Earning Less Than 10L? Use Rajiv Gandhi Scheme to Save More Tax

Rajiv Gandhi Equity Scheme offers tax benefits over & above the . 1 lakh under Sec 80C, investors with an appetite for equities can invest in this scheme , says Prashant Mahesh

Some investors are taking a close look at the Rajiv Gandhi Equity Savings Scheme (RGESS) this tax-saving season. Taxpayers with gross annual income of . 10 lakh or less can invest up to . 50,000 under Section 80CCG in the scheme. The benefit is available to first-time investors for investments through their demat accounts opened on or after November 23, 2012, or demat accounts which have not yet been used for equity investments.

RGESS offers tax benefits over and above that one gets under Section 80C of the I-T Act which is available for savings or investments up to . 1 lakh. “Since this scheme gives you an added tax benefit, investors with an appetite for equities and keen to build an equity portfolio for the long-term can invest in this scheme,” says Vishal Dhawan, chief financial planner at Plan Ahead Wealth Advisors.

As per the provisions of the scheme, you can invest in direct equities (any stock belonging to BSE 100 or NSE CNX 100, equity shares of Maharatnas or Navratnas) or you can buy units of exchange traded funds (ETFs) investing in RGESS-eligible shares provided these units are listed and traded on stock exchanges and settled through the depository mechanism.

“Investments in individual stocks carry higher risk as compared to investments in equity mutual funds. We recommend first-time investors to invest through the mutual fund route,” says Aseem Dhru, MD & CEO, HDFC Securities.

PREFER MUTUAL FUNDS TO DIRECT EQUITIES

Many investment advisors have reservations about individuals investing directly in stocks under RGESS. “It is very difficult for the retail investors to predict individual stock price and how they will behave,” says S Shankar, chief financial planner at Credo Capital. Take the example of a couple of Nifty stocks. In 2012, IDFC gained 87% while BPCL lost 25%. So if you buy a wrong stock, you could end up losing a lot of money. As compared to this, a mutual fund invests in a basket of stocks thereby lowering the risk.

“Equity mutual funds offer the benefits of diversification which helps lower risk and optimise return,” says S Shankar. He advises investors to invest in RGESS by using the ETF route.

THE TAX BENEFITS

As per RGESS, if you invest . 50,000, you shall get a 50% deduction of . 25,000 under this scheme. Now if your income is taxed at 10%, you save tax of . 2,500; if you are in the 20% tax bracket, you will save . 5,000. In case you were to buy stocks under this scheme, keep in mind the brokerage costs that you may have to shell out in addition to the annual depository maintenance costs. For example, if you buy shares worth . 50,000, you shall pay a brokerage of . 250 and an STT (Securities Transaction Tax) of another 0.1%, or . 50. Keep these costs in mind before investing. As of now, if you happen to miss this scheme, there is no clarity as to whether this scheme will be extended to the next financial year.

THE PROCESS

All those looking to invest in RGESS, need to open a demat account with a depository participant and a broking account with a recognised member of a stock exchange. The depository will certify your ‘new investor’ status at the time of designating your account as a demat RGESS account. Once this is done you can buy stocks from BSE 100, NSE CNX 100, Maharatnas or Navratnas or exchange traded funds (ETFs) as specified under the scheme. An investor can invest in RGESS securities/ ETFs as many times as he wants in the first year of investment.

However, tax benefits are allowed only in the first year of RGESS investment. Even if one claims a small amount in deduction in first year, no deductions can be claimed in subsequent years.

The investment made under RGESS is locked in for a total period of three years. However, as per the terms of the scheme, only the first year is a fixed lock-in. In the subsequent two years, the investment is subject to a flexible lock-in. During this flexible lock-in period, the investor has a freedom to book profit or alter the securities in her/his portfolio provided the value of the securities in the demat account is maintained or is equal to the amount declared as investment under RGESS in the first year. You will lose tax benefits availed under Section 80CCG of the I-T Act if you fail to comply with the lock-in requirements.

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