Does it make sense to invest in a 10-year closed-ended ELSS?

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Several mutual fund houses have recently launched 10-year closed-ended Equity Linked Saving Schemes. ICICI Prudential Mutual Fund has launched ICICI Prudential Long-term Wealth Enhancement Plan, BOI AXA Mutual Fund has launched its first series of BOI AXA Midcap Tax Fund- Series 1, and UTI has also launched its sixth series of its UTI Long Term Advantage Fund. While the fund houses believe that a 10-year closed ended fund is a good long-term wealth solution, mutual fund advisors frown upon these schemes.

“The selling point of ELSSs against other tax-saving instruments is their shorter lock-in period. Not saying that investors should redeem the scheme after three years, but having an option to do so is an advantage,” says Vishal Dhawan, Founder, Plan Ahead Wealth Advisors.

ELSS or tax saving mutual fund schemes have a mandatory lock-in period of three years. Other investments permitted under Section 80C of the Income Tax Act have much longer lock-in period. For example, Public Provident Fund (PPF) is a 15-year product. Though investors can make partial withdrawals from the seventh year.

Mutual fund advisors have always stressed on the importance of long-term investment in equity mutual funds and ELSS was no exception. But these advisors believe that curtailing liquidity is no way of encouraging long-term investments. “An investor might need the money in urgency. Moreover, what if the fund fails to perform? We can’t take such risks on our money," says Suresh Sadagopan, Founder, Ladder7 Financial Advisories.

However, these schemes allow investors to sell their investments on the stock exchange after the completion of the mandatory lock-in period. Some mutual fund houses are also facilitating repurchase of units after the lock-in period. But both these routes may not fetch the best price to investors.“In the case of selling the units on the exchange, it is difficult to find buyers. Even if you find the buyer, you will have to sell your units on discounts,” says Suresh Sadagopan. “In the case of repurchases, some fund houses say that they will buy the units back, but there is a possibility of you having to sell them at discounted rates which beats the purpose of long –term investments,” Sadagopan adds.

“In my view, investors should invest in existing open-ended ELSSs with a good track record. If you are getting the tax-benefits from a scheme which has a good track record with an advantage of liquidity, it is a better choice,” says Vishal Dhawan.