



Equity Linked Saving Schemes as Tax saving Investment for Salaried Class

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ABSTRACT

The recent fall in the interest rate on savings bank and other deposits have been responsible for diverting the investment towards other schemes. In addition to this, Income Tax benefits are also important for salaried class, pensioners and other income tax payers. This study will focus on various schemes of ELSS (Equity Linked Saving Schemes). In the present economic scenario and globalisation process, investment in equity has gained importance and as such it will be useful to critically examine the schemes under ELSS.

KEYWORDS

ELSS (Equity Linked Saving Schemes), Investments, Tax Saving.

INTRODUCTION

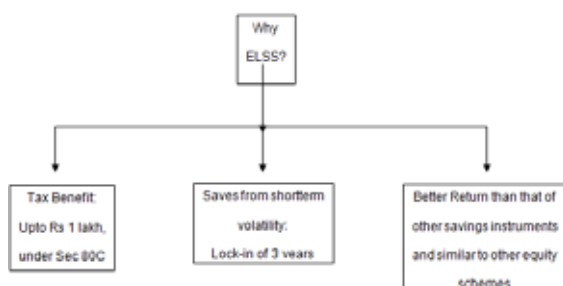
Equity Linked Saving Scheme- Gearing you up for the future:

The common retort to the oft-asked question by anxious investors, of the best way to save tax, is to invest in Post Office savings schemes, or perhaps a regular investment in a public provident fund, or to buy insurance policies. It is unfortunate that the greatly advantageous Equity Linked Savings Scheme (ELSS) is hardly ever mentioned, which is not a surprise, since, even though it is one of the high yielding products, it remains one of the lesser known ones. That is another reason that investors do not yet comprehend the potential benefits of this product.

ELSS holds the advantage of being the only equity-based tax saving instrument available in the country today and offers tax deduction on investments up to Rs1,00,000, under Section 80C of the Income-Tax Act. Experts are of the opinion that equities, proven time and again to be the best asset class in the long term, would continue to beat inflation over the next few years, considering the strong growth rate in the economy and a healthy rise in corporate earnings. It would be prudent for long-term investors to invest in an asset that will do just that. We have elucidated the nature of an ELSS, which rightly deserves its due.

Meaning of ELSS

Equity Linked Savings Schemes (ELSSs) are similar to the normal equity diversified schemes that invest across the board and market segments. Features that differentiate ELSS from an open-ended equity diversified scheme are tax saving benefit (deductions under Sec 80C) and a lock-in period of three years, which are explained hereunder. Also, one can invest in these schemes in small amounts through a Systematic Investment Plan (see last issue for details) and begin with a small fund size to add to this expense (i.e. entry/exit load) of investing in an ELSS is similar to any other equity scheme



Tax Benefit :

Until FY05, Sec 88 of the Income Tax Act had fixed an overall ceiling of Rs 1,00,000 for investments in the tax saving instruments, including a cap of Rs 10,000 for investment in ELSS. The investors would get a rebate based on his taxable income. However, investments upto Rs 1,00,000 are eligible for deduction from Gross Taxable Income and the ceiling on investments in ELSS is removed. This investment is deducted from the Gross Total Income, hence reducing the taxable income.

METHODOLOGY

The following paragraphs deal with the methodology of the study.

Objectives of the study :

Any scientific study required proper and scientific approach. For this purpose it is necessary to set certain targets to achieve desired results. Given below were the objectives of the study :

1. To analyse the Indian conditions with respect to equity investment under ELSS.
2. To examine various financial aspects of ELSS.
3. To analyse schemewise benefits under ELSS for tax savings.
4. To study the position of equity market.
5. To evaluate the performance of various schemes under ELSS.

SCOPE OF THE STUDY

This study is limited to equity linked saving schemes as applicable to saving of income tax. The geographical limitation is various salaried income group people in Nagpur District.

HYPOTHESES

1. The schemes under ELSS are useful for income tax purpose.
2. Pensioners are mostly benefited by ELSS.
3. Salaried Class can invest to save income tax.
 - A) Universe of study will be Nagpur District..
 - B) Sampling – Primary Data was collected from Salaried Class, Pensioners and other income tax payers from Nagpur District.
 - C) Sampling Frame – The sample size of the respondents was prepared according to the following table

S.No.	Type of Respondent	No.
1.	Salaried Class,	200
2.	Pensioners	100
3.	Other income tax payers	200
4.	Total	500

D) Data collection –

Primary & Secondary data was collected from various sources. Primary data was collected by canvassing questionnaire to the Salaried Class, Pensioners and other income tax payers.

The Secondary data was collected from Reports and other authentic materials available at different offices, articles published in Newspapers, Magazines etc.

DATA INTERPETATION TOOLS

The most often tools used to Examine are SPSS

- Percentage.

RESEARCH FINDINGS

Equity Linked Saving Schemes (ELSS) provide a good avenue for capital appreciation and tax benefit under section 80C of the Income-Tax Act, 1961.

Benefits of ELSS**Tax Benefits**

- Deduction under section 80C
- No tax on Capital gains
- Dividends are tax free in the hands of investor

Lock in period (3 years)

- Lowest among all tax saving instruments under section 80C
- Long enough to minimize market volatility

Better Return

- Compared to all tax saving instruments under sec 80C

Comparison of ELSS with other tax saving instruments					
Particulars	PPF	NSC	ELSS	Bank Deposits	ULIP
Tenure (Years)	15	6	3	5	5
Min. investment (Rs)	500	100	500	10,000	10,000#
Max. Investment (Rs) for sec 80C benefits	70,000	1,00,000	1,00,000	1,00,000	1,00,000
Return (CAGR)	8.00	8.00	32.25^	8.25*	NA

* Source : ICICI Bank # As annual premium ^ Avg Return of top five ELSS schemes, source :Value Research

Top Schemes as per Value Research

Scheme	1 Year Return (%)	3 Years Return# (%)	Rating*
HDFC Tax Saver Fund	32.86	51.79	*****
SBI Magnum Tax Gain	43.58	64.28	*****
Birla Equity Plan-Dividend	31.57	36.76	****
HDFC Long Term Advantage Fund	21.58	41.56	****
Sundaram BNP Tax Saver	31.63	44.99	****
Birla Sun Life Tax Relief 96	40.86	32.48	***
Franklin India Tax Shield	25.83	34.79	***
Prudential ICICI Tax Plan	25.20	43.67	***

* Source : Value Research, Returns (%) as on Jan 05, 2007 # Annualised Return

~ Value Research is an independent provider of investment information. Founded in 1990, it has emerged as the most trusted provider of mutual fund information in India.

Salaried Class (Sample size 200)**Table. No. 1. Annual Incomewise distribution of sample respondents**

Sr. No.	Income Group (Rs.)	No. of Respondents	Percentage
1	Upto 1,00,000	40	20
2	100000 to 200000	105	52.5
3	200000 to 400000	28	14
4	400000 and above	27	13.5
5	Total	200	100

The above table signifies that 105 (52.5%) respondents belong to income group of 1 lac to 2 lacs per annum. Minimum number of respondents are 27 (13.5%) in the income group of 4 lacs and above.

For salaried class there is TDS as such salary earners follow systematic investment plan for adopting ELSS in order to save the tax.

Table. No. 2. Money investment by Sample

Sr. No.	Percentage of Income	No. of Respondents	Percentage
1	Upto 10%	25	12.5%
2	Upto 20%	65	32.50%
3	Upto 30%	67	33.50%
4	Upto 40%	23	11.5%
5	Upto 50%	16	8%
6	Above 50%	04	2%
7	Total	200	100

From the above table it may be observed that salaried class investor mostly contribute 20% to 30% of their income towards investment which are linked with tax. Once the limit of rebate is crossed they divert their savings towards other investment.

The above table shows that 67 (33.50%) invest 30% their income followed by 65 (32.5%). Only 4 (2%) contribute above 50%.

Table. No. 3 Pattern of Investment

Sr. No.	Type / pattern	No. of Respondents	Percentage
1	F.D.	102	51
2	P.O.	18	9
3	NSC/GDF/PPF/EPF/CPF	107	53.5
4	LIC	103	51.5
5	Mutual fund	86	43
6	Shares	28	14

From this table it is clear that out of 200 respondents 107 contribute towards postal investment or PF, 103 contributes regularly towards LIC Policies, 102 transfer their saving to Fixed Deposits, 86 are presently interested to invest in Mutual Fund specially in ELSS.

This trends shows that there is still a big potential of population which can contribute towards various ELSS schemes.

Table. No. 4. Investment in Mutual funds

Sr. No.	Category	No. of Respondents	Percentage
1	ELSS	80	89
2	Others	6	11
3	Total	86	100

As regards Mutual Fund investment 80 out 86 (89%) have preferred ELSS while remaining 6 (11%) have investment in other mutual fund / Bonds.

Salaried class is not fully aware of ELSS schemes and other investment.

Table. No. 5. Order of preference for investment

Sr. No.	Name of company	Order of preference	No. of Respondents	Percentage
1	DSP Meryll lynch	1	72	36
2	Franklin Templeton	2	47	23.5
3	Reliance	5	20	10
4	ICICI Prudential	3	26	13
5	UTI	4	24	12
6	HDFC	6	11	5.5
			200	100

From this table as per the response recorded DSP Meryll lynch stands No.1, Franklin Templeton at No.2, ICICI Prudential at No.3, UTI at No.4, and Reliance at No.5 and HDFC at No.6. This preference is given by salaried class.

conclusions

The conclusions presented below are based on the analysis of primary data collected from Salaried class.

1. Salaried Class

It may observe that 113 (56.5%)respondents are in the age group of 31 to 40 years followed by 38 (19%) in the age group of 41 to 50 years. These age groups are more dynamic in investments. Age group 51to 60 has 15 (7.5%) respondents least of the lot.

It may observed that maximum respondents 103 (51.54%) are from government services followed by 69 (34.5%), 28 (14%) respondents belong to semi Government service.

The study signifies that 105 (52.5%) respondents belongs to income group of 1 lac to 2 lacs per annum. Minimum number of respondents are 27 (13.5%) in the income group of 4 lacs and above.

For salaried class there is TDS as such salary earners follows systematic investment plan for adopting ELSS in order to save the tax.

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It may be observed that salaried class responded are more towards good return on investment 72 (36%) with tax benefits 101 (50.5%) responses for other parameter are comparatively less.

In response to question about least formalities in mutual fund investment (ELSS), 100% respondents are favourable.

conclusions on Hypothesis :

1. The schemes under ELSS are useful for income tax purpose.

This hypothesis is accepted because the salaried class, pensioners and businessmen prefer to invest in ELSS for saving tax.

2. Pensioners are mostly benefited by ELSS.

Pensioners are conservative considering their age and are more interested in getting better returns along with the benefits of tax rebates. This hypothesis is also accepted.

3. Salaried Class can invest to save income tax.

Salaried class prefers ELSS because their taxes are deducted at source and as such obtaining tax rebate helps them in reducing their tax burden. This hypothesis is also holds true.

Suggestions

Based on the analysis and conclusions, the following suggestions are put forward.

1. The scope of Income Tax Act should be widened to include losses suffered by investor especially the pensioners and salaried class because they have fixed income and loss suffered due to investment in ELSS reduces the benefits likely to be earned by these classes of respondents or investors.
2. The limit for tax rebate under Income Tax Act should be directly proportional to the inflationary trend in the market.
3. The investment made by the salary earners or pensioners in the name of dependants should also be considered for tax rebates.
4. Maximum limit of investment in ELSS should be enhanced to suit the needs of the investors.

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