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EARN HANDSOME RETURNS AND SAVE TAX TOO!

The maiden budget of the new government has brought a lot of cheer to the common man. The budget delivered twin benefits - deduction limit for investments under Section 80C was increased from Rs.100,000/- to Rs.150,000/- and nil slab for taxable income to Rs.250,000/-.

We are in the middle of a new financial year - a time when most of us ought to consider tax saving investments. Most of us defer our tax saving investments till the last few months of the financial year - for example, in case of salaried employees till they receive a reminder from the HR department (usually in the month of January) for submission of proofs of tax saving instruments,or in the case of a self – employed his/ her Chartered Accountant (CA) reminds one about tax-planning for the financial year. Some of us rush at the eleventh hour and start looking at the investments sometimes as late as the month of March! However, this is merely a 'tax-saving' exercise and cannot be called 'tax planning'. Tax-planning is all about planning in advance, which involves evaluating your overall tax strategy and implementing it before the yearend. This way, you can make the most of the tax-saving opportunities, which will help you accumulate wealth over the long-term. Tax planning is an essential part of financial planning and you should devote enough time and effort for the same.

Investments in tax saving instruments should command the same well-researched and careful approach that other investments do. After all, it is one's hard earned money. The best time to start thinking about tax planning is now. Starting now will give you ample time to draw up a financial plan, research about the best tax saving investments and allocate resources between them in alignment with one's financial goals.

Importance of starting/ planning early

There are several advantages of starting early in the year:

- You can make better choices and right investment decisions
- You can save tax more efficiently and capitalize on investment returns
- You avoid the last minute paper work and mistakes
- You can eliminate the circumstance where you could end up having not enough money to spare for a lump sum investment

The best approach to tax planning is to invest throughout the year in stages, such that by the end of the year you have taken advantage of most of the tax saving opportunities. The strategy of investing throughout the year in a staggered manner will not put liquidity pressure at the end of the year.

Section 80C and some options eligible under this Section

Section 80C of the Income Tax Act, 1961 provides that investors (Individuals & HUF) will be able to claim a deduction upto Rs. 150,000 p.a. from their taxable income if they invest in eligible investments like Public Provident Fund (PPF), National Savings Certificate (NSC) & Equity Linked Savings Scheme (ELSS).

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Illustration of eligible tax saving options under Section 80C of the Income Tax Act, 1961				
		PPF	**NSC**	**ELSS**
Tenure (years)		15	6	Unrestricted
Lock-in (years)		15; Partial withdrawal of 50% after 6 years	6	3
Investment	Minimum	500	100	500
	Maximum	1,50,000	Unlimited	Unlimited
Returns*		8.7% (compounded annually)	8.6%-8.9% (compounded half-yearly)	Market linked; not assured
Risk		Low	Low	Market linked
Taxation		Tax Free	Taxable	Dividend & capital gains are tax free

The power of ELSS: What makes it special?

ELSS derives its power from being market-linked. Income from tax saving instruments other than ELSS is fixed on an annual basis. PPF interest rate is dependent on the average bond yield of the previous year while the interest rate on NSC is decided by the government.
Here is where ELSS is unique. It gives an investor the prospect of earning returns linked to equity markets. This is what makes ELSS exclusive among all tax saving instruments.

Some of the benefits of ELSS are as follows:-

1) Opportunity to grow with equity markets:

ELSS is a tax saving instrument eligible under Section 80C which invests money in equity markets. The average WPI inflation in India has been 5.9% while the average annualized return of CNX Nifty has been 18%, for the past 18 years. This makes ELSS a suitable instrument to fight the menace of inflation.

2) Lowest lock-in period among all tax saving instruments:

ELSS has a lock-in period of 3 years, the lowest among the currently available tax saving options. ELSS is not constrained by limitations either in terms of amount of withdrawal or its frequency. It allows investors to withdraw their investments after 3 years giving investors higher liquidity.

3) Tax free returns:

Additionally, ELSS being an equity oriented fund, long term capital gains are also tax free in the hands of the investor. Dividends paid out are tax free under Section 10(35) of the Income Tax Act, 1961.

4) Facility to regularly invest through Systematic Investment Plan(SIP):

Mutual funds provide the SIP facility to regularly invest in an ELSS product. This brings a discipline in investing and removes the hassle of timing the market.

Illustration:
If one invested a sum of Rs.70,000/- every March on an annual basis in one of the best performing ELSS schemes since March'1996, he/ she would have invested a sum of Rs 13,30,000 till March 2014. Its present value as on September 1, 2014 would be around Rs 1.60 crore. If one had invested the same amount annually in PPF, the value would have been Rs 32.04 lakhs.That is the power of market return in a scheme like ELSS!

Conclusion

Overall, ELSS is a good investment vehicle to save tax as well as to grow your investments over the long term. You could reap better returns from appreciation in equity markets over the long term. You can also choose the SIP route to avoid the ups and downs of markets. If you really want to reap the rewards of your tax saving investments, think beyond the lock-in period of three years. Over the long-term, returns from equities have always been greater than any other investment. So what are you waiting for? Drive your money in the ELSS vehicle to save tax as well as create wealth over the long term.

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