



Introduction

On 14 January 2022, the Reserve Bank of India (RBI) issued a Discussion Paper (DP), proposing revisions to the existing norms governing the classification, valuation, and operation of investment portfolios held by commercial banks. After a period of considering the feedback on the DP, the RBI has now taken the next step by issuing the Master Direction - Classification, Valuation and Operation of Investment Portfolio of Commercial Banks (Directions), 2023, which was officially released on 12 September 2023. These new directions mark a significant development in how commercial banks manage and account for their investment portfolios, following a thorough consideration of stakeholder input.

These highlights provide an overview of the key expectations outlined in the RBI's directions regarding the classification, valuation, and operation of investment portfolios for commercial banks. These guidelines are designed to enhance transparency and consistency.

Synopsis

- Classification norms:** The directions introduce new criteria for classifying investments held by banks and also provide clearer guidelines for categorising various types of investments.
 - E.g.: The introduction of a category for Fair Value Through P&L (FVTPL) and Held for Trading (HFT) shall be a separate investment sub-category within FVTPL and the ceiling criteria for holding HFT investments for a 90-day period is removed.
 - Separate classification norms for subsidiaries, joint ventures, and associates.
- Valuation guidelines:** The RBI has included fair valuation requirements along with accounting treatment for gain/loss ensuring that investment portfolios are assessed accurately, reflecting their current market values.
 - E.g.: All investments now shall be measured at fair value on initial recognition. Fair value measurement of investments is based on a hierarchy of Level 1, Level 2, and Level 3 inputs.
- Accounting guidelines:** The RBI has incorporated comprehensive guidelines for accounting treatment across various scenarios, encompassing aspects like initial recognition, subsequent measurement, and re-classification. These guidelines have been introduced to address ambiguities and bring uniformity throughout the banking industry.
 - E.g.: Where the securities are quoted or the fair value can be determined based on market observable inputs any Day 1 gain/loss shall be recognised in the Profit and Loss Account but any Day 1 gains arising from Level 3 investments shall be deferred and any Day 1 loss arising from Level 3 investments shall be recognised immediately.
- Transition provisions:** RBI has defined a transition period during which banks are expected to align their operations with the updated norms to facilitate a smooth transition to these new directions.
 - E.g.: These directions are applicable from 1 April 2024 and at the time of transition reclassify investments as on 31 March 2024 as per new directions. Further, these directions guide accounting impacts at the transition date and creation of various new reserves like AFS-Reserve and transfer of balances from the Investment Reserve Account.
- Reporting requirements:** The RBI has introduced extensive reporting requirements, enabling better oversight and monitoring of commercial banks' investment activities. This aims to improve regulatory compliance and transparency.
 - E.g.: The introduction of new disclosure requirements based on the inclusion of disclosure of fair value by category, fair value by a hierarchy of valuation basis (Levels 1,2 and 3), and carrying value of investments
- Regulatory supervision:** The RBI has introduced additional supervision on the investment portfolio of the bank and the bank's compliance with these Directions.
 - E.g.: Implementation of these directions shall be reviewed under the supervisory process and any non-compliance in this regard shall be dealt with appropriately by the RBI.
 - Banks shall not reclassify investments between categories without the approval of their Board of Directors and prior approval of the Department of Supervision (DoS), RBI.
- Investment policy framework:** The directions outline a comprehensive investment policy framework which includes guidelines on risk management, reporting requirements, etc.

Gear up Activities

Banks gear up, inter alia, to evaluate and assess:

- Impact on the business model, financials, capital, ratios, taxation, disclosures
- Impact due to elimination of reclassification option
- Portfolio and its optimal composition considering various scenarios in compliance with these Directions
- Impact on transition
- Technology enhancements
- Changes to policies and processes across the departments

This document is prepared to provide an overview of these Directions and is not intended to be an exhaustive list. If you require a more in-depth understanding or have any questions, please do not hesitate to contact us for further clarification.

Deloitte refers to one or more of Deloitte Touche Tohmatsu Limited, a UK private company limited by guarantee ("DTTL"), its network of member firms, and their related entities. DTTL and each of its member firms are legally separate and independent entities. DTTL (also referred to as "Deloitte Global") does not provide services to clients. Please see www.deloitte.com/about for a more detailed description of DTTL and its member firms.

This material is prepared by Deloitte Touche Tohmatsu India LLP (DTTILLP). This material (including any information contained in it) is intended to provide general information on a particular subject(s) and is not an exhaustive treatment of such subject(s) or a substitute to obtaining professional services or advice. This material may contain information sourced from publicly available information or other third party sources. DTTILLP does not independently verify any such sources and is not responsible for any loss whatsoever caused due to reliance placed on information sourced from such sources. None of DTTILLP, Deloitte Touche Tohmatsu Limited, its member firms, or their related entities (collectively, the "Deloitte Network") is, by means of this material, rendering any kind of investment, legal or other professional advice or services. You should seek specific advice of the relevant professional(s) for these kind of services. This material or information is not intended to be relied upon as the sole basis for any decision which may affect you or your business. Before making any decision or taking any action that might affect your personal finances or business, you should consult a qualified professional adviser.

No entity in the Deloitte Network shall be responsible for any loss whatsoever sustained by any person or entity by reason of access to, use of or reliance on, this material. By using this material or any information contained in it, the user accepts this entire notice and terms of use.

© 2023 Deloitte Touche Tohmatsu India LLP. Member of Deloitte Touche Tohmatsu Limited