Five ways to save your tax

By Gouri Shah | The Established | 01 April, 2022

TRIED AND TESTED INVESTMENTS THAT WILL HELP YOU ANNUALLY WITH INCOME TAX

As the financial year draws to a close, the incessant pings on the tax expert's phone can only mean one thing—clients sliding into the inbox with queries on where to invest and how much to invest so they can fend off the income tax.

While most people frantically rustle through the mixed bag of usual suspects to meet their tax-saving goals before the March 31st deadline, experts suggest using a different strategy this time. One that is better suited to you and doesn't spell panic.

Firstly, pick what is right for you. "Our Income Tax Act has been enacted so beautifully that as long as you follow your financial goals, the tax benefits will follow," says Gaurav Mashruwala, a Mumbai-based certified financial planner and practitioner, and author of Essential Guide to Carefree Retirement. So, whether you pay rent or have taken a housing loan, are paying school fees or a higher education loan, buying life insurance to secure your family's future or saving for your retirement, tax-saving opportunities present themselves at every point.

Most forms of tax-saving investment plans fall under Section 80C of the Income Tax Act, 1961. Investors can claim tax deductions up to a maximum limit of ₹1.5 Lakh. These investments include the Public Provident Fund (PPF), ELSS (Equity Linked Saving Scheme), NPS (National Pension System), Life Insurance, fixed deposits and bonds, among others. Over and above this, there are a few other provisions in the IT Act that allow investors to claim tax deductions for health insurance, interest on home loans, donations to charitable institutions, house rent, etc

Experts recommend five tax-saving avenues for you to choose from.

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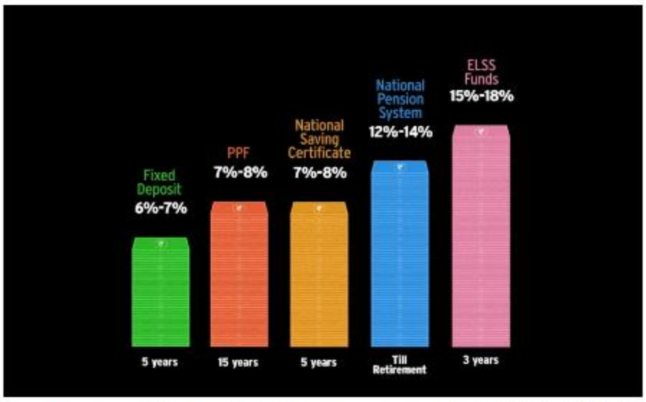

Investors can claim tax deductions up to a maximum limit of ₹1.5 Lakh with such investment plans. Image: AGENC

PUBLIC PROVIDENT FUND

A popular long term investment scheme, PPF is considered the golden child of tax-saving investments in India. Largely because it is one of the few investment products that come with an EEE or Exempt-Exempt-Exempt status. What this means, is that everything—from the contribution you make and the interest you earn on this PPF scheme, to the final maturity amount are all exempt from tax.

The way the financial product is structured, it has a maturity period of 15 years. When the 15 years are completed, this can be further extended in blocks of five years. Unlike insurance schemes where the premium payments can be fairly hefty, this investment product gives you the flexibility to contribute anywhere from ₹500 – ₹1.5 Lakh each year to keep the account going. This contribution can be made in monthly instalments or as a lump sum, depending on your preference.

While the interest rate on the PPF is reset every quarter, it still offers a better interest rate than a bank deposit. Moreover, as a government backed-saving scheme it is also considered a safe investment option. "The downside is that if you can't set aside your money for 15 years, that lock-in period can be fairly long," says Vishal Dhawan, CEO and founder, Plan Ahead Wealth Advisors, a Mumbai-based SEBI licensed, registered investment advisory firm. While loans against investments and early withdrawals are possible, terms and conditions apply.

ELSS (EQUITY-LINKED SAVING SCHEME) MUTUAL

ELSS funds are equity mutual funds that invest in a diversified basket of shares. While this is considered a volatile investment as its performance is linked to the market, the ELSS continues to be a popular tax-saving instrument option for young investors due to the high rate of returns as well as the short lock-in period. “Over longer periods, equity tends to outperform most other asset classes. That is the advantage of the product and the way it is structured,” says Dhawan.

ELSS schemes have a lock-in period of three years before you can redeem them. However, experts advise you to stay invested longer to reap the benefits. Ideally, for a period of five to ten years. There are a couple of ways that you can invest your money in an ELSS. The first, you can invest a lump sum, something that the last-minute tax-saving plan may warrant. Or second, where you go down the SIP (systematic investment plan) or STP (systematic transfer plan) route, which allows you to invest small amounts at regular intervals.

“The second option, of a SIP or STP, is preferred as it allows investors to average out their purchases and allows them to reap the benefit of rupee-cost-averaging, which is very useful when investing in equity,” says Dhawan. However, the downside is that it attracts a long term capital gains tax of per cent on redemption.

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Experts caution against viewing health insurance purely as a tax-saving investment

LIFE INSURANCE

While the main aim of this investment is to provide insurance coverage, the tax-saving benefit is an attractive cherry on top. In this investment option, the premium paid and maturity proceeds towards the policy are tax-free.
To start with, evaluate how much life insurance you actually need. The value should be based on your family structure, dependency on your income, expenses and financial goals. This will become the basis for how much insurance cover you need, which will in turn determine the premium.

Experts state that the most important thing to keep in mind is that life insurance policies warrant a long-term financial commitment. “So, unlike the ELSS, where you can make only a one-time payment or a PPF where you can keep your account going by contributing just ₹500 each year, with an insurance policy you’re committing to a much longer time frame in terms of making the payments. So the decision has to be carefully thought through,” says Dhawan, who adds that it is ideal to buy term insurance rather than endowment, ULIPS (Unit Linked Insurance Plans) or money-back policies. “It is best to keep your investments and insurance separate from each other,” he advises.

HEALTH INSURANCE

This investment is a no-brainer. It falls under Section 80D of the Income Tax Act. Not only does this investment offer you additional tax saving benefits over and above the ₹1.5 lakh tax-saving investment cap under Section 80C, but is also considered a critical tool to shield you from unexpected medical expenses. Investors can claim ₹25,000 in tax benefits under this section for payments towards health insurance premiums for their family and includes a ₹5000 tax-benefit for preventive health checkups. That amount goes up to ₹50,000 if the contributions include health insurance payments for senior citizen parents.

However, experts caution against viewing health insurance purely as a tax-saving investment. “Most people are driven by the tax benefit. However, it would be more prudent to work backwards and figure out how much medical coverage you actually need depending on which city you live in, and which hospital you would prefer to go to should the need arise," says Dhawan.

Provisions in the IT Act allow investors to claim tax deductions for interest on home loans, donations to charitable institutions etc. Image: Pexels


Keep in mind that life insurance policies warrant a long-term financial commitment. Image: Pexels

NATIONAL PENSION SYSTEM

In the absence of a social security system in India, the NPS becomes a good and preferred tool for people to save in a dedicated manner towards their retirements. The benefits that come with picking the NPS are multifold.

"To begin with, there are multiple managers within the NPS that you can choose from. Then, there is the advantage of choosing your mix of assets—you can decide how much to go to equity, corporate bonds, government securities or alternate assets. Alternately, there is an auto life cycle option, where depending on your age the mix of assets automatically changes. So as you get older the equity reduces," says Dhawan.

This contribution, up to a maximum amount of ₹1.5 Lakhs, can be claimed for tax exemption under Section 80C of the Income Tax Act. Investors can also get an additional benefit of ₹50,000 under Section 80CCD (1b). Making it a popular choice for investors. However, it cannot be withdrawn before retirement except in specific situations.

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