Don't Rush Into Tax-Saving Investments

Unplanned, hurried purchases can add to your future monetary burden

Partha Sinha | TNN

Illustration: Ram

As we enter the last three months of the current financial year (FY15), a large number of salaried individuals will rush to meet their tax-saving investment obligations to reduce their annual tax burden. Ideally, one should do tax planning at the start of the year. But a large number of people fail to do so. In their rush to meet the deadline for investing in tax-saving instruments and reduce the tax burden, people often invest in financial products that become monetary burdens for years to come but, on the surface, remain unnoticed to most.

To avoid such a pitfall, financial planners and advisers say that one should plan early and invest throughout the year to save on taxes. "Rather than rushing into buying the first available instrument, it is critical that investors do their tax-planning exercise in a structured manner," says Vishal Dhawan, founder of Plan Ahead Wealth Advisors. "Make your tax-saving strategy an integral part of your overall financial life to help it work for you at its fullest."

Don't invest randomly

They also insist on having a strong purpose behind every investment decision in tax-saving instruments and these should never be made randomly. "The purpose of tax planning is to achieve future goals by planning your finances in a tax-efficient way," says Tarun Birani, founder & CEO, TBNG Capital Advisors. "Tax-efficient financial planning is basically arranging your financial affairs in such a way that you can take full advantage of all the exemptions, deductions, etc, allowed by the government. While investing with an aim to reduce tax liability, one should invest keeping in mind factors like age, risk appetite and tax slab."

Dhawan agrees with this. According to him, for example, younger clients saving for goals that are more than 10 years away — like education for their children, retirement, etc — can use a larger component of equity in their tax-planning portfolios. This is because, according to Dhawan, "equities tend to outperform other asset classes over longer time frames and are also inflation-adjusting. Therefore, ELSS mutual funds could be the preferred instrument for tax saving due to their 100% equity exposure".

Relating to risk appetite, Dhawan says, "If you are extremely uncomfortable with even temporary capital losses in your portfolio, avoid products that have 100% equity exposure. Investors with a balanced risk profile could explore options that have a combination of both stocks and bonds. For instance, pension plans from MFs or insurance companies. Investors with an aggressive risk profile could opt for a full ELSS portfolio for tax planning as well."

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Creating Wealth With Sec 80C's ₹1.5lakh Annual Limit:

Monthly Investment (in ₹)	Investment Period (in years)	Expected Annual Return (in %)	Investment Corpus (in ₹)
12,500	10	10	26 lakh
12,500	10	12	29 lakh
12,500	20	10	95 lakh
12,500	20	12	1.24cr
12,500	30	10	2.83cr
12,500	30	12	4.37cr

Source: TBNG Capital Advisors

Look at existing portfolio

One should also consider existing asset allocation while planning for tax-saving investments. "For an individual having a large contribution towards employee provident fund, which is fixed income oriented, it may not be advisable to put more money into a PPF account, whereas a self-employed individual could use PPF as a contribution tool towards retirement to balance business risks," says Dhawan.

Also, one should look for the most suitable alternative, rather than buying what everyone else buys. "Be sure to understand all the alternatives available to save taxes. For example, a couple of mutual funds offer pension plans that have a mix of bonds and stocks and are, hence, less volatile. They also offer the advantage of allowing one-time contributions unlike many of the pension plans from insurance companies that require payments regularly," says Dhawan.

According to Birani, careful planning and discipline in investments with proper asset allocation can help build long-term wealth on tax-saving investments. "For instance, a monthly investment of Rs 12,500 (aggregating to the Rs 1.5 lakh annual investment limit under section 80C) over 30 years and generating an annual return of 12%, can help create a Rs 4-crore corpus," says Birani (Look at table *Plan Early To Earn More*).