HDFC MF Weekend Bytes

(A weekly article series from HDFC Mutual Fund)

Why it's time to start tax planning for 2022-23

Did you rush towards the end of March deadline for investing in instruments eligible for tax deduction under Section 80C? Were you relieved that you won't have to think about taxes for a few months now? So, why are we talking about taxes already? As Confucius said - A man who does not plan long ahead will find trouble at his door, if you don't plan your taxes when you have the time, you will be left scrambling at the last minute. You will try to invest in eligible instruments under Section 80C in haste or invest in unfavourable products simply because of lack of time to analyse among the options. This delay in financial planning could prove costly. It may lead you to miss good opportunities to invest correctly. Not to mention the additional stress.

Here are some tips on how you can plan your taxes early every year to get optimum benefits from your investments, reduce your tax liability and be on the path to achieving your financial goals.

Start planning in April

The beginning of the financial year is a good time to assess your total annual income and estimate your taxes. Several tax planning tools are available to help you do this, or you can follow the advice of your financial planner. If you are a freelancer or a self-employed professional, you may not know the exact amount of your total income for the year. In this case, you can work with an estimated figure.

Plan your investments

Use the time to research and decide the various tax-saving instruments you will invest in and the amount to invest in each. It is prudent to invest through instalments to gain the advantages of rupee cost averaging and avoid liquidity issues. Section 80C allows taxpayers a maximum deduction of ₹1,50,000 per annum from their total income. Let's assume, after contributing to the Employee Provident Fund, if a salaried person is left with, say, ₹96,000 to invest in a financial year (assuming Rs. 54,000 is the year's EPFO contribution, and Rs.96, 000 is left for tax planning out of the Rs.1,50,000 for the year), he/ she can start a SIP of ₹8,000 for 12 months in an Equity Linked Savings Scheme (ELSS).

ELSS is an equity-oriented mutual fund that invests a minimum of 80% of the total corpus in equity and equity-related instruments. Investments in ELSS have a mandatory lock-in of 3 years and are eligible for deduction under Section 80C of the Income Tax Act.

Some of the benefits of an SIP into ELSS include:

- Investment in a diversified basket of equity stocks in a staggered manner to take care of the highs and lows of the equity market
- Potential for wealth creation through investment in equity
- Disciplined savings every month
- Tax planning without losing sleep over it towards the end of the year

Organise your investment portfolio

While making investments to achieve optimal tax planning, manage your asset allocation to avoid disrupting your financial goals. Fine tune your investments based on your financial health. For example, if you're expecting a salary hike, you can increase your investments to balance the tax increase. If you have exhausted the deduction limits, look for alternate instruments you can invest in that will help you achieve your financial goals. All of this is possible only if you start planning early.

Unplanned and lumpsum investments earn returns too, but postponing tax planning for the end of the year, may result in missing out of deadlines due to possible liquidity crunch and suboptimal tax planning. Well-planned investments throughout the year help you avoid end-moment stress, allow you to earn returns for a longer period and lower your tax liability.
