TAX PLANNING

Savings get joyous boost

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THE CHANGE in the personal tax slabs has given tax payers upto Rs 50,000 of incremental savings. The joy on hearing these words post the finance minister's speech was evident. From a "Holi bonus" to "let's party" to "a boost for consumption", all the early reactions that I heard seemed to indicate that this change called for a celebration. Obviously, celebrations call for spending and it made me wonder, "Was this change in the tax slabs by the FM given to boost spending or increase savings or absorb the burden of increased consumer inflation?" The financial planner in me firmly believes that this change was driven by a combination of a decreased savings rate last year, and as a shield for inflation that looks like it is going to continue to challenge household Budgets in the near and medium term.

In order to approach the changes in the Budget at a personal finance level, you can invest an additional amount of Rs 20,000 in long-term infrastructure bonds under a new section 80CCF and get a tax deduction on the same. This deduction would be available over and above the Rs 1 lakh deduction that you get under section 80C.

Keep your ears open on the issuance of these new long-term infrastructure bonds, as these will be notified by the Central government soon. The FM has announced that the new direct tax code will come into effect from April 1, 2011 — This could entail a dramatic change in tax slabs, removal of exemption on gains from equities, and changes in tax saving vehicles and limits, as compared to how they stand today. One should also begin a Systematic Investment Plan (SIP) in a good quality mutual fund for the amount of tax saved.

For example, if you earn Rs 10 lakhs a year, start a fresh SIP for Rs 4,000 per month from April 1, to effectively invest the tax savings generated. Please note that this amount should be over and above any SIPs that you are already running. The choice of whether the mutual fund should be in equities or bonds or a combination of both would be driven by your overall financial plan and asset allocation strategy. Alternatively, prepay your loans to the extent of tax saved — for example, if you earn Rs 5 lakhs per year and have savings of Rs 30,000 because of the changes,you should prepay your loan to the extent of Rs 30,000. In case you have multiple loans, prepay the most expensive loan first.

Beware of your floating rate loans. With food inflation continuing to be a matter of concern, and fuel hikes likely to result in a further impact on inflation, it is only a matter of time before interest rates are raised further, as a result of which your floating rate loan gets readjusted upwards.

> **At a personal finance level, you can invest an additional amount of Rs 20,000 in long term infrastructure bonds under a new section 80CCF and get a tax deduction on the same. Further begin a Systematic Investment Plan (SIP) in a good quality mutual fund for the amount of tax saved.**

The author is a financial planner