proxy) arise as follows:
  - Recalculating the fair value amount at 6 June 2017 for assets which are otherwise held on the balance sheet at amortised cost, being the fixed income portfolio within Loans and receivables (€654m) and Held-to-maturity assets (€6,997m). These portfolios were entirely made up of corporate and sovereign bonds with observable market prices (Level 1). Further details regarding the realisation values of these items can be found in the “Equity and fixed income estimated asset realisation” table in section 4.6 of the Report. The realisations for Loans and Receivables – Fixed Income were included in the summary table in the Executive Summary (“Estimated assets realisation values in liquidation”) under Loans and Receivables.
  - Recalculating the fair value amount on **Level 3 assets** included within the Available for Sale portfolio. The methodologies used for the valuation of these assets, which did not have an observable market price followed market standard methodologies. An adjustment arose based on use of our modelling approach and inputs, which were different to those adopted by BPE. Total book value of level 3 assets was €331m.
- Regarding the Comments surrounding the valuation of BPE’s **derivatives**, the calculation methodology and assumptions, their compliance with the applicable technical valuation standards, and the results obtained are detailed in the Report in section 4.7 "Derivatives position".

10. **Other assets**

The Comments relating to Other Assets were in terms of the valuation approach used and a request for explanation of the **resulting values**.

Our answers regarding other assets are summarised below:

- The different nature and typology of the assets that fall within the so-called “other assets” portfolio, makes the adoption of a single **valuation approach** inappropriate.
- The **recovery amounts** for the Other Assets section was €166m. Additionally a further c€702m was set-off against net liabilities reducing creditors by the same amount.

11. **Legal contingencies**

The Comments relating to legal contingencies covered the following topics:

- Whether the “Sources of uncertainty” as set out in the Report and the noted **unavailability of certain information** surrounding contingent claims, affected our conclusions, the additional information considered (e.g. 2016 capital issuance) as well as the challenges to the legal contingencies costs for the **2012 capital issuance**.
A request for further **explanation** of the distinct categories of potential legal exposure and **litigation costs assumed for BPE** as well as comparison to the level of accounting **provisions made by BPE** in its financial statements.

The distinction in the hierarchy between the **different types of plaintiffs**.

Our answers regarding legal contingencies are summarised below:

- As set out in the Report, we did not consider that the **unavailability of more detailed information** on contingent claims would affect the overall result for ASCs, as referenced in section 4.9 of the Report. The contingencies not provided were valued with a value of zero by Deloitte, so having more information from BPE would have resulted in a value equal to or greater than zero, negatively impacting the ASCs.

- In terms of the **capital increase of 2012**, we noted in the Report that claims may arise, due to: (i) claims of the shareholders looking back to potential errors or omissions in the original capital raise prospectus as grounds for a claim which if successful, would allow the shareholder to recover damages against BPE, but as an ordinary creditor, rather than as a shareholder and (ii) the statute of limitations had not expired. We observed that while potentially less likely than in relation to the 2016 capital increases (hence our low scenario we assumed zero claims) the possibility of claims in relation to the 2012 increase could not be entirely ruled out. We included in the analysis the risk of Capital Increase claims in a liquidation scenario, based on our knowledge of the sector.

- Surrounding the Comments requesting further explanations for the five discrete categories of potential legal exposure, the Report contains an individual **explanation and valuation** in respect of all the different categories. These explanations can be found in section 4.9 of the Report.

- In terms of Comments relating to litigation costs, the scenario of the Report is the liquidation of BPE. When making a comparison to resolution any additional **litigation costs** arising in the liquidation, which would not arise in resolution, need to be included in the analysis. This is the basis upon which we prepared the Report.

- Regarding the consideration of **BPE’s accounting provisions**, and as set out in Section 4.9 Legal Contingencies, we challenged the assumptions made by BPE and recalculated the potential amount which could be claimed, taking into account that we were modelling a hypothetical liquidation scenario. We note that the provision levels of BPE will necessarily be different as BPE’s provision levels reflect a going concern scenario.

- Some Comments were raised around the distinction in the hierarchy between the **different types of plaintiffs**. When it comes to the claims arising from capital increase, to estimate the potential claims of shareholders, we considered the investor profile, the shareholding structure provided by BPE, the shares by the board of Directors, and the elapsed time. Hence, we have excluded from the perimeter the percentage of shares owned by BPE Directors and by shareholders holding more than 5% of BPE’s equity, mainly because we did not consider it a potential risk for the following reasons:
  - The Directors will be considered as persons specially related to the BPE under the article 93.2. 2º of the Spanish Insolvency Act.
  - Following the Bankia case precedent, those claims would not prosper.
12. **Liquidation costs**

The Comments relating to liquidation costs covered the following topics:

- A suggested **overestimation of the liquidation costs**
- A suggested **overestimation of lawyer and Liquidator’s remuneration**.
- The level of **operating expenses** in the liquidation scenario.

Our answers are summarised below:

- We considered the expenses that would likely arise in the hypothetical case that BPE would enter into an insolvency proceeding to be the following: Liquidators’ fees and costs, employee related costs, contract termination costs, and operating costs.

- The **lawyer's remuneration** was calculated using a scale from the guidelines approved by Lawyers’ Bar association. We also considered the **Liquidator’s remuneration**. Reflecting the size of BPE (its asset values) and the complexity of its business and group structure, we understand that the judge would reasonably approve a higher remuneration exceeding the limit set out in the Law (including the 50% increase on the original 12 months).

- **Operating costs** for the liquidation period were adjusted (significantly downwards) to reflect the fact that under the scenario this would no longer be a functioning bank (hence there would be no need for a branch network) – but reflecting also the cost of the redundancy exercise.

13. **Shareholders, creditors and Deposit Guarantee Scheme hierarchy**

The Comments relating to the shareholder, creditor and DGS hierarchy covered the following topics:

- A request for further clarity around the different levels of the hierarchy under Spanish insolvency law, specifically in terms of calculating the aggregate assets and aggregate liabilities.

- The creditor and DGS hierarchy: a specific comment that subordinated creditors would incur a greater loss compared to shareholders due to their loss of principal and accrued interest and the hierarchical difference between shareholders and subordinated bondholders.

Our answers regarding the shareholder, creditor and DGS hierarchy are summarised below:

- In terms of Comments around the different levels of the hierarchy (aggregate assets and liabilities), we note that the creditor position was detailed and explained in section 3.4 “Creditor Hierarchy” - Table Creditor Hierarchy”. The value of the assets was analysed in Section 4. Liquidation Valuation: Analysis of results, and the realisation of assets has been presented in Section 5. Estimated Assets realisation.

- It has been observed in certain Comments that subordinated bondholders’ losses are greater than those of shareholders, since in case of the former their losses will also include accrued coupons. Both the nominal and the coupon are subordinated credits.

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10 Recopilación de criterios del Colegio de Abogados de Madrid en la emisión de sus dictámenes sobre honorarios profesionales a requerimiento judicial (aprobados por la Junta Gobierno de 4 de julio de 2013) y Arancel de Derechos de Procuradores de los Tribunales (https://www.cgpe.es/arancel/)
Regarding **hierarchical difference**, we confirm that shareholders are not ranked ahead of subordinated bondholders.

Finally, we note that this Clarification Document, just like the Report itself, does not provide an exhaustive list of possible scenarios regarding the liquidation of BPE. We consider the scenarios and assumptions developed in the Report to be appropriate and valid to the best of our judgement.
2. Resolution action and appointment of Deloitte as an Independent Valuer

Valuation of difference in treatment

Following the implementation of the Resolution Decision, Deloitte performed a valuation of difference in treatment as referred to in Article 20(16) and (17) of Regulation (EU) No 806/2014. The SRB published a non-confidential version of the Report on 6 August 2018.

The Report was prepared for the purposes of Article 20 of the Single Resolution Mechanism Regulation (SRMR). That is, as specified under Article 1 of the Commission Delegated Regulation (EU) 2018/344 of 14 November 2017 (DR) in accordance with Article 20 (16) and (17) of Regulation (EU) Nº 806/2014 and Article 74 (2) BRRD, the scope of the Report is to provide a valuation of the difference between the treatment of shareholders and creditors in the resolution, as compared to a normal insolvency proceeding.

The Report was prepared based on unaudited financial information as of 6 June 2017 when available, or as of 31 May 2017 when the 6 June 2017 information was not available, as well as on financial and non-financial information obtained from public sources, including digital and written information media (such as Bloomberg, S&P Capital IQ, research reports). All the information provided to us through the Virtual Data Room facilitated by Banco Popular Español S.A. has also been taken into account when preparing the Report.
3. **Right to be Heard**

3.1. **Commencement of a Right to be Heard process for affected shareholders and creditors**

On 6th August 2018 SRB published its preliminary decision that it was not required to pay compensation to the Affected Shareholders and Creditors of BPE pursuant to Article 76.1.e) of Regulation (EU) No 806/2014. At the same time, a non-confidential version of the Report was published as an annex to the decision. Thereafter, the SRB commenced a Right to be Heard process for affected shareholders and creditors regarding the SRB’s preliminary decision and the underlying reasoning. Specifically, the process wants “to allow eligible registered parties, or their representative, to submit their written comments in respect of the preliminary decision not to grant them compensation and its underlying reasoning”.

3.2. **Purpose of this document**

As a consequence of the Right to be Heard, SRB received a number of Comments from affected shareholders and creditors. Deloitte has not had any direct interaction with the Affected Parties during this process. The purpose of this Clarification Document is to review and respond to the Comments on the Report. That means:

- Deloitte will not provide any advice to the SRB as to the content of its decision under Article 76(1)(e) of Regulation (EU) No 806/2014. This decision remains a matter for the SRB.

- This Clarification Document is exclusively addressed to our client, the SRB.

- This Clarification Document and the information contained herein, does not constitute, and cannot be understood or construed as, any recommendation or advice as to whether any kind of action or process should be initiated by any party.

- This Clarification Document is not a new valuation report. Deloitte has not analysed any new additional documentation other than the documents used for the purpose of issuing the Report and the Comments.

- This document should be read in conjunction with the Report. The limitations set out in the Report (see in particular the Important Notice – replicated in section 7 below) apply also to this document.
4. The role of Deloitte

4.1. Methodology: Work done with the Comments received

In June 2019, the SRB provided Deloitte with a number of documents with the Comments. We understand this was a subset of comments received that the SRB determined pertained to the Report. These documents consisted of an Excel file with 1,095 comments, as well as 7 Word documents: These documents consist of the following:

- The excel file provided by the SRB included 1,095 comments;
- Seven word documents also included comments deemed by the SRB to be directly related to the Report;
- The SRB provided the Comments on an anonymous basis, so Deloitte was not aware of the identity of the ASCs.

A number of the Comments related to similar topics on the Report and we therefore grouped the Comments into topics and as necessary grouped remarks. Thereafter, the Comments were reviewed by the appropriate subject matter experts. As an additional quality check, analysis and challenge was provided by Deloitte individuals not previously involved in the preparation of the Report.
5. Analysis of the Comments

The majority of the Comments revolved around the following topics: criteria behind the methodologies used, requests for additional information, challenges regarding the assumptions used, and requests for additional and/or more detailed explanations.

After reviewing the Comments, to the best of our judgement, both the strategy and various liquidation scenarios detailed in the Report continue to be valid. Following the assessment of the Comments, we remain of the view that the methodologies adopted and analyses applied in the Report remain valid.

Our detailed responses to the Comments are set out below and cover the following:

1. Specific Context of the Report
2. Macroeconomic Scenario
3. Liquidation Strategy
4. Loans and Receivables
5. Real Estate
6. Tax Assets
7. JVs and Subsidiaries
8. Intangible Assets
9. Fixed Income and Derivatives
10. Other Assets
11. Legal Contingencies
12. Liquidation Costs
13. Shareholders, Creditors and Deposit Guarantee Scheme Hierarchy

We also provided further clarifications on certain aspects, as request by the SRB.

5.1. Specific context of the Report

The results of our analysis, in terms of asset realisations, as set out in the Report are summarised below:

<table>
<thead>
<tr>
<th>Assets</th>
<th>NBV (30 June 2017)</th>
<th>18M Scenario</th>
<th>3Y Scenario</th>
<th>7Y Scenario</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Best Case</td>
<td>Worst Case</td>
<td>Best Case</td>
<td>Worst Case</td>
</tr>
<tr>
<td>Equity, fixed income and derivatives</td>
<td>21,543</td>
<td>20,410</td>
<td>20,392</td>
<td>20,410</td>
</tr>
<tr>
<td>Loans and receivables</td>
<td>83,330</td>
<td>66,521</td>
<td>63,430</td>
<td>68,499</td>
</tr>
<tr>
<td>Joint ventures, associates and subsidiaries</td>
<td>9,908</td>
<td>8,382</td>
<td>7,496</td>
<td>8,382</td>
</tr>
<tr>
<td>Real estate assets</td>
<td>3,728</td>
<td>2,514</td>
<td>2,252</td>
<td>2,832</td>
</tr>
<tr>
<td>Intangible assets</td>
<td>1,198</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Tax assets</td>
<td>5,992</td>
<td>2,334</td>
<td>2,334</td>
<td>2,334</td>
</tr>
<tr>
<td>Other assets</td>
<td>1,245</td>
<td>166</td>
<td>166</td>
<td>466</td>
</tr>
<tr>
<td>Total insolvency realisation</td>
<td>100,327</td>
<td>96,067</td>
<td>102,624</td>
<td>98,669</td>
</tr>
<tr>
<td>Liquidation costs</td>
<td>(990)</td>
<td>(889)</td>
<td>(1,078)</td>
<td>(1,077)</td>
</tr>
<tr>
<td>Total realisation for shareholders &amp; creditors</td>
<td>99,338</td>
<td>95,178</td>
<td>101,546</td>
<td>97,592</td>
</tr>
</tbody>
</table>

[1] Equity, fixed income and derivatives portfolio includes cash and cash with the Central Bank totaling €1,354m, and excludes fixed income from the loans and receivables portfolio of €1,490m.

Source: Banco Popular Individual Financial Statements, Deloitte analysis

The Comments relating to the specific context of the Report covered the following topics:
• The methodology used being based on regulatory frameworks which had not been finally approved at the Valuation Date and/or the rationale for the use of hypothetical scenarios when preparing the Report.

• Whether we adopted a dynamic scenario for the valuation of BPE.

• The comparison of the balance sheet used in the Report to figures reported to Asociación Española de Banca.

• A request for clarification of the source of the information on the loan portfolio assets with a net book value of €4,000m which were not included in the loans data tape.

• The exclusive development of a liquidation scenario among all the possible scenarios for a “normal” insolvency proceeding.

• The rationale around our assumption of the removal of BPE’s banking licence following the SSM’s FOLTF decision.

• The comparison between the hypothetical liquidation scenario developed for BPE to other (actual) bank insolvencies/failures.

5.1.1. Valuation Context, Methodology and Assumptions

Some comments were raised with regards to the regulatory frameworks that governed our valuation approach, and whether or not they were valid at the time of the resolution.

The legal and regulatory framework for the Valuation of Difference in Treatment are fully explained in section 1.2. of the Report. Specifically we have considered the expected cash flows arising from asset realisations and costs, on an undiscounted basis, during the liquidation period based on our envisaged liquidation scenario. We should point out that considering that repayment dates to creditors do not necessarily correspond to asset realisation dates, as the former depends on the Liquidator’s approval and experience shows that there could be material time lapse in between, moreover, recovery values for the different liquidation scenarios have not been discounted to consider the time value of money. Nonetheless, should recoveries amounts be discounted as of the date of resolution, this would result in lower amounts than the ones shown in the Report. As we noted in the Report, we considered the Liquidator’s approach to act diligently to obtain the best value when realising BPE’s assets. However, this approach has to take into account changes in the Spanish Insolvency Act, which accelerate the liquidation process to avoid an undue prolongation of the liquidation phase, and creditors wish to receive repayments of amounts due in a reasonable period of time. For further details, please see Appendix I of the Report.

In terms of Comments questioning the use of hypothetical scenarios, article 20(16)-(18) of SRMR and 74(2) of the BRRD requires a valuation of difference in treatment, with the aim to assess whether shareholders and creditors, affected by the resolution action in respect of BPE, would have received better treatment were BPE to have entered into an insolvency proceeding. Valuation of difference in treatment underpins the NCWO safeguard that no creditor or shareholder written down because of resolution should incur greater losses than they would have incurred if an institution had wound up under a normal insolvency proceeding. Therefore, the very nature of this Report is a hypothetical and prospective exercise to estimate the recovery value of BPE’s creditors, for which it is necessary to adopt a series of hypothetical scenarios.

Furthermore, we built these hypotheses and assumptions based on information provided by BPE, which was analysed and quality checked. Where information required for our work was not available, we used data from public and reliable sources, including digital and written information media.

We also built some hypotheses and assumptions from several trustworthy and public detailed analyses, samplings and benchmarking data. In those cases where two or more
hypotheses were plausible, we adopted a potentially optimistic approach in order to provide a more favourable view of recoveries to ASCs, on the basis this is more prudent for the SRB.

As we highlighted in the Report’s Important Notice (see Appendix), the content and conclusions in the Report are based on prospective scenarios. Some assumptions or projections could materialise differently and unanticipated events may occur during any insolvency proceeding. Therefore the actual outcome could have been different to the one concluded, and variations could be material and have a material impact on the content and conclusions stated herein. However, we consider the prospective scenarios and assumptions we developed in our analysis to be appropriate.

5.1.2. Valuation Approach

Some comments were raised regarding whether Deloitte adopted a [dynamic scenario](#). The scenario being modelled is the hypothetical liquidation of BPE, which would see a cessation of operations and realisation of assets over the liquidation period. We considered three scenarios: 18 months, 3-year and 7-year. Within each scenario we considered the optimal strategy and disposal period to maximise realisations for the different asset classes, according to their underlying nature and liquidity.

For example, the majority of the following assets, have been realised at the commencement of the liquidation period (taking into account their liquidity):

- cash, cash balances at the central bank and other demand deposit portfolios
- financial assets portfolios (i.e., held-for-trading, available-for-sale, loan & receivable- fixed income, held-to maturity, derivative-hedge accounting and fair value changes of portfolio hedge of interest risk)

The realisation strategy for each asset class is explained in section 3.2. of the Report.

Moreover, in performing our analysis we considered the macroeconomic forecasts for the Spanish economy as at the Valuation Date (i.e. the date of resolution) so as to evaluate how asset values and realisations would evolve over the liquidation period.

The asset realisation tables, reflected in section 5 of the Report, consolidate the cash flows resulting from BPE and their subsidiaries’ asset realisations to give an overall amount available for distribution to the creditors.

5.1.3. Comparison of balance sheet used in the Report to figures reported to Asociación Española de Banca

Some comments were raised about the value of the loans and receivables within BPE’s balance sheet as at 6 June, as set out in the Report, specifically in terms of comparison to figures reported to Asociación Española de Banca (“AEB”) as at 31 May 2017.

BPE reported to the AEB as at 31 May 2017 loan and receivable assets totalling €90.3bn. However, from 31 May to 6 June 2017, BPE restructured its Real Estate subsidiaries, converting more than €6.6bn from loans to equity. This conversion affected BPE’s financial statements, decreasing loan and receivables and increasing investments in subsidiaries, joint ventures and associates. This reduction (€6.6bn) explains more than 90% of the variation from €90.3bn to €83.3bn (€7.0bn) between the two dates.

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11 A dynamic scenario is understood as a method that sets different moments of realisation during the liquidation and subsequently establishes a value of the asset based, among others, on the realisation time.
5.1.4. Loans not on the loans data tape

Regarding the comments surrounding the loans that were not on the data tape, the €4,000m (NBV) in loans not reported on the data tape were as follows:

- €2,152m of exposure held with Group companies. The records that support this figure were requested, obtained and subsequently reconciled.
- €1,781m of exposure held with customers, which was not reported on the data tape provided ("loan tape") but is recorded in other records. These records were requested, obtained and subsequently reconciled.

Therefore details of these €4,000m asset balances were obtained and recoveries were included in the overall recoveries.

5.1.5. Alternative Scenarios / Approaches

We received Comments as to why we exclusively developed the **liquidation scenario** that was used in the Report among all the possible scenarios.

Some Comments suggested that Deloitte’s approach, in assuming that the normal insolvency proceeding would end in a liquidation (without it being possible to sign a creditors agreement or the maintenance of the company activity), is flawed.

Firstly we note that, Spanish Law 11/2015 which transposes the BRRD specifically states that Valuation of Difference in Treatment, should be performed assuming that the entity has entered into a liquidation proceeding\(^1\).

Moreover, in the case of BPE, it would not be possible to complete a sale of business as a going concern (by way of a pre-packaged insolvency process or otherwise) nor arrange a creditors’ composition for the following key reasons:

- Given the liquidity position of BPE on the Resolution Date, and the SSM’s FOLT, BPE could not continue to operate while negotiations were undertaken, leading to significant value destruction.
- The banking licence that is required to accept customer deposits, which are fundamental to the ongoing operation of BPE and its sale as a going concern, would be revoked.

**Banking licence removal**

The banking licence could be revoked under Spanish Law due to any of the below:

- Inability to pay funds to depositors or to offer guarantees of being able to fulfil its obligations to creditors
- A judicial decision to open a liquidation phase in an insolvency proceeding (Article 8 of Law 10/2014)\(^2\). In this regard we note that, even in the unlikely event of Banco de España not taking action to revoke the licence, the risk of a run on deposits created by the FOLT decision and (in this counterfactual scenario) the SRB’s decision not to apply its resolution powers, would force the directors to seek to file for liquidation which would then trigger revocation of the banking licence (as noted above).

Both conditions would be satisfied in the counterfactual scenario envisaged for the purposes of the Report. This would be consistent with the case of Banco de Madrid, S.A.U. (hereinafter “Banco Madrid”).

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\(^1\) Article 10.1 of RD 1012/2015  
\(^2\) Article 8 of Law 10/2014
Considering the above, liquidation under Spanish law is the only appropriate insolvency counterfactual for a Valuation of Difference in Treatment, even though alternative scenarios were considered when preparing the Report.

Some Comments referenced the possibility of creating a pre-packaged insolvency involving a good bank/bad bank strategy. The creation of a good bank/bad bank is not considered in the Spanish Insolvency Act and in any event would have required time to set up which was not available in the circumstances.

5.1.6. Comparison to previous insolvency cases

Some of the Comments submitted made comparison to insolvency cases in different jurisdictions, in large part in relation to the duration assumed for the liquidation of BPE (which were longer in the cases mentioned in the Comments).

As set out in the Report, we considered whether other European liquidation cases could provide insight into the hypothetical liquidation scenario.

Insolvency proceedings are exclusively governed by national laws. Moreover, the nature of the institutions in question (in terms of scale and the nature of their business) may vary greatly. Therefore, comparison to other insolvencies across Europe is only of limited value.

Further comment on the liquidation periods used in our analysis is provided at 5.3.

Regarding the UK cases of Northern Rock and Bradford & Bingley, these are commented on, at 5.3. below.

Regarding other liquidation cases in Spain, we have taken into account Banco Madrid’s insolvency proceeding to prepare the Report, but as we noted in the Report (page 21), Banco Madrid’s case took place before important legal changes in Spanish Insolvency Act. These changes would potentially have the effect of restricting the liquidation process to 18 months duration.

For further details regarding the Report specific context, please reference sections 1.1, 1.2., 1.3., 1.4., 1.5., 2.1., 2.2., 2.3., 3.2., and 4 of the Report.

5.2. Macroeconomic scenario

A number of Comments were submitted on the validity of the macroeconomic forecasts used in the Report, including whether reference should have been made to alternative sources and later versions which showed higher rates of recovery in the Spanish economy.

5.2.1. Choice of macroeconomic forecast

The Report was developed using the latest available financial information as at the Valuation Date. As explained in the Report, under the BRRD and Article 20(17) of the SRMR, the Valuation Date is mandated as the date of resolution.

The above was also validated “ex post” (after the Resolution Date) by Commission Delegated Regulation 2018/344 of 14 November 2017, which establishes that this valuation should be based on information about facts and circumstances which existed and could reasonably have been known at the resolution decision date which, had they been known by the valuer, would have affected the measurement of assets and liabilities of BPE at that date.

This applies to all information, including the work based on BPE’s balance sheet as at close of business on 6 June 2017.

Therefore, the principal economic forecasts on which the Report was based and from which our hypotheses and assumptions are derived, is the report on the Spanish economic
forecasts published by the European Commission during spring of 2017\textsuperscript{14}, this being the most recent in time prior to the date on which BPE was resolved and therefore the most relevant for the hypothetical insolvency scenario. We considered other economic forecasts during our valuation, from both public and private institutions, and decided to use the EC’s forecasts based on their timing and independence.

Moreover, with regards to the Comments surrounding our limited or dated use of information, we confirm that other public sources (e.g. Instituto Nacional de Estadística (“INE”) or Banco de España) were also taken into account for some economic hypotheses regarding collateral or foreclosed asset valuation.

Nevertheless, any difference between the forecast for the Spanish Economy produced by the European Commission and forecasts produced by other public and private institutions at the Resolution Date is not significant to modify the result of the Report.

In terms of later revisions to the forecasts, we note that we looked at the forecasts closest to the Resolution Date which is consistent with the requirement set out under the regulations for the Report. Moreover, we note that the hypothesis being modelled is one of the insolvency of what was one of the largest banks in Spain at the time. The consequences of such an event are likely to be broad and prolonged such that later forecasts would potentially have needed to be amended.

For further details regarding the macroeconomic context and the use of information available after the Resolution Date, please reference sections 1.3 and 2.4 of the Report.

5.3. Liquidation strategy

The "Liquidation Strategy" sub-section of this Clarification Document provides further explanation of the hypothetical liquidation strategy considered in the Report, by explaining the three proposed time scenarios, as well as the envisaged strategy for the realisation of BPE’s Real Estate assets.

The Comments relating to the liquidation strategy covered the following topics:

- Comparison of the results from our valuation to the results of realisation actions taken by the acquirer after the Resolution Date.

- The view that the established time scenarios for the liquidation as set out in the Report were either too long or too short including the opinion that greater recoveries would have been achieved with a longer insolvency scenario.

- The legal basis for the time limitation established on the Liquidator’s remuneration.

- Our assumptions around the strategy and timeline for disposal of the real estate subsidiaries including that these seemed inconsistent with those applied to foreclosed assets held directly by BPE and the opinion that greater recoveries would have been achieved with a longer term work out over the (full) liquidation period.

- Comparisons to other failed bank cases (notably Northern Rock and Bradford & Bingley in the UK) regarding the timescale for the realisation of loan portfolio assets, including the Comment that had a similar approach been applied to BPE this would have resulted in higher realisations.

5.3.1. Actions taken by the acquirer

International valuation standards require that we consider events as at the Valuation Date, and do not take into account events occurring after the date as they impact value. In fact, Commission Delegated Regulation 2018/344 of 14 November 2017 established that our valuation should be based on information about facts and circumstances which existed and could reasonably have been known at the resolution decision date. Moreover, it is important to note that the hypothetical liquidation basis we are required to assume in the Report is entirely different to the going concern basis of the business under ownership of the acquirer, and there are a number of important differences that mean the valuation of assets are not directly comparable between the two scenarios such as the inability of the Liquidator to provide reps and warranties; decline in the value of the business while in liquidation; financing structures; quality of information available to a Liquidator; market conditions, etc..

5.3.2. Time Scenarios

A number of Comments touched on the length of the proposed liquidation scenarios, suggesting that they may be either too long or too short.

As set out in section 2.2 of the Report, the position under Spanish Insolvency law, following the reforms of 2015, is that a period of 18 months would be the effective maximum for the liquidation of BPE.

The purpose of these changes was to avoid indefinite extensions of the liquidation proceedings, which had been a concern prior to the reforms. The Spanish Insolvency Act established undue prolongation of the liquidation phase as a reason to replace the Liquidator. This statement is particularly relevant when we are talking about a market which at the time of liquidation was wide and liquid.

In the circumstances, direct comparison cannot be made to liquidation processes commenced prior to these changes.

Nevertheless, given the complexity of BPE’s hypothetical insolvency proceeding, and that a very quick process would lead to market capacity issues, distressed prices and low realisation values, we also considered two longer liquidation time scenarios than the one legally established by the Spanish Insolvency Act of 18 months.

On the one hand, we proposed a 3-year scenario, from 6 June 2017 until 31 December 2020, which, in our view, would equate to the minimum period necessary to liquidate BPE’s assets, since one half of the credit portfolio will have matured by the end of this scenario.

On the other hand, we proposed a 7-year scenario, from 6 June 2017 until 31 December 2024, which would be the longest liquidation scenario chosen, as a sufficiently large portion (c.75% of the total) of BPE’s credit portfolio should naturally amortise by the end of this period.

We considered these additional scenarios would enable BPE’s assets to be liquidated more efficiently and with greater recovery rates than under the 18-month scenario, while respecting the principle of also returning value to creditors in a reasonable timeframe.

As noted, the impact of a liquidation of BPE on the Spanish economy is likely to be deep and broad. In terms of a longer liquidation period than the 7-year scenario, inevitably this would lead to higher liquidation costs, higher management and maintenance costs and increased uncertainty (i.e. macroeconomic risk) for the Liquidator in terms of the levels of

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15 Articles 73 y 74 of the BRRD and the Article 20(17) of the SRMR, the Valuation Date is to be the date of resolution, also validated “ex post” (after the Resolution Date) by Commission Delegated Regulation 2018/344 of 14 November 2017.
asset realisations. Against this background we considered that a Liquidator would be unwilling to speculate as to possible upsides in the future which are highly uncertain.

Moreover, in terms of a longer scenario, we considered that, the intentions of the Insolvency Act and pressure from creditors would not support an even longer scenario than the 7-year scenario included in the Report. In particular

- The Spanish Insolvency Act\textsuperscript{16}, determines the rules to liquidate the assets of the insolvent bank, with (on the one hand) the overall objective of obtaining the highest realisation value. As established by the Spanish Insolvency Act\textsuperscript{17} the Liquidator is required to act diligently to obtain the best value for the entity's asset realisation within the parameters allowed by the legal framework (including the time allowed for the liquidation); however, they are not required to speculate on uncertain outcomes.

- On the other hand, the Spanish Insolvency Act\textsuperscript{18} encourages the timely sale of the entity's assets under liquidation. These changes in the Spanish Insolvency Act were designed to speed up liquidation proceedings and avoid indefinite extensions, which had been a concern prior to the reforms. In this regard, we note that (following the reforms) the Spanish Insolvency Act established the right for creditors to apply to Court for the replacement of the Liquidator if there was “undue prolongation” of the liquidation phase. This statement is particularly relevant when we are talking about a market which at the commencement of liquidation was wide and liquid.

- Creditors would require their claims be repaid in a reasonable period, especially those occupying a higher ranking within the creditor hierarchy. This is particularly the case where given the provisions of Spanish Insolvency law interest on unsecured claims (i.e. that post liquidation interest is not payable) senior creditors (including the deposit guarantee scheme) are unlikely to be compensated for delays in repayment of amounts due and therefore push for a shorter liquidation period.

Finally, we refer back to 5.1.6 and below to 5.3.5, in terms of comparisons drawn in the Comments to bank failures in other countries.

\section*{5.3.3. Liquidators’ remuneration limitations}

Some comments were raised surrounding the \textit{limitation set out by law on the Liquidator's remuneration}, in particular the time period for which the Liquidator can be remunerated. In this respect we would clarify that, according to changes in the Spanish Insolvency Act\textsuperscript{19}, a Liquidator can only be remunerated for 12 months with a possible 6-month extension.

\section*{5.3.4. Real Estate subsidiaries liquidation strategy}

As set out in the Report we considered the impact of BPE’s liquidation on its subsidiaries taking into account operational and financial linkages. Based on our analysis, we considered that 38 of BPE’s subsidiaries, including Real Estate ones, could continue as going concern entities and be sold in 18 months.

It has been suggested in Comments that our proposed liquidation strategy for \textbf{Real Estate subsidiaries}, was inappropriate and inconsistent with information detailed elsewhere in the Report, including as regards own use properties/ foreclosed properties held directly by BPE,

\textsuperscript{16} Article 149 of the Spanish Insolvency Act
\textsuperscript{17} Article 149 in accordance with articles 35 and 43 of the Spanish Insolvency Act
\textsuperscript{18} Article 153 of the Spanish Insolvency Act and Transitory Provision Third of Law 25/2015
\textsuperscript{19} Article 153 of the Spanish Insolvency Act and Transitory Provision Third of Law 25/2015
namely that realisations would be maximised through an orderly disposal of assets across the entire liquidation period and that the 18-month period noted above was unnecessarily accelerated resulting in a significant understatement of recoveries.

In response to this, we note that when preparing the Report, we considered alternative strategies, including for BPE to retain the entities and work the assets out itself over a longer period or to phase the disposals over a longer period; however, this would have been a potentially more capital intensive and complex process to manage – in particular considering BPE’s liquidation. Specifically, pending asset disposals, the entities could require funding, moreover, in the context of BPE’s failure and potential macro-economic impact on asset values such a strategy would expose the Liquidator to additional risk (including from an operational perspective) which, in our opinion, the Liquidator would be reluctant to accept. Moreover, given the additional costs and risks we considered that a longer period of time for the sale of these entities would potentially negatively impact the realisable amount, given the potential impact of a liquidation process of the parent in the management of these entities. Furthermore, the non-sale of real estate subsidiaries until the end of the liquidation timeline would entail higher liquidation costs, as well as higher management and maintenance costs, and not necessarily higher recoveries.

When conducting our valuation of the Real Estate subsidiaries, we considered all Real Estate subsidiaries as ongoing companies and not simple property owners. This consideration allows them to be realised, once sold, in a quicker and more orderly way without distressed property prices nor saturating market capacity. Disregarding the aforementioned consideration runs a risk of lower realisations for the acquirer, and therefore lower recoveries for BPE.

As set out in the Report, adjusted book value was used to value the Real Estate subsidiaries. In the adjusted book value methodology, the Real Estate asset values correspond to a market value under normal realisation strategies without liquidation pressures.

In addition, it is important to highlight that although an 18 month period was considered, no forced-sale adjustment was considered in the sale of these Investees.

Details of our valuation methodology for real estate assets, including those held by Real Estate Owned (“REO”) subsidiaries are set out in section 4.2 of the Report and below at section 5.5. 

5.3.5. Comparisons to other failed bank cases

We note that insolvency law is set at national level and different legal frameworks, different macroeconomic contexts and different market dynamics are likely to apply. Moreover, the nature of the institutions in question may vary considerably, which will impact on the nature of the liquidation, including timeframe and realisation strategy.

It has been suggested that the failures of Northern Rock (NR) and Bradford & Bingley (B&B) in the UK could provide useful insight as to the strategy and range of recoveries which could be achieved in a liquidation of BPE.

For the avoidance of doubt we considered this at the time of preparing the Report, including as regards the overall liquidation strategy for the loan book. However, we note that these cases are not directly comparable to the BPE case due to different applicable laws, political environment, different portfolio structures and different macroeconomic situations.

In particular, the loan books of these two banks consisted almost exclusively of residential mortgages, specifically 99.7% and 97.5% for NR and B&B respectively, according to their 2007 published accounts. In contrast, BPE's portfolio consisted of only 28.0% of residential mortgages, the remainder being made of corporate exposures (including SMEs). The difference is significant, as corporate loans follow very different dynamics compared to residential mortgages, as further detailed below in subsection 5.4.2.
In addition, the two countries experienced different macro-economic patterns, with the impact on Real Estate prices in Spain being substantially worse than in the UK. Historical default rates too are different in the two countries.

Finally, it is important to note that in both UK cases the unwinding of the loan portfolios took place in the context of initial and significant state intervention (including use of public funds) thereby providing a stable platform for the run-off. This is likely to have had a significant impact on recovery rates. As noted previously, for the purposes of the Report we are required to ignore any option for state intervention.

For further details regarding the liquidation strategy used in the Report, please reference sections 2.1, 2.2, 2.3, 3.2 and 4 of the Report.

5.4. Loans and receivables

The NBV in the Report are summarised below.

### Loans and receivables NBV

<table>
<thead>
<tr>
<th>Asset</th>
<th>NBV (6 June 2017)</th>
</tr>
</thead>
<tbody>
<tr>
<td>A. Fixed Income</td>
<td>654</td>
</tr>
<tr>
<td>B. Credit Institutions</td>
<td>7,664</td>
</tr>
<tr>
<td>C. Loans and advances to customers</td>
<td>75,012</td>
</tr>
<tr>
<td><strong>Total loans and receivables</strong></td>
<td><strong>83,330</strong></td>
</tr>
</tbody>
</table>

Source: Banco Popular Individual Financial Statements

Our approach and valuation methodology is set out in section 4.1 of the Report, including segmentation, methodology, approach, key assumptions and results.

Before responding in more detail to the specific comments, we would observe that a liquidation of BPE would be unprecedented and unlike anything seen before in the Spanish market or indeed elsewhere – processes such as Northern Rock or Bradford and Bingley which have been cited to us required state intervention and as note above, are not entirely comparable. Moreover we note that, while we included a “Worst case” scenario in each of our ranges, these did not incorporate certain other negative factors which are likely to arise in a situation such as this (that is the liquidation of the 6th largest bank in Spain at the time), but where the impact is unquantifiable, such as macro-economic dislocation, contagion to the broader economy, impact on collateral values, etc. In the circumstances, we consider that our valuation range as set out in the Report represents realistic estimates as to the amount which could be recovered in the three liquidation scenarios.

Specific Comments received included those on the following methodologies and assumptions:

- **The run off of the performing loan portfolio**, specifically with regard to the receipt of interest on the book in the liquidation period.
- Suggestions that the **prepayment assumptions** for performing loans were overly aggressive and resulted in a material understatement in interest received on the book in the liquidation period.
- **Application of IFRS 9 methodology** to estimate defaults and recoveries for the performing loan portfolio.
- Requesting greater clarity on the **reclassification of certain loans as non-performing**.
- Our assumptions around the non-performing loan portfolio **disposal timeline** including that the disposal timeline was too short and that alternative hybrid strategies should have been considered.
Our assumptions around the **discount rates** applied in calculating estimated realisations from the sales of i) the non-performing loan portfolio and ii) the remainder of the performing loan portfolio at the end of the run off period, including the Comment that these were higher than “normal” levels observed in the Spanish market.

- Requests for clarification of the treatment of **intragroup/non-intragroup positions**.
- The relationship between the **accounting impairments** surrounding loans and receivables and the realisable value of BPE’s credit portfolio in the hypothetical liquidation scenario.

We comment on each of these items in the next sections.

### 5.4.1. Run off of the Performing Loan Portfolio

Some of the comments received related to the proposed strategy for the liquidation of the performing loan portfolio, including around the receipt of interest during the run off period, and the drivers for the range of recoveries.

As set out in the Report, we have assumed that the performing loan portfolio will be run-off until the end of the liquidation period at which point any remaining portion would be sold. We used an 18 month scenario, a 3-year scenario and a 7-year scenario.

During this period we have modelled that BPE would continue to receive interest on the book in line with the underlying contractual terms. The estimates of the amounts collected during the run off period reflect (amongst other things) our assumptions on the evolution of the prepayment rate and new delinquencies. In particular, whereas the level of interest received on the book post liquidation will tend to increase overall recoveries, higher prepayments in a liquidation scenario will reduce the amount of interest received. Similarly increased levels of defaults would also reduce overall recoveries. Our assumptions on prepayments and default levels are set out in section 4.1. of the Report, and further clarified below.

As set out in the Report we considered that, on balance and taking into account all the other factors, the 7-year scenario represents a reasonable scenario, which may generate enhanced recoveries through a more orderly disposal and work out of these assets.

We received Comments surrounding the run off of the performing loan portfolio, and our valuation of said portfolio. The performing portfolio of loans and receivables (credit to customers) at the date of analysis presented a GBV of €59,521m\(^20\) (NBV of €59,350m). In the best-case scenario within the 18-month time horizon (note that this is not the overall best case for the 3 scenarios), this portfolio would have an estimated realisable value of €52,563m. The worst-case scenario for the same time horizon, and the best and worst case realisable values that would arise in the other time horizons (3-year and 7-year scenarios) were also considered and the results presented in the Report\(^21\).

### 5.4.2. Prepayments

We received comments that the **prepayment assumptions** for performing loans, and specifically for corporate and mortgage customers, appeared unduly high in comparison with a going concern scenario and consequently that we were understating the level of interest receivable on the book. We comment on this below.

**Corporate customers**

We noted in the Report that corporate customers rely, for the running of their daily operations, on a fully functioning bank that can offer a full range of products and services;

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\(^20\) Pages 39 & 44 of the Report

\(^21\) Page 50 of the Report
a bank in liquidation would be unable to provide certain of these, specifically, transactional banking activities which a corporate customer would need to move to a new financial institution.

Moreover we noted that the Spanish retail banking business model is based on building deep relationships with clients. In this scenario of BPE’s liquidation, many of the corporate customers would hold commercial discussions with alternative bank providers, during which the alternative entity would be well placed to capture the corporate customer’s loans as well as their transactional banking activities. For the avoidance of doubt, we are not assuming an operational link between the two products. However, we are assuming that the resulting commercial discussions would cover the customer’s entire banking requirement (both transactional and loans) and that the alternative provider would want to capture the largest possible amount of new business. Such discussions may be easier where a banking relationship already exists (multi banked clients). In particular, SMEs and lower end corporate franchise of BPE would, in our view, have been of strategic interest to other banks in Spain at that time such that a proactive strategy to capture BPE clients by one or more competitors would have been a likely outcome in a liquidation scenario. As such, we consider that the assumptions behind the increased level of loan prepayments as set out in the Report are reasonable.

In terms of Comments on relative rates of interest (loan pricing) and switching costs, as further set out in the Report, in formulating our prepayment assumptions we took into account both the customer’s appetite for change (e.g. relative rates of interest charged as between BPE and alternative providers), potential barriers (e.g. switching costs) as well as the customer’s attractiveness to other finance providers when considering a refinancing of the customer’s loans with BPE (taking into account the borrower’s risk profile, credit history, segmentation, financial standing, etc.).

In this respect, as set out in the Report we considered:

- Relative rates of interest - comparing the interest rate payable on outstanding loans (as shown in the loan data tape provided) with the interest rates applied to new analogous transactions at the termination date; and
- Termination costs – including reviewing a sample of contracts in order to gain an understanding of the termination costs arranged for each standard contract, as well as measuring the impact of terminating those contract.

Moreover, as noted in the Report, in terms of the attractiveness of the customer to the alternative provider we also considered the customer’s credit quality – and we assumed that, even if they wished to refinance, certain borrowers would be unable to migrate as a result of poor credit history, sectoral issues, etc.

Finally, we received comments suggesting that borrower inertia would drive down the level of migration and that customer behaviour is not always rational. In response, while we would agree this is a factor in a going concern situation, in a liquidation scenario the situation is very different. As noted above, customers who rely on BPE for transactional banking services will be forced to re-bank, and even if there is no operational linkage are likely to migrate their loans at the same time to maintain service levels and for administrative convenience.

**Mortgage customers**

We applied a similar approach when developing the prepayment assumptions for mortgage customers.

Specifically, we segmented the book and identified those loans where the borrower was likely to find it difficult to refinance (taking into account the LTV and risk profile of the borrower) and we stripped out loans with only a short period of time left to run. Taking this into account we estimated that the majority of borrowers were likely to remain with BPE – but that 34% of all performing mortgage exposure would be prepaid within 18 months of insolvency.
Specifically, in developing the prepayment assumptions, we took into account the following:

(i) the interest rates agreed upon for each transaction to be prepaid (comparing them with new market interest rates at the Valuation Date); and

(ii) the costs of repaying the debt held with Banco Popular and the costs of arranging the new transactions with the destination banks.

When estimating the migration of clients to other entities, and as explained in the Report, all factors that could impact the process have been considered, from the perspective of supply (credit quality of the client, collateral availability, etc.) and from the perspective of demand. From this second point of view, the impact of the cancellation costs of the mortgage loans held at BPE was analysed, as well as the costs of formalising the new mortgage loans at the alternative provider.

It should also be noted that there are no barriers to prevent a customer moving their mortgage to another provider notwithstanding the fact that certain loans have a prepayment fee. Customers with deposits at BPE will have to find an alternative provider for the deposits and we considered it likely that those providers will give incentives and simplify the process of moving their other products. As a result, we did not consider this fee to be a disincentive to customers moving their mortgages. We also considered the Liquidator may be unable to enforce the prepayment fee if customers are seen as having to move because of operational difficulties of BPE following the liquidation. Finally, we estimated these fees to be in the region of €40m, for all customers leaving BPE, (i.e. not material) and therefore we did not include income related to this.

Finally, and in order to verify this last point, a sample of transactions were reviewed in order to understand the standard cancellation costs contracted by BPE, which we concluded were within market ranges.

Thus, the set-up costs associated have been considered, and we conclude that they would not create a barrier to the other forces driving migration.

It has been suggested in the Comments that when considering the economic incentives for customers to switch banks/prepay, the interest rate threshold we applied was incorrect and that this overstated the case for borrowers to switch mortgage providers. Specific reference was made to the Statistical Bulletin prepared by Banco de España dated July 2018 and data from the ECB published by Standard & Poor’s.

In responding to this comment, we would note that the mortgage rates used in the Report were calculated by benchmarking the rates (both fixed and variable) of BPE’s portfolio with those on offer at 6 June 2017 from the main mortgage providers in the Spanish market.

Moreover, we considered the rates in place for the whole life of the mortgage (rather than just the initial term), since mortgages in Spain tend to have a different rate at the beginning of the loan than in the rest of the life of the contract.

These rates were calculated by averaging the percentage of both variable and fixed mortgages in the Spanish market at the time. These weights were multiplied respectively by the average rate offer for new business for variable and fixed rate mortgages. The resulting rates will be different to the ones indicated by both Banco de España and S&P, since Banco de España and S&P reflect only the initial rate of the mortgage.

5.4.3. Application of IFRS 9 methodology

A number of Comments suggested that our use of IFRS 9 methodology was inappropriate to determine estimated cashflows in a liquidation.

For the avoidance of doubt, as set out in the Report, we adopted a DCF approach when preparing the valuation of the loans and receivables portfolio reflecting the contractual cash flows, including interest and amortisations, over the liquidation period. In the circumstances, a number of assumptions had to be made, including the use of Probabilities of Default (PDs)
and Loss Given Default (LGDs) as proxies for the default and recovery curves, the data for which was unavailable to us.

Based on our analysis, the PDs and LGDs estimated by BPE correspond to the last default rates observed in BPE. Consequently, based on BPE’s credit portfolio at the Valuation Date and the PDs and LGDs estimated by BPE:

- The expected cash flow from repayment, of the principal and interest, on a portion of the portfolio was adjusted.
- The future default rates were estimated. These were considered in the valuation of the portfolio at the point of sale of the rump portfolio at the end of the relevant liquidation period, simulating the analysis that a potential or actual investor would perform.

5.4.4. Reclassification of certain performing loans as non-performing

As set out in the Report, an insolvency of BPE would have far reaching consequences, including for borrowers, and was likely to lead to an increase in the level of defaults (e.g. borrowers also holding transactional accounts with BPE could see those frozen and be unable to access their funds, others may raise counterclaims as a reason for not making or delaying scheduled repayments). This increase would be concentrated in the parts of the portfolio and/or for borrowers, already under stress and would be exacerbated by the difficulties in maintaining a proactive stance in the management of these loans given the disruption to BPE operations and staffing resulting from the insolvency. Based on our experience and expert judgement, we consider that those borrowers identified as stage 2 in the data provided are at a high risk of default. This classification jointly with other factors (e.g.: associated collateral) drive the estimation of the delinquency increase and reclassification. In this respect the situation is different to a going concern accounting analysis.

Regarding the amount reclassified, the total NPL exposure before the reclassification amounted to €19,055m and €20,200m after this reclassification. After the reclassification, the total NBV of the NPLs, represents 25.3% of GBV with 87% corresponding to companies and 10% to exposure to mortgage loans. The remaining 3% is composed of consumer and other household loans, as well as general government loans.

Regarding the comments surrounding the term “watch list” used in the Report, the concept of watch list/ under special surveillance, was defined by BPE for the purposes of management, monitoring and control of the credit risk to which it was exposed. This definition is aligned with the regulatory and prudential definition of watch list/ under special surveillance (IFRS 9 and its best adaptation to Spanish legislation, that is, Banco de España Circular 4/2017, along with capital regulations that were applicable to BPE).

The term implies an indication of clear credit impairment risk (e.g. the debtor is a certain number of days in default at the date of analysis), which will make more difficult the borrowers’ ability to migrate its loans to another finance provider. Moreover, we note that in the course of our work, we reviewed BPE’s criteria for categorising impaired operations in the watch list, and conducted a query to determine the correct categorisation of these operations within the watch list.

5.4.5. Non-Performing Loan Portfolio disposal timeline

It has been suggested that the timetable proposed for disposal of the NPL portfolio was incompatible with a strategy designed to maximise value – in particular comments have been made that greater recoveries would have resulted from a disposal and work out over a 7- year time line and/or that a “hybrid” strategy of realising different smaller/ targeted portfolios should have been considered.

In responding, regarding the NPL portfolio disposal timeline, we note that we remain comfortable with the 18-month time horizon.
The argument of BPE retaining and working out the NPLs for a longer timeframe (suggested in certain Comments) was considered when preparing the Report. However, it was considered that greater recoveries via this approach would be uncertain, whilst the costs of retaining the work-out team (taking into account the risk around key personnel leaving which would increase the level of potential inefficiencies), as well as certain other factors like the reluctance of defaulted borrowers to enter into discussions with an insolvent bank, were more certain.

A longer time frame also increases macro-economic risk; in particular there was an active market for NPLs in H2 2017 and we considered it unlikely that a Liquidator would want to speculate on favourable conditions continuing for a lengthy period of time (particularly against a background of possibly significant macro dislocation which could follow BPE’s liquidation). It was therefore concluded that a relatively short term sale was ultimately more beneficial and would not result in capacity issues which would impact on the level of realisations achieved.

In terms of additional Comments around “hybrid” options, by which we understand to mean the sale of smaller portfolios, tailored to different purchasers appetite’s, in practice the strategy would evolve following a consideration of all options including, but not limited to:

1. Sale of single name credits
2. Sale of several discrete portfolios
3. Sale of the entire NPL book
4. Hold of certain single name credits

Determining which is the most appropriate or the blend of which strategies produces the optimum result on a risk/reward basis, is likely to take the Liquidator somewhere in the region of 3-6 months, a process which would include investor soundings and would be dependent on market conditions at the time. Holding individual names for a longer-term workout by the bank would, in most cases be unlikely given the resource requirements and competing pressures on the Liquidator.

Notwithstanding the variety of strategic options available, the pricing achievable on the book is unlikely to have been materially different from that set out in the Report. Further, the timeframe for disposal of the entire book (whether as a whole or in part, in tailored buckets, etc.), within 18 months, should in our expert opinion have been achievable providing time for strategic assessment, portfolio optimisation, data collation and enhancement and execution.

5.4.6. Choice of discount rates to apply to the sale of NPL and (rump) PL portfolios

The Comments also made reference to the discount rates used in the NPLs and PLs valuation, specifically that alternative benchmarks should have been considered.

Responding to this, we note that, as set out in the Report, specific and separate assumptions were used for secured NPLs and unsecured NPLs during the valuation. As noted the discount rate will reflect the likely acquirer’s required rate of return for each asset class, as well as the quality of available data (amongst other factors), and as such may vary considerably between different portfolios.

In terms of the levels used in the Report, we consider these assumptions to be in line with market experience, derived from our considerable experience of working on a large number of Spanish NPL transactions and taking into account the nature of the BPE portfolio. Whilst the discount rates applied are slightly above levels that were observable in the Spanish NPL market in 2017, as noted in the Report, this reflects the likely lower quality of the processes and information provided to potential buyers, and the lack of representations and warranties on a sale out of liquidation.
When developing our assumptions for the discount rate to apply to a disposal of the rump PLs, we considered historical corporate and mortgage securitisations and the average level of yield demanded in the Spanish market in order to set a relevant benchmark. 

For further information regarding the discount rates used to model sale of the NPL portfolio and (at the end of the liquidation period) the rump of remaining performing loans, please refer to section 4.1 of the Report.

5.4.7. Intra group loans

An additional point of clarification in this sub-section is related to the classification of both intra-group and non intra-group positions. As set out in the Report intra-group positions can be with both credit institutions and non-credit institutions. Intragroup positions with credit institutions are reflected within Loans and Receivables (Credit Institutions)\(^{22}\) and have a NBV of €4,081m. Intra-group positions with non-credit institutions are reflected within Loans and Advances to Customers\(^{23}\) and have a NBV of €2,345m.

5.4.8. Impairments

With regards to the accounting impairments surrounding loans and receivables, it should be noted that the methodology for calculating value adjustments for credit risk, attributable to the possible default of the client (“accounting impairments”), does not reflect the realisable value of BPE’s credit portfolio, both performing and non-performing, in a liquidation scenario.

The level of accounting impairments made by BPE and included in its financial statements reflect the losses that would result from defaults in a going concern scenario taking into account accepted accounting rules. The valuation made and reflected in the Report considers cashflows across the entire lifespan of the individual loans and the additional impairment that would result from a liquidation scenario.

Finally, we note that in our valuation, variables not reflected in BPE’s accounts have been considered. Some examples of these are: (i) the increase in NPLs resulting from a liquidation scenario and (ii) migrations of part of BPE’s customers to other operating banks.

For further details regarding loans and receivables, please reference sections 2.2, 3.2, 4.1 and 4.4 of the Report.

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\(^{22}\) Page 37 of the Report

\(^{23}\) Table included in page 38 of the Report that is detailing the line “C. Loans and advances to customers” of page 37 of the Report
5.5. Real Estate

Section 4.2 of the Report sets out the work done in respect of Real Estate assets, our valuation approach, assumptions and conclusions.

The results of our analysis are set out in the table below.

**Real Estate estimated asset realisation (€m)**

<table>
<thead>
<tr>
<th>Real Estate assets</th>
<th>NBV (6 June 2017)</th>
<th>18M Scenario</th>
<th>3Y Scenario</th>
<th>7Y Scenario</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Best case</td>
<td>Worst case</td>
<td>Best case</td>
<td>Worst case</td>
</tr>
<tr>
<td>Foreclosed assets</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>A. Non-current assets held for sale</td>
<td>3,057</td>
<td>2,113</td>
<td>1,889</td>
<td>2,386</td>
</tr>
<tr>
<td>B. Investment property</td>
<td>442</td>
<td>323</td>
<td>290</td>
<td>361</td>
</tr>
<tr>
<td>C. Inventories</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Own use</td>
<td>117</td>
<td>78</td>
<td>73</td>
<td>85</td>
</tr>
<tr>
<td>A. Building &amp; branches</td>
<td>5,166</td>
<td>2,514</td>
<td>2,252</td>
<td>2,832</td>
</tr>
<tr>
<td>B. Furniture</td>
<td>129</td>
<td>0.1</td>
<td>0.1</td>
<td>0.1</td>
</tr>
<tr>
<td>Total (excl. furniture)</td>
<td>3,745</td>
<td>2,514</td>
<td>2,252</td>
<td>2,832</td>
</tr>
</tbody>
</table>

Comments relating to real estate assets covered the following topics:

- Suitability of the Valuation approach – specifically the use of a “statistical” model, haircuts and the effects of using a massive portfolio, as well as the suitability of the valuation model to estimate realisations in a liquidation scenario.
- Application of macroeconomic forecasts – specifically whether the Report captured the real estate market recovery.
- Disagreement with the assumed disposal period.
- The consideration of the impairment coverage ratio when valuing the real estate assets.

5.5.1. Valuation approach

In terms of the Comments that suggested an asset-by-asset approach should have been used, we note that the portfolio comprises c.512,000 assets. Considering that a valuer typically requires between 2 and 3 hours on average to conduct one property valuation, and that an asset-by-asset analysis of this portfolio would require between 1 million and 1.5 million working hours, this approach was not followed.

As noted in the Report, we therefore used a statistical model to value the Real Estate asset portfolio, following a consistent valuation methodology. This incorporates a national database of values and takes into account the heterogeneity of the Spanish regions and specific local real estate conditions. This methodology adjusts the latest appraisal value provided for each asset considering its location, typology, status, and other macroeconomic inputs, such as CPI, unemployment rate, disposal income, labour force, etc. to a current value as at the Resolution Date. This would be consistent with the approach which Banks typically take to value their real estate assets.

To complement this approach, we followed an asset-by-asset analysis for a sample of assets within the portfolio. We conducted this analysis, considering the cases with the highest GBV, in order to challenge (and as necessary adjust) the outcome from the results produced by our statistical model. For consistency, we applied a similar approach when valuing properties owned by the REO subsidiaries (although we note that the liquidation strategy for these was different as the entities could be sold as going concerns).
Aside from these assets, the branches and headquarters within BPE’s real estate portfolio were valued utilising a market approach.

Comments were raised about using the ECB’s bottom-up analyses when conducting the valuation for BPE’s real estate assets. It is important to highlight that this scenario is not considered in the Report, since it references a going-concern scenario, and not one of BPE’s liquidation.

Comments were also raised on the haircuts applied under Circular 04/2016 (which defines some guidelines to adjust, in general terms, the appraisal value of each Real Estate asset in order to estimate its realisation value) including that these have been reduced under Circular 04/2017. We note that these haircuts have been calibrated by Banco de España considering the Real Estate commercial experience of all the Spanish financial sector, and not only of BPE. In this context, instead of considering a sectorial approach, we applied an approach base on the estimation of the individual real estate asset’s market value. The application of this methodology refines in a better way the valuation of the properties.

In terms of the use of a massive portfolio sales approach, taking into account the nature and size of BPE’s real estate portfolio, we believe this is the optimum approach to consider the realisation of these assets in a liquidation scenario in the defined periods. Furthermore, the quality of individual Real Estate assets was taken into account by the model and the portfolio sale strategy would not preclude sales of individual assets – however we do not consider that this would change the overall level of realisations.

With regards to the reliability of the Statistical/Automatic Valuation Model, as set out above we considered that the most appropriate way to conduct a valuation of a large Real Estate asset portfolio was through an AVM (Automatic Valuation Model). The market practice for the valuation of banks’ real estate exposure is the use of an Automatic Valuation Model which is consistent with our approach and based on our experience from acting as Liquidators what a Liquidator would do in the circumstances. The employed model has been used in the valuation of a large volume of Real Estate assets owned by financial entities and Investment Funds.

In addition, it is necessary to highlight that the resulting valuation corresponds to a valuation under a liquidation scenario that considers the disposal of the entire real estate portfolio in a defined term (18 months, 3-year & 7-year scenarios) as set out in the Report.

5.5.2. Application of Macroeconomic Forecasts

Some of the Comments suggested that Deloitte did not take into account the real estate market recovery when preparing its Report.

As noted above (in section 2 of this Clarification Document), for the purposes of the Report we were required to estimate the insolvency recoveries based on the information and circumstances at 6 June 2017. Given the above, our analysis was based on information as at close of business on that date or which could reasonably have been obtained at that date.

As noted above, given the age of some of the valuations, we indexed these upwards to reflect the situation as at the Valuation Date. The Real Estate asset valuation thus included the market recovery registered from 2015 to Jun 2017.

Moreover, third-party valuation reports provided by BPE for collateral had not been updated for some years. We indexed these values from the year in which the valuation was carried out to the Resolution Date, using a trusted index conducted by Deloitte, based on public information such as Ministerio de Fomento or INE and accepted by the market.
Finally, when assessing future prospects, consistent with the requirements above, we took into account the economic forecasts as at Q2 2017. The forecast improvement in the Spanish market is therefore reflected in our estimates. Under article 1 of the Commission Delegated Regulation (EU) 2018/344 – 14 November 2017 (DR), we are not allowed to take into account further upward revisions in the forecasts - the same would apply in terms of any downward revision.

5.5.3. Disposal Period

In terms of Comments on the assumed disposal period, as noted in the Report we considered three scenarios for the liquidation of BPE. Based on this valuation exercise, the realisation value of this portfolio ranged from €2,252m (worst case) to €2,946m (best case) depending on the assumed scenario.

In performing our analysis, we first established the optimum disposal period for the sale of each of the real estate assets based on the specific typology and location of the individual asset. Deloitte’s expert judgement, based on a benchmark that considers the historical sales of financial entities with Real Estate exposure, allowed us to assign a specific timeframe for each one of BPE’s Real Estate assets, reflecting the condition of the Spanish market.

As noted above, we are required to consider the disposal of all assets in the liquidation period. Accordingly, where the optimum disposal period was shorter than available under the scenario, we made an adjustment to reflect a shorter timeframe.

The range provided for the valuation under this liquidation scenario is deemed reasonable from a market perspective.

5.5.4. Real Estate impairments coverage

Finally, in reference to the Comments on the impairments coverage ratio, we note that accounting provisions do not reflect specific cash flows that are released when selling the assets. Rather, they represent allowances for possible diminution in value which may occur on disposal and as such are applied directly against the accounting value. Moreover, accounting impairments for Real Estate assets were considered when we prepared the Report.

For further details regarding BPE’s Real Estate assets please reference sections 3.2., and 4.2. of the Report.

5.6. Tax assets

The results of our analysis as set out in the Report are summarised below:

<table>
<thead>
<tr>
<th>DTA estimated asset realisation (€m)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tax Assets</td>
</tr>
<tr>
<td>------------</td>
</tr>
<tr>
<td>CTA</td>
</tr>
<tr>
<td>Protected DTA</td>
</tr>
<tr>
<td>Non Protected DTA</td>
</tr>
<tr>
<td><strong>Total</strong></td>
</tr>
</tbody>
</table>

Source: Deloitte analysis

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The Comments relating to tax assets covered both the scenario of the valuation of the tax assets, and how this scenario compared to the situation after the resolution.

5.6.1. Comparison to the post resolution scenario

The valuation of the tax assets was conducted under a scenario of BPE’s liquidation, as referenced in the Report, and not under a “sale of business as a going concern” scenario to another banking group.

Some comments suggested alternative approaches could have been taken when analysing the Protected DTAs of BPE. It is important to note that the regulation of the conversion of the Protected DTAs into a credit against the Spanish Tax Authorities is regulated by Article 130 of the Spanish Corporate Income Tax Act (Law 27/2014 of November 27th).

Looking at the Comments, there are two clarifications that may be of assistance in understanding the value of BPE’s DTAs:

- Protected DTAs: All protected DTAs (€2,031m) were included in the estimated realisation value.
- Non Protected DTAs: The DTAs that were not considered in the realisation value in the Report, correspond to the major part of the Non Protected DTAs, where recoverability is dependent on set off against future taxable profits - as such this is not applicable to a bank in liquidation. In addition, Non Protected DTAs cannot be sold separately, and Non Protected DTAs not utilised before the dissolution of BPE will be lost.

Therefore, Deloitte conducted a liquidation scenario, and estimated that the realisation value of the tax assets as of June 6th 2017 would be a total of €2,334m out of a possible €5,692m.

For further details on the realisation value of the tax assets of BPE, its protected DTAs and the approach on the adjustment to the realisation value of the Non Protected DTAs, please reference section 4.3 of the Report.

5.7. JVs and subsidiaries

The Comments relating to JVs and subsidiaries covered the following topics:

- Our approach to determining the impact of BPE’s liquidation on its Investees and which entities would go into a liquidation proceeding, the completeness of our analysis, and potential capital gains of selling certain Investees.
- Some Comments noted that the “Preferred Securities” in Popular Capital should have received different treatment and been preferred creditors in the liquidation of Banco Popular and questioned if Popular Capital had been considered in the Report.
- How intragroup debt is placed in the hierarchical ranking
- Relative levels of recoveries for the 3 banking entities which would be forced into their own insolvency processes.
- The impact of terminating JV agreements, specifically whether additional termination costs were considered.
- The sources used for the calculation of the multipliers used in the market value approach.

5.7.1. Approach to determining which entities would go into liquidation

Some comments suggested that further clarity on the approach we adopted to determine the impact of BPE’s liquidation on the rest of the group (focusing on the Investees that would be affected) would be helpful.
As suggested in the Report, when considering realisations which would flow to BPE from its subsidiaries and JV investments, a necessary first step was an assessment of the impact of BPE’s liquidation on the rest of Banco Popular Group. In particular, BPE’s liquidation might lead to potential new insolvency proceedings across the Group, due to contagion effects.

We analysed the impact of BPE’s liquidation on its respective Investees, based on their financial and operational linkages, taking into account subordination of amounts due from BPE, liquidity requirements, etc. The Report explains in detail which group companies we considered would, in the event of BPE’s liquidation, enter into an insolvency proceeding or may continue to operate on an ongoing basis – our determination for each is listed at Appendix III of the Report.

To determine if an Investee might need to enter into insolvency proceeding or not, we took into account their asset value at the Resolution Date, potential impairment in assets due to BPE and other Group companies liquidation (in particular in relation to subordination of intragroup receivables) and liquidity issues which they were unlikely to be able to address in the financial markets.

Based on this prior assessment, we divided all group companies or Investees into two different clusters:

- Investees not affected by BPE’s liquidation or where the impact was minor, which could continue to operate and be sold as a going concern; or
- Investees significantly affected by BPE’s liquidation and therefore could not continue operating. In this case, the Investee would inevitably enter into an insolvency proceeding.

A number of Comments were submitted regarding the completeness of our analysis of JVs and subsidiaries in terms of the impact of an insolvency of BPE and value which would flow back to BPE. For the avoidance of doubt, when modelling realisations for BPE (either in terms of a recovery of intragroup receivables or in terms of equity held by BPE) we included all group entities, as set out in the JV and subsidiaries section of the Report.

For the Investees not affected by BPE’s liquidation, we estimated their equity and other assets recoverability.

In the case of significant Investees (assets greater than €1bn) that enter into an insolvency proceeding due to BPE’s liquidation, we conducted an extensive exercise to determine the recoverable value of BPE’s rights in liquidation. Finally, regarding non-significant Investees in liquidation, the recoverable value of BPE’s rights were assumed to be immaterial.

Banco Popular Group at the Resolution Date comprised 123 legal entities of which BPE, the parent company, had a direct stake in 79.

Regarding Comments on how the values included in the Report (section 4.4) are broken down, the NBV of JVs, Subsidiaries and Associates was €9,908m. Of all these entities, there were 38 where BPE had shares (directly held), that we identified would remain ongoing. The realisable value for 34 of these 38 entities was calculated on an individual basis, as referenced in section 4.4 of the Report. We did not calculate realisable values individually for the outstanding 4 entities since their NBV was lower than €0.1m.

The NBV of the 38 entities was €8,271m. For these entities, we estimated a recoverable amount range between €7.5bn and €8.4bn.

With regards to BPE’s equity investment in Joint Venture, Associates and Subsidiaries, we have not assumed any specific penalties or price reduction on their valuation due to the liquidation scenario, except for those forced to enter into an insolvency proceeding due to BPE's liquidation.

Within the range provided, the Report implies potential capital gains for several investments (mainly WiZink, Allianz Popular, Totalbank and other financial services entities), whereas the estimated recoverable amount for other entities was below to the net book value (mainly real estate related entities). Regarding the Comments that mention known offers for
Investees, we can state that for those entities for which an offer or price indication had been received prior to resolution, we assumed that the potential bidder had a deep knowledge of BPE’s situation as of the offer date and, therefore, no discount was applied.

5.7.2. Popular Capital

We note that the Popular Capital SA legal entity was considered in our analysis. In terms of Comments around the treatment of the Preferred Securities, we note that according to article 48.1 a) of the Law 11/2015, the internal recapitalisation will be executed by amortising or reducing the amount of the shares, capital instruments or liabilities following the order stipulated in the aforementioned article, starting with the ordinary capital elements of Tier 1 in proportion to losses and as far as possible. In BPE’s case, the Preferred Securities issued by Popular Capital were recorded as Tier 1 capital instruments by BPE and as set out in Popular Capital’s prospectus. Moreover, the prospectus sets out that the proceeds would be deposited on a permanent basis with BPE or with another credit entity of the Group and will be available to absorb losses of the Group once shareholders’ equity has been reduced to zero.

The prospectus further notes that in the event that proceedings for the liquidation, dissolution or winding up of BPE are commenced or there is a reduction in the shareholder’s equity of BPE pursuant to Article 343 of the Spanish Corporations Law, the Issuer shall be liquidated by BPE and the holders of Preferred Securities at the time outstanding will be entitled to receive only the Liquidation Distribution in respect of each Preferred Security held by them. In such an event, the Liquidation Distribution per Preferred Security shall not exceed that which would have been paid from the assets of BPE had the Preferred Securities been issued by BPE.

At the resolution date, Popular Capital had a balance sheet of €93m, of which €88.1m were loans to BPE, €1.7m were deposits in BPE and €3.3m were non protected DTAs. The total recoverability estimated for Popular Capital’s assets, based on the latest available financial information, was zero.

The €88.1m of loans to BPE and €1.7m of deposits in BPE were intra-group claims. According to article 42 of the Commercial Code, any creditor claim over another from the same Group Company in an insolvency proceeding has to be considered as an Intragroup claim, regardless of asset type or encumbrance.

In the case of BPE’s liquidation, for the three proposed time scenarios, the recovery value of intragroup claims would be nil (see section 6 of the Report).

Given the above, Popular Capital would be forced to make provisions and write-offs worth €89.8m (€88.1m + €1.7m), or 96% of total assets, and would therefore be forced into an insolvency proceeding.

The remaining €3.3m of Popular Capital assets, according to the information provided, consisted of non protected DTAs. As explained in the Report (see section 4.3), no recoverability is expected (in general terms) from non protected DTAs in a normal insolvency proceeding.

Therefore, the recovery value for Popular Capital’s bondholders would be zero.

5.7.3. Subordination of Intragroup Claims

Some Comments related to the liquidation scenario as it relates to BPE’s JVs and subsidiaries and the treatment of amounts due from group entities. In this respect we note that intragroup claims are subordinated under the Spanish Insolvency Act - there is a hierarchy within the subordinated class and intragroup claims are at the bottom of this, just

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one-step above equity. Therefore, if a group entity enters into an insolvency proceeding due to BPE’s liquidation, all of BPE’s rights against these (now) insolvent intra-group companies will be subordinated and its recovery value is likely to be significantly impaired.

We should highlight that the intragroup claims position in the Portuguese Insolvency Act is different.

What is common between the Portuguese and Spanish insolvency acts is that all subordinated claims are ranked behind unsecured/ common creditors, and that intragroup claims in Portugal are also subordinated, but at a different level within the subordinated class when compared to the position under Spanish law.

5.7.4. Banca Privada, Banco Pastor & Banco Popular Portugal

Some comments focused on the range of recoveries for the 3 banking entities (Banca Privada, Banco Pastor and Banco Popular Portugal) and requested further clarification as to the differences between these entities and BPE itself.

As noted in the Report, we considered that, following a liquidation of BPE, all of these would enter into an insolvency proceeding, reflecting asset impairment (loan subordination - Banca Privada and Banco Pastor) and (Banco Popular Portugal) because of liquidity issues.

Relative rates of recovery, will vary depending on the underlying assets in each entity and thus direct comparison is not possible; however, we can confirm that the same methodology and assumptions were applied across the group.

**Banca Privada**

For Banca Privada, its intragroup position at 6 June 2017 was 41.5% of all total assets, which substantially reduces the overall level of recoveries.

Banca Privada’s asset realisation value was almost identical for the three chosen time scenarios. Banca Privada’s overall assets were concentrated in two financial portfolios, loans and receivables and available-for-sale financial assets. Both portfolios accounted for 94.4% of total assets (including intragroup positions) and their realisation value was almost identical in the three chosen time scenarios.

- 77.5% of Banca Privada’s loans and receivables portfolio are intra-group positions against BPE, and would not be recovered if BPE entered into an insolvency proceeding. As we stated in the Report, intragroup liabilities are deeply subordinated under the Spanish Insolvency Act. We note that another 12.1% were loans against other non-intragroup credit financial institutions where we estimated a full 100% recovery.

- 96.4% of all securities within Banca Privada’s available-for-sale financial assets portfolio were level 1, which had quotes in active markets so we considered they were already at their realisable value. They would be realised within the first few months of the commencement of the insolvency proceeding.

- Other Banca Privada significant portfolios were cash and balances with central banks and derivatives for hedging accounting, which we (similar to above) considered already at realisable value and with a full 100% recovery.

**Banco Pastor**

A high percentage of Banco Pastor’s assets were intra-group positions with the parent company (BPE) or other Group companies, which would also enter into a liquidation proceeding. In particular, for Banco Pastor, 53.3% of its total assets were intra-group positions. Given the subordination of intragroup claims under Spanish insolvency law, this substantially reduces the overall level of recoveries in this entity.

**Banco Popular Portugal**

When looking at BPE’s investment in Banco Popular Portugal, it is necessary to consider our comments above around the different treatment of intragroup claims in Portugal. Moreover
we note that Banco Popular Portugal was in the situation of having net payables to BPE. Based on our analysis, asset realisations in Banco Popular Portugal are sufficient to repay part of the intragroup positions due to BPE (we calculated a recovery range between 55.7% for the worst case and 76.4% for the best case).

5.7.5. Joint Venture Agreement Termination

In terms of Comments relating to termination rights exercisable by third party partners in relation to JV investments, we did not include the potential costs to BPE associated with terminating existing JV agreements. Liquidation could trigger some of the JV agreements termination clauses and rights for the non defaulting party to either claim BPE or acquire the shares from BPE. The Report assumed that BPE’s part of the JVs would be sold to the JV partner, since the alternative would be to lodge a claim as creditor with uncertain prospects of recovery. The impact of including additional termination costs would be to further lower recoveries and would therefore not change the overall conclusion of the analysis.

5.7.6. Multipliers used in our valuation

Our methodological approach for valuing BPE’s ongoing subsidiaries and JV’s is set out in the Report.

Regarding comments raised around application of the market approach, our estimates of the recoverable amount are based on (as applicable): (i) third party valuation reports; (ii) offers or price indications received; (iii) transactions already announced; (iv) price of put / call options included in investment agreements; and/or, (v) other valuation techniques. In cases where market multiples were applied the sources used to calculate the multipliers were obtained from generally accepted information providers.

For further details regarding the liquidation and valuation of BPE's JVs and subsidiaries, please reference sections 2.2, 3.1, 4.1, 4.4, 5, 6 and appendix III of the Report.

5.8. Intangible assets

As noted in the Report, the requirement (and scenario) is the hypothetical insolvency of BPE at the Resolution Date. As set out in the Report, we considered that this would lead to the loss of the banking licence and BPE’s liquidation which would result in a cessation of operations other than to realise BPE’s assets and distribute the recoveries to creditors. Given the nature of the intangible assets, based on our analysis and experience, we considered that the realisable value for these assets was nil or very low.

Some of the Comments suggested that BPE’s intangible assets should have had a higher recovery value than assessed in the Report.

Intangible assets on the BPE balance sheet as at the date of Resolution comprised: goodwill, trademarks, computer software and customer relationships. While the computer software would be utilised by the Liquidator during the liquidation period, none of these assets have any material realisable value in their own right.

Furthermore, since we operated under a liquidation scenario, and given the nature of the intangible assets, the recoverable amount of these assets would not be affected by the length of the liquidation period.

Our additional comments and explanations are set out below.

5.8.1. Recovery Value

Considering the nature of the intangible assets, under a liquidation scenario, we estimated that the recoverable amount of these assets would be nil or very low.

- Goodwill: As noted in the Report this derives principally from the acquisition of Banco Pastor, which itself is likely to enter into liquidation. Goodwill is primarily an accounting concept and as such has no intrinsic value of its own which can be
separated out and sold. The net book value of the asset, as included in BPE’s balance sheet, is not appropriate as a base for the amount which could be realised. Under a liquidation scenario and the loss of the banking licence, we considered that the recoverable amount of goodwill would be nil, and that no third party would pay for this kind of asset.

- Customer relationships: While it is the case that (on occasion) value can be realised from the sale of a customer database/customer relationships, this depends on a stable customer base and an on-going concern business. In the scenario of BPE’s liquidation with customers’ deposits frozen, customers needing to migrate their banking requirements as a matter of urgency and significant antipathy to BPE it is unlikely that the Liquidator would be able to realise any significant value for this asset.

- Trademarks: we consider that in the event of a cessation of the business and the Banks’ insolvent liquidation, with customers unable to withdraw their money, etc., any brand value would be severely tainted which would adversely impact any potential realisation. While it has been possible in other non-financial liquidation situations to sell on the name, we considered this unlikely, in this case, given that the banking industry relies heavily on customer confidence.

- Software: Given the specific nature of the software that BPE had recorded in its balance sheet, it was not considered likely that any third party would pay to acquire it from the Liquidator. In particular the software would be heavily tailored to BPE’s own systems and requirements and is not separable in its own right. However, it was considered that the software could continue to be used to collect in the assets. Therefore, no third party servicing fee was considered in the loan portfolio valuation.

For further details regarding the estimated recoverable amount of the intangible assets, please reference section 4.5 of the Report.

5.9. Fixed income and derivatives

The Comments relating to equity, fixed income assets and derivatives covered the following topics:

- The methodology applied in Deloitte’s analysis, including the adjustments made to the fixed income asset portfolio, as well as a specific question as to whether any downward adjustment had been applied to fixed income assets included in loans and receivables.

- A suggestion that the methodology applied led to an undervaluation of the “level 3 assets”.

- Comments suggesting the undervaluation of BPE’s derivatives.

5.9.1. Valuation methodology & Adjustments

As set out in the Report, the scenario being considered for the Valuation of difference in treatment Report is the liquidation of BPE. In such a scenario, we would anticipate significant reductions in value versus the NBV due to, for example: contagion from the BPE failure causing market and liquidity issues impacting exit value; termination claims, re-hedging costs and other associated claims from derivative counterparties; and operational challenges from selling portfolios from liquidation.

However, in performing this exercise for the equity, fixed income and derivative portfolios, given the challenges in estimating these negative impacts, we used market standard bases for valuation assuming an orderly exit without adjusting these market values for liquidation specific challenges. The valuation outcomes in the Report are therefore unlikely to undervalue the realisations in liquidation.
The principal adjustments between book value and the amount estimated to be realised in liquidation (using fair value as a proxy) arise as follows:

- Recalculating the fair value amount at 6 June 2017 for assets which are otherwise held on the balance sheet at amortised cost, being the fixed income portfolio within Loans and receivables (€654m) and Held-to-maturity assets (€6,997m). These portfolios were entirely made up of corporate and sovereign bonds with observable market prices (Level 1). Further details regarding the realisation values of these items can be found in the “Equity and fixed income estimated asset realisation” table in section 4.6 of the Report. The realisations for Loans and Receivables – Fixed Income were included in the summary table in the Executive Summary (“Estimated assets realisation values in liquidation”) under Loans and Receivables.

- Recalculating the fair value amount on Level 3 assets included within the Available for Sale portfolio. The methodologies used for the valuation of these assets, which did not have an observable market price followed market standard methodologies. An adjustment arose based on use of our modelling approach and inputs, which were different to those adopted by BPE. Total book value of level 3 assets was €331m.

Adjustments were made after the valuations were calculated to remove the fair value of intercompany positions in the available for sale category and to correct minor errors in the Held to Maturity data tape. This accounts for the difference between the value ranges in section 4.6. of the Report and the summary table in the Executive Summary (“Estimated assets realisation values in liquidation”).

With regards to the Comments that suggested an undervaluation of BPE’s derivatives, the calculation methodology and assumptions, their compliance with the applicable technical valuation standards, and the results obtained are detailed in the Report in section 4.7 "Derivatives position".

5.10. Other assets

The Comments relating to Other Assets were in terms of the valuation approach and a request for explanation of the resulting values.

Given the different nature and typology of the assets within the so-called “other assets” portfolio, the adoption of a single valuation approach was inappropriate. Therefore, we analysed individually each item line and estimated its recovery rate based on available information and underlying asset nature.

5.10.1. Valuation approach and explanation of results

According to BPE's balance sheet at the liquidation date, the NBV of Other Assets amounted to €1,045m as set out below:

- €702.7m temporary positions (including an overvalued position of €420m and €282.7m being transactions in transit) which are netted against corresponding liabilities
- €17m intra-group positions
- €325m other assets (e.g. material storage, pending advertising invoices)

For the temporary positions these were reviewed and netted correctly with their corresponding liability positions, thereby reducing creditors by the same amount. Thus while the net recoverable value of temporary positions was zero the corresponding reduction in creditors also needs to be considered.

Breaking down the €17m corresponding to intra-group positions:
- €8m rights against on-going Investee companies (companies within BPE that are not affected by BPE's liquidation). We assumed a 100% recovery; and
- €9m against Investees in insolvency proceedings (companies within BPE that are forced to enter into a liquidation process due to BPE's liquidation, including Banca Privada and Banco Popular Portugal). For these we estimated a recovery of c.11% based on a detailed modelling of the liquidations of the relevant entities.

In relation to the remaining €325m, we carried out individual and detailed analysis in order to estimate their recoverability. We should highlight that data gaps and inconsistencies across the other assets portfolio were high as we could not easily source identifiable and valuable items, such as general and personnel expense accruals. Based on all information available and provided by BPE, we estimated a 48.2% recovery on this remaining €325m.
5.11. Legal contingencies

The Comments relating to legal contingencies covered the following topics:

- Whether the “Sources of uncertainty” as set out in the Report and the noted unavailability of certain information surrounding contingent claims, affected our conclusions, the additional information considered (e.g. 2016 capital issuance) as well as the challenges to the legal contingencies costs for the 2012 capital issuance.
- A request for further explanation of the distinct categories of potential legal exposure and litigation costs assumed for BPE
- Comparison to the level of accounting provisions made by BPE in its financial statements.
- The distinction in the hierarchy between the different types of plaintiffs.

5.11.1. Information surrounding contingent claims

The scenario being modelled is the hypothetical liquidation of BPE. Based on our experience, we considered that this is likely to lead to a significant increase in the level of claims. The process applied to evaluate the level of legal claims is set out in the Report.

As noted there, we reviewed BPE's financial statements (including the relevant calculation and assumptions), discussed them with BPE's internal legal team, and considered whether the estimates should be revised or whether additional claims could arise in the event of a liquidation of BPE. Our review included all relevant information available to us at the time.

In terms of the risk of capital increase claims in a liquidation scenario this was included in the analysis, and is based on our knowledge of the sector.

In terms of the “uncertainties” noted in the Report, we considered that the level of information available in relation to legal contingencies was sufficient to allow us to reach a conclusion as regards the treatment of ASCs for the purposes of the requirement, as referenced in section 4.9 of the Report.

The contingencies not provided were valued with a value of zero by Deloitte, so having more information from BPE would have resulted in a value equal to or greater than zero, negatively impacting the ASCs. In other words, the lack of information relates to the volume of claims, and not to any other aspect.

5.11.2. Discrete claims & litigation costs

Regarding the request that more information should be provided for the discrete categories of potential legal exposure discussed in the Report (namely floor clauses, mandatorily convertible notes, mortgage loan expenses, capital increases and real estate development bank warranties), the Report contains an individual explanation and valuation with respect to each of the different categories.

In terms of specific comments on the 2012 capital increase claims, as is explained in the Report, claims regarding the capital increase of 2012 may arise, due to: (i) claims of the shareholders looking back to potential errors or omissions in the original capital raise prospectus as grounds for a claim which if successful, would allow the shareholder to recover damages against BPE, but as a creditor, rather than as a shareholder (according to the Bankia precedent) and (ii) the statute of limitations had not expired.

As regards comments on the 2012 capital increase, that these were highly unlikely given the time passed, we considered that while potentially less likely than in relation to the 2016

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28 The Comments regarding the redaction of information in the Report will be addressed by the SRB.
capital increases (hence in our low scenario we assumed zero claims) the possibility of claims could not be entirely ruled out.

In terms of comments on litigation costs, the scenario of the Report is the liquidation of BPE. When making a comparison to resolution any additional litigation costs arising in the liquidation, which would not arise in resolution, need to be included in the analysis. This is the basis upon which we prepared the Report.

5.11.3. Comparison to provisions levels in the financial statements

As regards Comments on the level of the provisions in BPE’s financial statements and how these compared to our estimates, it will be noted that the financial statements were prepared on a going concern basis. The accounting criteria that BPE followed for the calculation of the provisions of legal contingencies, outside of the insolvency proceeding, would be different to the calculation to be carried out in the framework of a liquidation scenario. The accounting criteria does not apply in insolvency. Moreover, the creation of an accounting provision does not establish specific rights within the creditor hierarchy in a liquidation, and does not provide a preference to those creditors to recover any amount.

Accordingly, the provisions levels calculated by BPE in the financial statements will likely be different as BPE’s provision levels do not reflect a liquidation scenario (and indeed may be at a different point in time). The same would potentially apply to other estimates referred to in the Comments.

5.11.4. Ranking of Capital Increase claims

The Comments also included observations in relation to the ranking of claims in relation to the BPE capital increases.

The Report provided a detailed explanation with respect to the potential legal claims regarding BPE’s 2012 and 2016 capital increases.

Some Comments were raised around the distinction in the hierarchy between the different types of plaintiffs. With regards to the claims arising from capital increase, to estimate the potential claims of shareholders, we considered the investor profile, the shareholding structure provided by BPE, the shares by the board of Directors, and the elapsed time. Hence, we have excluded from the perimeter the percentage of shares owned by BPE Directors and by shareholders holding more than 5% of BPE’s equity, mainly because we did not consider it a potential risk for the following reasons:

- The Directors will be considered as persons specially related to BPE under the article 93.2. 2º of the Spanish Insolvency Act.
- Following the Bankia case precedent, those claims would not prosper.

For further details regarding the legal contingencies, please reference section 4.9 of the Report.

5.12. Liquidation costs

The scenario under consideration is the liquidation of one of Spain’s largest banks (at the Resolution Date). The methodology and approach adopted in arriving at our estimates of the costs of liquidation are set out at Section 4.8 of the Report.

For the avoidance of doubt, ongoing income (e.g.: loan interests in ”Loans and Receivables”) which would offset costs incurred, has been included in the Report on the assets side, as set out in the relevant sections within the Report.

The results of our analysis as set out in the Report are summarised below:
The Comments relating to liquidation costs covered the following topics:

- A suggested **overestimation of the liquidation costs**.
- A suggested **overestimation of lawyer and Liquidator’s remuneration**.
- The level of **operating expenses** in the liquidation scenario.

### 5.12.1. Liquidation costs

Regarding concerns around a suggested **overestimation of the liquidation costs**, and the nature of these costs, we provide the following clarifications. As we explained in detail in the Report, we considered the costs that would likely arise in the hypothetical case that BPE would enter into an insolvency proceeding.

These costs were divided up into the following four main categories:

- Liquidators’ fees and costs
- Employee related costs
- Contract termination costs
- Operating costs

### 5.12.2. Liquidators’ and Lawyers’ remuneration

In terms of **lawyer and Liquidator’s remuneration**, as indicated in the Report, the lawyer’s remuneration was calculated using a scale from the guidelines approved by Lawyers' Bar association. This scale is defined based on the total amount of the debtor's liabilities. In this regard, the rules to be applied are those set out in Madrid Lawyers' Bar association. The basis for our calculation of the Liquidators fees is set out in Section 3.3.1.a) of the Report.

Apart from this, reflecting the size of BPE (its asset values) and the complexity of its business and group structure, we understand that the judge would reasonably approve a higher remuneration exceeding the limit set out in the Law (including the extension from 12 months to 18 months permissible under the Law). Considering the nature and complexity of the

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29 Recopilación de criterios del Colegio de Abogados de Madrid en la emisión de sus dictámenes sobre honorarios profesionales a requerimiento judicial (aprobados por la Junta Gobierno de 4 de julio de 2013) y Arancel de Derechos de Procuradores de los Tribunales (https://www.cgpe.es/arancel/)
hypothetical insolvency of BPE we therefore consider that these are low estimates of the costs.

5.12.3. Employee related costs & operating expenses

As set out in the Report we considered the staffing and other requirements of the Liquidator to manage the realisation of assets process (including the ongoing service of the loan book and receipt of interest), the consideration of claims and distributions to creditors. Employee costs for the liquidation period were adjusted (significantly downwards) to reflect the fact that under the scenario this would no longer be a functioning bank (hence there would be no need for a branch network) – but reflecting also the cost of the redundancy exercise. Similar adjustments were made in terms of other operating costs reflecting the Liquidator’s requirements to manage the insolvency proceedings. Our detailed assumptions are set out in the Report.

For further details regarding the calculation of the liquidation costs, please reference sections 3.1, 3.3, 3.4 and 4.8 of the Report.

5.13. Shareholders, creditors and Deposit Guarantee Scheme hierarchy

The Comments relating to the shareholder, creditor and DGS hierarchy covered the following topics:

- A request for further clarity around the different levels of the hierarchy under Spanish insolvency law, specifically in terms of calculating the aggregate assets and aggregate liabilities.

- The creditor and DGS hierarchy: a specific comment that subordinated creditors would incur a greater loss compared to shareholders, due to their loss of principal and accrued interest, and the hierarchical difference between shareholders and subordinated bondholders.

5.13.1. Levels of the hierarchy

We note the following elements around the different established levels of the hierarchy for shareholders, creditors and deposit guarantee schemes outlined in the Report.

The creditor hierarchy used in the Report is as set out in the Spanish Insolvency Act.

In terms of Comments around the different levels of the hierarchy (aggregate assets and liabilities), we note that the creditor position was explained in section 3.4 "Creditor Hierarchy" - Table Creditor Hierarchy". The value of the assets was analysed in Section 4. Liquidation Valuation: Analysis of results, and the realisation of assets has been presented in Section 5. Estimated Assets realisation.

5.13.2. Creditor & DGS Hierarchy

In terms of Comments that suggested subordinated bondholders’ losses are greater than those of shareholders, since in the case of the former their losses will also include unpaid coupons. Both the nominal and the coupon are credits and both are subordinated credits.

In terms of Comments surrounding the hierarchical difference between shareholders and subordinated bondholders. Under Spanish law, shareholders are ranked behind subordinated bondholders – and have been modelled as such in the Report.

In reference to concerns regarding difference in treatment, above all for subordinated bondholders creditors AT1/ Tier II, we applied the hierarchy defined under the Spanish Insolvency Act.

Some of the Comments raised concerns around the treatment of the subordinated bond ISIN ES0213790001. This subordinated bond, issued by BPE, was classified as Tier II and would
mature by December 2019. For the purposes of our analysis, in a liquidation scenario, this bond would be classified in the subordinated claims class, and within that group, as AT1/Tier II.

The necessary information relating to the estimated recoveries to shareholders, creditors and Deposit Guarantee Schemes, can be found in the Report. These explanations include, among others, the amounts identified as total liabilities.

With regards to comments on non-intragroup interbank deposits, referred to in the Report as institutional non covered deposits, these were classified in the creditor hierarchy section of unsecured creditors, as ordinary claims. Payment of ordinary claims will be made once pledge creditors, claims against the state and claims with general preference have been satisfied in full.

Regarding Comments surrounding the position in relation to post liquidation interest, according to the Spanish Insolvency Act, unsecured claims will not accrue interest after the liquidation date. In the case of secured claims, interest will be accrued and paid out of secured asset realisations (but clearly limited to the realisation value of their pledged asset). This was the basis applied in preparing our analysis.

For further details regarding the shareholder, creditor and deposit guarantee scheme hierarchy, please reference sections 3.4, 4.9, 5 and 6 of the Report.
6. Limitations, Liability and Assumptions

- The Comments reviewed to prepare this Clarification Document have been provided to us by SRB. We have not participated in drafting these comments nor have we checked their accuracy to the source data. Therefore, we accept no responsibility for them.

- Deloitte has not analysed any additional documentation or data since the release of the Report, apart from the Comments, so the date of the information is up to 6 June 2017 (close of business).

- No due diligence or other auditing of data provided by BPE has been performed.

- Neither Deloitte nor any of its affiliates, employees or partners, assume any liability or responsibility, and shall not under any circumstances whatsoever be under any liability or responsibility, for the SRB or any third party’s use, or the results of such use, of any information contained in the Report or in the Clarification Document, and in particular, but not limited to, for the revelation of confidential or sensitive information included in the Report or this Clarification Document.

- This document has been prepared for the SRB in the framework of the aforementioned process. Thus, it cannot be used for a different purpose.
7. Appendix – Important Notice from the Report

The Report has been prepared for the purposes of Article 20 of the Single Resolution Mechanism Regulation (SRMR). That is to say, the Report is a fair, prudent and realistic valuation of the assets and liabilities of Banco Popular and it is prepared with independence from the Board and intended for the Board.

The Report is exclusively addressed to our client, the Single Resolution Board ("SRB"). We acknowledge SRB’s right to make a copy of our final Report public, observing confidentiality such as the identity of Deloitte staff.

The Report, and the information contained herein, does not constitute, and cannot be understood or construed as, any recommendation or advice as to whether any kind of action or process should be initiated by any party.

Neither Deloitte nor any of its affiliates, employees or partners, assume any liability or responsibility, and shall not under any circumstances whatsoever be under any liability or responsibility, for the SRB or any third party’s use, or the results of such use, of any information contained in the Report, and in particular, but not limited to, for the disclosure of confidential or sensitive information included in the Report.

As specified under Article 1 of the Commission Delegated Regulation (EU) 2018/344 – 14 November 2017 (DR), the scope of the Report is to assess the treatment that shareholders and creditors in respect of which resolution actions have been affected would have received, or the relevant deposit guarantee scheme had the entity entered into normal insolvency proceedings at the resolution decision date.

In preparing the Report, Deloitte has acted as an Independent Valuer.

Neither Deloitte nor any of its affiliates, employees or partners, assume any liability or responsibility, and shall not under any circumstances whatsoever be under any liability or responsibility, to the SRB or any third party for whatever decision taken or action adopted either by the SRB or any such third party in reliance on the Report or any other advice, information or opinion provided by Deloitte to the SRB.

The Report does not include verification work and is not, and cannot be used or understood as an audit report under any auditing standard. No due diligence or other auditing of numbers or data has been performed in the Report.

Although a number of legal issues have been identified and/or analysed throughout the Report, the Report does not constitute the provision of legal advice in any way.

The Report, and the information contained herein, has been prepared based on unaudited financial information as of 6 June 2017 when available, or as of 31 May 2017 when the 6 June 2017 information was not available, as well as on financial and non-financial information obtained from public sources, including digital and written information media (such us Bloomberg, S&P Capital IQ, research reports). All the information provided to us through the Virtual Data Room facilitated by Banco Popular Español S.A. (hereinafter “Banco Popular” or “the Bank”) has also been taken into account.

We have worked under the assumption that no information that might have changed, qualified or replaced our statements and conclusions within the Report, has been omitted. Likewise, we have not carried out any review of the completeness, accuracy, truthfulness, authenticity, validity and integrity (or the existence of any other documentation or information that might alter the content or analysis of the same) of the information provided, and we have assumed that this information is accurate, true, reliable and complete in all aspects. Accordingly, the content and conclusions herein described could be different if any of the information used was not accurate, true, reliable and complete in all aspects.

In addition to the foregoing, it must be highlighted that, within the information reviewed, there are a number of data gaps and inconsistencies in the available information, which have both adversely impacted our work and caused delays in the production of the Report.
Events and circumstances frequently do not occur as expected and there will usually be differences between prospective and hypothetical scenarios and actual results, and those differences may be material. Accordingly, to the extent that any of the information used in this analysis and Report requires adjustment or that actual results could develop or could have developed in a different way, the resulting content and conclusions herein described may be different.

The content and conclusions herein are based on prospective scenarios. Some assumptions or projections could materialise differently and unanticipated events and circumstances may occur during the periods considered by us. These could include major changes in the economic environment; significant increases or decreases in interest rates and/or terms or availability of financing; changes in the real estate market; and/or major regulatory changes. Therefore, the actual outcome could have been different to the one concluded and variations could be material and have an impact on the content and conclusions stated herein. We consider the prospective scenarios and assumptions we have developed in our analysis to be appropriate, even if alternative scenarios could be developed.

We accept no responsibility for the reliability of the information reviewed to the extent it is inaccurate, incomplete or misleading, or for matters not covered by the Report or unidentified due to the limited nature of our enquiries.

We consider that the management of the Bank is the body responsible for the information and for the data that they made available to us.

This final report is issued as at 12 June 2018 under our Specific Contract with the SRB. Our fieldwork was substantially completed as at 23 March 2018 and a draft report was circulated on 20 April 2018 after which we have not updated the content of the report or reassessed data and assumptions. We have no responsibility to update this report for events and circumstances occurring after the date of this report.

Without prejudice to the generality of the foregoing, which applies to all and any of the areas of the Report, we also refer to the relevant areas where a section called “Sources of uncertainty” containing specific limitations and assumptions has been included.

For your convenience, the Report has been made available to you in electronic copy format.