HDFC MF - *INVESTING ESSENTIALS*

LEARNING FOR THE SMART INVESTOR

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The need for Tax Planning

Benjamin Franklin once famously said, "In this world nothing can be certain except death and taxes". In today's times, these golden words cannot be truer, as taxes can play a crucial role in the investment journey of a young investor.

Taxes can eat into your annual earnings, and usually, the higher are your earnings, the bigger is your tax bill. So much so, that improper tax planning can possibly be the difference between meeting and failing to meet our investment objectives. And that is why, tax planning should form a focal part of our financial planning. It is a legitimate way of reducing your tax liability for a financial year by utilizing various available exemptions, deductions and benefits offered by tax authorities.

The Income Tax Act, 1961, offers several such exemptions (such as those under section 10) and deductions (such as those under Chapter VI-A). The most popular deduction among most tax-payers is the one provided under section 80C, where several investments/expenditures such as life insurance premium, deposits in Public Provident Fund, principal repayment on housing loan, National Saving Certificates, etc., are covered. However, when it comes to wealth creation, one investment avenue covered under section 80C is the Equity Linked Savings Scheme (ELSS).

An ELSS is a mutual fund investment that qualifies for a deduction from the gross total income of individuals/HUFs up to Rs. 1,50,000, along with other prescribed investments under section 80C of the Income Tax Act, 1961. It invests a large proportion of its corpus in equity and equity related instruments, enabling investors to participate in the growth journey of businesses, and thereby being able to generate wealth in the long run.

Since an ELSS invests predominantly in equities, it offers investors a higher potential return, albeit at a higher risk. It comes with a 3 year lock-in period, which is the least among all tax-saving options under Section 80C. The lock-in period prevents investors from getting swayed by the ups and downs of the markets, and helps them tide over the volatility which inherently comes with equities as an asset class.

To conclude, the importance of tax planning should never be understated. Paying taxes is an important way to contribute to the nation's development, but when the authorities themselves have provided us various opportunities to reduce our tax bill in a legitimate manner, it is only smart to do so.