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Liability for misleading prospectus after Banco Popular resolution

In June 2017, Banco Santander acquired Banco Popular for €1 in a process managed by the Single Resolution Board and the FROB. It acquired it without an asset protection scheme after assessing the risks. It was the first time this procedure was applied and remains the only one in which it has been applied. Shareholders together with subordinated bondholders contributed to the rescue without the need for public aid. The Banco Popular shares were written down to zero. Shareholders lost all their capital. Banco Santander became the sole shareholder of Banco Popular until its final takeover. Thus, by universal succession, it became liable for all of Banco Popular's obligations, including the sentences arising from liability for the misleading prospectus in the 2016 capital increase.

In this regard, the Securities Market Law makes the issuer liable for losses caused by a misleading prospectus, i.e. for raising funds from the public with a prospectus that does not reflect a true and fair view of the issuer. This is a legal risk not excluded in the resolution agreement that led to the acquisition of Banco Popular by Banco Santander. This is how Deloitte understood it in the report that was used by the Single Resolution Board to decide on the scope of the resolution at the sacrifice of the shareholders. This is also a peaceful issue for Banco Santander, as evidenced by the fact that in the first oppositions to the claims for misleading prospectus, it did not allege that the resolution opposed the exercise of this liability by the damaged shareholders.

For this reason, it is striking that the Advocate General of the Court of Justice of the European Union, Jean Richard de la Tour, in his conclusions on a preliminary ruling on the resolution of Banco Popular raised by a Spanish court, has considered that the resolution regime precludes shareholders who have been harmed by having subscribed shares in the months prior to the resolution from claiming the liability of the issuer for the misleadingness of the prospectus. De la Tour considers that the bank resolution rules are in the general interest, since their objective is to preserve financial stability by avoiding systemic risk, an objective which precludes shareholders who have suffered damage as a result of having subscribed shares with a misleading prospectus from being compensated.

In his view, the private interest of the shareholders yields to the general interest of the resolution in preserving the stability of the system. To that end, he considers that the rule declaring liability for misleading prospectus is a company law rule which conflicts with the bank resolution regime essential to avoid systemic risk. But to maintain that liability for a misleading prospectus is limited to regulating individual shareholder rights undermines an essential part of the financial system. Prospectus liability protects investor confidence in the securities market. In short, it is the general interest in the proper functioning of the financial market that underpins both the rule governing liability for misleading prospectus and the rule governing bank resolution.

Furthermore, De la Tour contradicts the conclusions reached in a previous case, that of the Supreme Court's preliminary ruling on the extension of prospectus liability in favour of institutional or qualified shareholders in Bankia's IPO. In that case, De la Tour considered that the rule establishing liability for misleading prospectus has as its objective the "protection of investors", which involves the publication of complete, reliable and accessible information so that they can make informed decisions. Liability for misleading prospectus is a regulation that protects the investor, whether retail or qualified, whether in shares or in any other instrument used to raise their savings, against all those responsible for the prospectus, including the issuer and guarantors. On the other hand, the obligation to inform through the prospectus is a pre-contractual obligation which places the liability for a misleading prospectus under non-contractual liability. The right to be compensated for the loss caused by a misleading prospectus arises at the moment of making the investment. It is therefore not a right of the shareholder who is affected by the subsequent resolution of the issuing bank with redemption of the shares when their value is reduced to zero.

The bank resolution regime allows, as in the case of Banco Popular, for the redemption of shares in anticipation of the losses that would be borne by shareholders in a bankruptcy liquidation. What this regime does not allow is to sacrifice ordinary creditors, including creditors for claims arising from the exercise of liability actions for misleading prospectus. In order for Banco Santander to have been protected against the legal risk of actions for misleadingness of the prospectus, it would have been necessary for this to have been expressly agreed in the resolution agreement through an asset protection scheme (EPA).

This type of scheme has been common in the management of the savings bank crisis following the collapse of Lehman Brothers. They have allowed acquiring banks to cover the risks of integration, including losses caused by convictions for the improper placement of preference shares and other complex instruments. The Bank of Spain puts this guarantee at 12.48 billion euros. But Banco Santander took over Banco Popular without a protection scheme and must bear the consequences. There are precedents of entities acquiring the banking business of banks in difficulties that, without having an asset protection scheme, have tried to avoid being condemned for improper placement of financial products. However, these claims have been forcefully rejected by the Supreme Court. This was the case with Caixabank's claim, after having acquired its banking business, to disassociate itself from the convictions of Bankpime for placing products without warning of the risks. "It is not admissible for the subrogation of the transferee in place of the transferor to be carried out in a way that allows the transferee to enjoy the advantages that such contracts entail for him, but frees him from the responsibilities contracted by the transferor in the conclusion of such contracts" because such a claim "implies the defrauding of the legitimate rights of banking customers" (STS 339/2019).

The financial system is essential for social and economic stability. It is a system that we all have to look after together. Liability for misleading prospectus and bank resolution are essential parts of this system. Excluding liability for a misleading prospectus in the event of a resolution of the issuing bank undermines the confidence of investors in the securities market. Who is going to invest in the capital increase of a bank knowing that liability for a misleading prospectus is excluded in the event of resolution? Let us hope that the CJEU departs from the conclusions of Advocate General Jean Richard de la Tour and confirms in its ruling on the preliminary ruling that Banco Santander has to face the condemnations for misleading prospectus in the last capital increase of Banco Popular.

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