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A HISTORICAL REVIEW OF EQUITY LINKED SAVING SCHEMES

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ABSTRACT

Equity Linked Saving Schemes are popular tax saving investment options available for deductions under the Income Tax Act 1961. ELSS allocates more than 80% of the corpus in equity and equity oriented instruments. It invests in sustainable, high quality stocks with consistent growth potential and looks beyond short- term fluctuations. High returns and shortest lock in period are the prime attractions of these schemes. Association of Mutual Fund of India (AMFI) is promoting Mutual Funds awareness programme and are also quite satisfied with the overall growth of Mutual funds. In this situation it will be interesting to look into the past and perform a renowned review of Equity Linked Saving Schemes.

INTRODUCTION

One of the means adopted by Government of India, to encourage investments into particular type of assets, is by providing individual investors with Income Tax incentives. Income Tax incentives provided for investments in general can take different forms like deduction, exemption and rebate. ELSS is one of the important investment options available for deduction under section 80C of income tax act 1961 as it invests majority of its corpus in equity instruments. ELSS is a best investment option as it has the shortest lock in period among all other investments available under sec.80C of the Income Tax Act 1961. During past years the returns on these schemes were quite high in comparison to other tax saving investment schemes like Public Provident Funds, National Saving Certificates, 5 Years Post Office Time Deposits, 5 Years Bank Fixed Deposits, Unit Linked Insurance Plans, National Pension Schemes etc.

Equity Linked Saving Scheme, as the name suggests it's a saving scheme which is completely linked or related to Equity. ELSS is a diversified equity mutual fund with maximum investment in equity and equity related products. Since, it's an equity fund; returns from an ELSS fund reflect returns from Equity Market. ELSS schemes are open ended that is, investors can subscribe to the fund at any day, NAV or the price of the fund is declared on every business day.

ELSS received some special privileges when it comes to the Income Tax Act 1961. These schemes are also known as tax saving mutual funds as an Individual/HUF can use to save income tax up to Rs 1.5 lakh under Section 80C every year.

NEED OF THE STUDY

There are so many investment options available under the Income Tax Act 1961. Equity Linked Saving Schemes are popular among all because of its extraordinary features. Majority of the investors are unaware of the transformational changes that occurred with the passage of time to ELSS during the tenure of different ruling parties. Hence, it is crucial to explore, appreciate and witness the changed provisions with respect to ELSS.

SIGNIFICANCE OF THE STUDY

1. The study will give an awaited insight about the changes that occurred to ELSS in past.
2. The study will help the investors, research scholars and professional bodies in gaining systematic and compiled information in respect to ELSS.

OBJECTIVES OF THE STUDY

1. To examine past year union budgets and explore the historical aspects of ELSS.
2. To add contextual background required to fully understand and interpret the changes occurred.

RESEARCH METHODOLOGY

Research Methodology is a way to systematically solve research problem. It study the various steps that are generally adopted by the researcher in studying research problem along with the logic behind it.1 It is a science of studying how research is to be carried out. Essentially, the procedure by which researchers go about their work of describing, explaining and predicting phenomena are called research methodology.

Research Design

The preparation of research design facilitates research to be as efficient as possible yielding maximal information. In other words, the function of research design is to provide for the collection of relevant evidence with minimal expenditure of effort, time and money.[2]

A historical research design has been used to design the study. The purpose of a historical research design is to collect, verify, and synthesize evidence from the past to establish facts. This approach is well suited to do past analysis of events.

Data Collection

Since, it is a historical research design hence it used secondary sources for data collection.

Source of data collection

The instruments used to collect secondary data include union budgets of various years.

HISTORY OF ELSS IN INDIA

Various important announcements have been made regarding ELSS in the union budgets of year 1989-90, 1990-91 and 1991-92 and so on. In year 1989-90, Shri S.B.Chavan, the former finance minister, firstly discussed about ELSS and described that to increase the flow of personal saving, equity can be opted as an investment option. He also announced the whole structure, working and contribution of ELSS in tax deductions.

The announcement was as follows:

"In order to stimulate the flow of personal savings into equity, the Government intends to introduce an Equity-Linked Savings Scheme. The Scheme will operate through UTI and recognized Mutual Funds and investments will be eligible for tax deductions on the basis of net annual additions to such savings. Details of the Scheme will be announced shortly".[3]

Union Budget 1989-90 (Shri S.B. Chavan, Minister of Finance, 28 February, 1989)

Finally in year 1990-91 it came under the tax bracket as a fully fledged investment option. The budget stated that Investment in units under the Scheme would be eligible for deduction up to a maximum of Rs.10,000 from the total income. Returns from the schemes were eligible for deduction under section 80L of the Income Tax Act 1961 although any capital gain arising from the sale would be taxed in the hands of investor only.

*** Section 80 L of Income Tax Act 1961-Deductions In Respect Of Interest on Certain Securities, Dividends, and Etc.**[4]

The announcement was as follows:

"The Equity Linked Savings Scheme (ELSS) announced last year has now been finalised on a 'netting' principle. Investment in units under the Scheme will be eligible for deduction up to a maximum of Rs.10,000 from the total income. The annual return on the investment in the units will be eligible for tax concession under section 80L. On repurchase of the units by the Mutual Funds, the capital amount representing the cost of the units will be taxed as income in the year of repurchase and the excess will be liable to tax as capital gains. The Equity Linked Savings Scheme will eventually replace the present deduction under section 80CC. Meanwhile, this provision is being extended for investments made up to 31st March, 1991."5

Union Budget 1990-91 (Prof. Madhu Dandavate, Minister of Finance, 19th March, 1990)

In the union budget of year 1991-92, the government appreciated the scheme by stating that ELSS mutual funds are better option for investors as it provides tax incentives as well as it is suitable for those investors who do not want to invest directly into companies shares. The Scheme eventually replaced the eligible deduction under section 80CC in year 1991-92. A new section 80CCB relating to deduction in respect of investment made in accordance with the notified equity linked saving schemes has been inserted with effect from the A/Y 1991-92.[6]

Few lines from union budget 1991-92 were as follows:

"In regard to Mutual Funds, some progress towards evolving a competitive structure has been made in the last few years with encouraging results. For many investors, mutual funds are a more suitable investment vehicle than direct ownership of shares. The Government is already giving tax incentives for equity-linked savings schemes offered through mutual funds. The Government has now decided to further promote the development of mutual funds by throwing the field open to the private sector and joint sector mutual funds. In order to safeguard the interests of the investing public, and to encourage a healthy growth of the capital markets, a comprehensive set of guidelines is being evolved for the operation of all mutual funds. Consideration will also be given to enactment of legislation for this purpose".[7]

Union Budget 1991-92 (Shri Manmohan Singh, Minister of Finance 24th July, 1991)

From the financial year 1991-92 onwards, the tax incentive was modified to a tax rebate benefit, under Section 88 of the Income Tax Act, with 10,000, remaining the eligible investment amount.8 However; Tax rebates under Section 88 are not available to those earning above Rs. 5 lakh a year.[9]

In year 1999-2000 an important announcement was made by Mr. Yashwant Sinha that time Finance Minister. He stated that all the returns received from UTI and Mutual funds will be fully exempted from taxation as it will help the small investors. For Mutual Funds Company he stated that those companies who have open-ended equity-oriented schemes with more than 50% investment in equity are exempted from dividend distribution tax. The announcement was made with the intention to encourage the investments of small investor to the capital market and revive their confidence.

The announcement was as follows:

"First, I propose to fully exempt from income tax all income from UTI and other Mutual Funds received in the hands of the investors. This will not only reduce the incidence of tax, but will eliminate the inconvenience faced by small investors in paying tax and claiming refund in connection with income derived from such investments".[10]

Union Budget 1999-2000 (Shri Yashwant Sinha, Minister of Finance 27th Feb, 1999)

In union budget of year 2004-2005 once again announcement was made by the finance minister, Mr. P Chidambaram on July 08, 2004, he announced that Taxes on long term capital gains from securities transactions will be abolished.

The announcement was as follows:

"Capital gains tax is another vexed issue. When applied to capital market transactions, the issue becomes more complex. Questions have been raised about the definitions of long-term and short-term, and the differential tax treatment meted to the two kinds of gains. There are no easy answers, but I have decided to make a beginning by revamping taxes on securities transactions. I propose to abolish the tax on long-term capital gains from securities transactions altogether".[11]

Union Budget 2004-05 (Shri P Chidambaram, Minister of Finance 08th July, 2004)

Again, in the union budget of 2005-2006, Section 88 was formally replaced by section 80C.

The announcement was as follows:

"Every tax payer to be allowed a consolidated limit of Rs.1 lakh for savings which will be deducted from the income before tax is calculated; all prevailing sectoral caps to be removed; rebate under Section 88 being eliminated and Section 80L being omitted to reflect the new regime".[12]

Union Budget 2005-06 (Shri P Chidambaram, Minister of Finance 28th Feb, 2005)

***Section 88 of the Income Tax Act allows tax rebate from the amount of tax payable in respect of sums paid or deposited towards list of certain investment options which include ELSS also.**

Section 80C replaced the earlier Section 88 which was available till 1st April 2005. The Deductions permitted in the 80 C Section of Indian Income Tax is more or less the same investment mixes that were available in Section 88. However, this new section has allowed a major change in the method of providing the tax benefit. Section 80C of the Income Tax Act allows certain investments and expenditure to be tax-exempt. Unlike Section 88, there are no sub-limits and is irrespective of how much you earn and under which tax bracket you fall. The section 80C limit was of Rs.100000 and consisted full deduction for Equity Linked Saving Scheme.

Time to time amendments was made by the past prevailing governments regarding the scheme. Later in union budget of year 2014-15, Investment limit under section 80C of the Income-tax Act raised from 1 lakh to 1.5 lakh, 13 which again acknowledged ELSS for full deduction.

The announcement was as follows:

Increase in savings and their productive use leads to higher economic growth. The households are the main contributors to savings. Therefore, to encourage domestic investment in long term savings, I propose to increase the investment limit under section 80C of the Income-tax Act from ` 1 lakh to ` 1.5 lakh.[14]

Union Budget 2014-15 (Shri Arun Jaitley, Minister of Finance 10th July, 2014)

In the Union Budget 2018-19, Finance Minister Mr. Arun Jaitley, re-introduced LTCG tax on stocks. The investor will have to pay 10% tax on gains exceeding Rs. 1, 00,000 during a financial year from the sale of shares or equity mutual fund schemes. Earlier, LTCG tax on stocks was abolished by then finance minister Mr. P. Chidambaram in the union budget 2004-05.

The announcement was as follows:
"The return on investment in equity is already quite attractive even without tax exemption. There is therefore a strong case for bringing long term capital gains from listed equities in the tax net. However, recognizing the fact that vibrant equity market is essential for economic growth, I propose only a modest change in the present regime. I propose to tax such long term capital gains exceeding `1 lakh at the rate of 10% without allowing the benefit of any indexation. However, all gains up to 31st January, 2018 will be grandfathered".[15]

Union Budget 2018-19 (Shri Arun Jaitley, Minister of Finance 1st Feb, 2018)

A BACKGROUND

ELSS has always been a crucial investment option and it gone through a lot of changes during past years. At the time of introduction it was a part of section 80CCA, then 80CCB, again it was treated as a rebate and came under section 88 and finally now from a very long time the provision comes under section 80C. There were some important changes occurred with respect to the eligible investment and maximum deductions under the Act. After all the amendments, Exhibit 1.0 showed the compilation of the taxation policy for ELSS.

Exhibit 1.0 Taxation Policy for ELSS – A Background

Year	Section	Eligible Investment	Maximum Deduction	Benefits
From 1/4/1990 to 31/3/1991	Section 80CCA	10,000	10,000	Returns from the scheme are eligible for deduction under section 80L
From 1/4/1991 to 31/3/1992	Section 80CCB	10,000	10,000	Returns from the scheme are eligible for deduction under section 80L.
From 1/4/1992 to 31/3/2005	Rebate under Section 88	10,000	30% of the Investment	Returns are Tax Free.
From 1/4/2005 to 31/3/2014	Section 80C	1,00,000	1,00,000	Returns as well as Capital gains after sale is also tax free.
From 1/4/2014 to 31/3/2018	Section 80C	1,50,000	1,50,000	Returns as well as Capital gains after sale is also tax free.
1/4/2018-till now	Section 80C	1,50,000	1,50,000	Long Term Capital Gains of more than Rs. 100000 in a financial year will be taxable @ 10% without the benefit of indexation.

Source:
https://www.indiabudget.gov.in/bspeech/bs199091.pdf,
https://www.indiabudget.gov.in/bspeech/bs199192.pdf
https://www.indiabudget.gov.in/bspeech/bs199293.pdf
https://www.indiabudget.gov.in/ub20056/bh/bh1.pdf,
https://www.indiabudget.gov.in/ub2014 15/bh/bh1.pdf
http://pibphoto.nic.in/documents/rlink/2018/feb/p20182104.pdf

The above mentioned Exhibit 1.0, described the historical amendments made by the ministry of finance in respect to the taxation policy for ELSS starting from F/Y 1990-91 to F/Y 2018-19.

FINDINGS AND CONCLUSION

There are so many necessary changes occurred to the scheme. Right from 1990-91 the scheme offers tax free returns. Although when we talk about the LTCG the scenario is bit different. The long term gains were taxable from starting itself but if got abolished in the union budget of 2004-05 by that time finance minister Mr. P. Chidambaram. From the year 2004-05 till 2017-18, the LTCG on ELSS was tax free. This means that the refund from the scheme was completely exempted. That was the reason why ELSS was also called as EEE schemes. From 2004-05 till 2017-18 the initial investment amount was fully allowable for deductions, the returns from the schemes were also tax free and withdrawals or refunds were also tax free.

Again, in the union budget of 2018-19, the finance minister, Mr. Arun Jaitley proposed and applied the concept of LTCG. He announced that the investor will have to pay 10% tax on gains exceeding Rs. 1,00,000 during a financial year from the sale of shares or equity mutual fund schemes without availing the benefit of indexation. Although the only difference between the announcements of union budget 2004-05 and 2018-19 is that in former the indexation benefit was there and there was not any threshold limit of Rs. 1,00,000 during a financial year.

A specified time to time change in the union budgets with respect to ELSS shows that it is a game changer option for the investors. Being a mutual fund, it is indirectly related to the share markets and hence it is a very much deciding factors when it comes to regulate the share market earnings. Any change with respect to the scheme will give new a dimension to share market and will have an impact on the investment patterns of the investor also as far as investment under section 80C is concerned.

Hence, it can also be stated that the past changes may also reflect in future announcements also.

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