All you need to know about systematic transfer plans

By Satya Sontanam 02 Mar 2022, 06:06 am

Withdrawal from debt scheme before 3 years will be considered as STCG and will be taxed at income tax slab rate

Are you planning to take advantage of the market correction by increasing your equity exposure? If you are a mutual fund investor, one of the ways of doing it is initiating a systematic transfer plan (STP) from a debt fund to an equity fund.

STPs allow you to transfer money to a select scheme (target scheme) periodically from another scheme (source scheme) in the same fund house.

This way, you don't have to worry about timing the market as your investments to the equity fund will be staggered over a period of time.

STPs come in handy when you have a lump sum amount but do not want to invest the entire money in equity at once. You can consider investing it in a liquid fund and initiate an STP to an equity fund. You will also get the benefit of rupee cost averaging, which helps in buying more units when the market is low and lesser units when the market is high.

Further, say, if you want to withdraw money from an equity fund in a one-year time, you can opt for STP from an equity fund to a debt fund.

Types of STPs

STPs generally come in two forms – fixed STP and variable STP. In a fixed STP, a fixed amount or number of units will be transferred from the source scheme to the target scheme at pre-defined intervals. In the case of a variable STP or a Flexi STP, the amount increases or decreases depending on the market conditions.

For example, under ICICI Pru MF's Booster STP, the installment amount can vary from 0.1 times to 5 times the base installment amount according to the equity valuation index, which is a proprietary model of the firm. If you have already enrolled in Booster STP of ICICI Mutual Fund, note that the fund house has recently changed the installment multiples effective from 28 February.

Some fund houses such as HDFC Mutual Fund and Kotak Mutual Fund also provide capital appreciation STP, wherein the profit made on the investment in the source fund will be transferred to the target scheme.

These STP forms can be submitted online, at the branch office of the mutual fund, or the authorized collection centers. Note that not all third-party aggregators such as Paytm Money may provide STP options in its app.

Points to note

Every STP transfer is considered a redemption from the source fund and reinvestment in the target fund. The redemption of mutual fund units from a source fund attracts capital gains tax in the hands of an investor. Withdrawal from a debt scheme before three years will be considered as a short-term capital gain and will be taxed at your income tax slab rate. The long-term capital gains on debt funds are taxed at a flat rate of 20% after indexation. In the case of equity funds, the short-term capital gains realized on redeeming units before one year are taxed at a flat rate of 15%, and the long-term capital gains exceeding ₹1 lakh a year attracts tax at 10%.

Generally, exit loads are also applicable for withdrawals within one year of investment.

The other key point to note in the case of an STP is its duration, as per Vishal Dhawan, founder & CEO, Plan Ahead Wealth Advisors. “If the target fund is a hybrid fund or a large-cap fund, investors can opt for STP for a shorter period (about six months); but if the funds are transferred to a mid-cap or a small-cap, they may choose to go over a long period of time (about 12 months) because of the higher volatility in this space," he added.

When markets correct, investors might get excited to add more to equity. “One should keep the strategic asset allocation between equity and debt in mind before going in for STP," as per Dhawan.

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