# Align tax-saving investments with your financial targets

## Take care of insurance needs first, then turn to investment instruments; avoid combination products

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Investing for tax-saving should ideally begin at the start of the financial year. But if you have not done so, begin immediately to avoid pressure on your cash flows in the final month of the year.

Starting now means you can make well-considered investment decisions. When taxpayers act in haste, they invest in poorly chosen tax-saving products.

Employers ask employees to declare the tax-saving investments they intend to make in April-May. In December-January, they ask for proof of those investments. If you don't submit them, the employer will deduct tax at a higher rate. "This results in a double whammy. Not only will the salary you get in the final months be lower, you will also have to make tax-related investments from that reduced amount," says Arvind A Rao, certified financial planner and founder, Arvind Rao & Associates.

### Do you need to invest?

Many expenditures and payments you already incur are eligible for Section 80C tax deduction, including children's tuition fee, home loan principal repayment, and insurance premiums. Employees' Provident Fund (EPF) contributions of employees are also eligible for Section 80C benefit.

Only if these don't suffice to meet your Section 80C limit of ₹1.5 lakh should you make additional tax-saving investments.

### Synchronise with financial goals

Investors must have clearly defined financial goals and then align their tax-saving investments with them. "If your goal is retirement planning, invest in a long-term instrument like the Public Provident Fund (PPF). But if you have a medium-term goal, you could invest in a five-year tax saver fixed deposit or an equity-linked savings scheme (ELSS)," says Vishal Dhawan, chief financial planner, Plan Ahead Wealth Advisers.

Your tax-saving investment should also be in sync with your asset allocation. "If your portfolio is already tilted in favour of fixed-income instruments, invest more in equity-oriented ones, and vice versa," says Deepesh Raghaw, founder, PersonalFinancePlan, a Securities and Exchange Board of India -registered investment advisor.

Preeti Khurana, director of advocacy and regulation, Clear suggests paying heed to one's risk profile and time horizon also when selecting tax-saving instruments.

### Buy adequate cover

First ensure that your family is financially protected. "Buy adequate term insurance if your family is dependent on your income," says Dhawan. The premium is eligible for Section 80C deduction.

Next, buy adequate health insurance and get tax deduction under Section 80D.

### Investment products you may opt for

■ **PPF:** It offers risk free and tax-free return of 7.1 per cent annually. It comes with a long lock-in. Its only downside is that one can't invest more than ₹1.5 lakh in a year.

■ **ELSS:** It combines equity exposure with tax saving. "Equity is one asset class that can produce inflation-beating returns over the long term," says Dhawan. The lock-in period is the shortest among all tax-saving products.

Since equities tend to be volatile, invest in ELSS with a horizon of five-seven years and by adopting the systematic investment plan (SIP) route.

■ **Voluntary Provident Fund (VPF):** If your EPF contributions don't reach ₹2.5 lakh, contribute more via VPF. The 8.1 per cent risk-free and tax-free return is unmatched on the fixed-income side.

■ **National Pension System (NPS):** Investors can earn a tax deduction of ₹50,000 on NPS under Section 80CCD (1B), over and above the ₹1.5 lakh deduction under Section 80C. "If you belong to a high tax bracket, don't need the money till 60, and if investing in NPS won't crowd out your other investments, then put ₹50,000," says Raghaw.

However, be prepared for the long lock-in. If you withdraw prematurely, 80 per cent of the money will be annuitised.

■ **Demography-specific instruments:** Senior citizens in need of regular cash flows may invest in Senior Citizens Savings Scheme, which offers 7.6 per cent (taxable, quarterly payouts, with Section 80C benefit). For those who have a daughter aged less than 10 years, Sukanya Samriddhi Yojana (7.6 per cent tax-free return with Section 80C benefit) is a good investment.

### Mistakes you should avoid

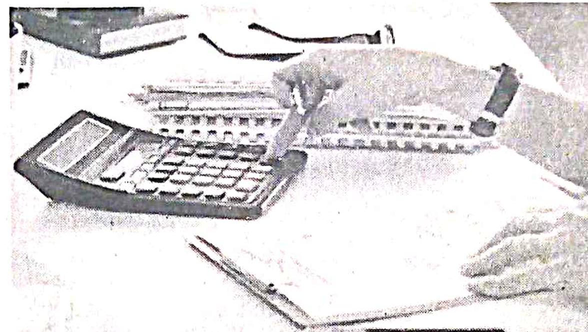
Avoid insurance cum investment plans, especially traditional plans. "You run the risk of remaining underinsured if you invest in them," says Raghaw.

Adds Rao: "These plans' internal rate of return rarely exceeds 5 per cent annually."

A common mistake taxpayers commit, says Khurana, is to not exhaust their Section 80C limit. She adds that taxpayers should also pay heed to the number of years of payment they are committing to, the likely return, the lock-in, and the taxability on maturity.

Pay advance tax on time. "If you have gains from activities in the market or other incomes that are not part of your salary, then deposit advance tax so that you're not faced with a huge tax liability in March," says Khurana. Rao adds that interest on unpaid advance tax can at times wipe out all gains from tax-saving investments.

In Budget 2022, Section 115BBH of the Income-Tax Act was introduced which provided that any income from transfer of a virtual digital asset (such as cryptocurrency) would be taxed at 30 per cent (plus applicable surcharge and cess). "Taxpayers must remember that they can't avail any deduction, set-off any losses, or carry forward losses to subsequent assessment years," says Suresh Surana, founder, RSM India.



### ELSS FUNDS: TAX SAVING WITH HIGH RETURNS

SIP returns (%)

| Taxsaver funds | 1-year | 3-year | 5-year | 10-year |
|---|---|---|---|---|
| Quant Tax | 24.99 | 42.40 | 32.04 | 24.31 |
| Bank of India Tax Advantage | 14.23 | 23.92 | 20.08 | 16.86 |
| IDFC Tax Advantage | 14.34 | 28.86 | 20.18 | 16.86 |
| DSP Tax Saver Fund | 12.81 | 22.42 | 17.87 | 16.17 |
| Canara Robeco Equity Taxsaver | 12.79 | 22.33 | 19.16 | 16.12 |
| Kotak Tax Saver | 16.72 | 22.98 | 18.09 | 15.64 |
| JM Tax Gain | 10.99 | 20.84 | 16.81 | 15.57 |
| Sundaram Tax | 15.01 | 23.54 | 16.81 | 15.18 |
| ICICI Prudential Long Term Equity | 13.31 | 22.09 | 16.65 | 14.50 |
| Axis Long Term Equity | 0.29 | 11.80 | 11.83 | 14.27 |

Returns are for regular, growth plans — Source: Morningstar AWS