Indian Express ND 22.10.2012 P-18

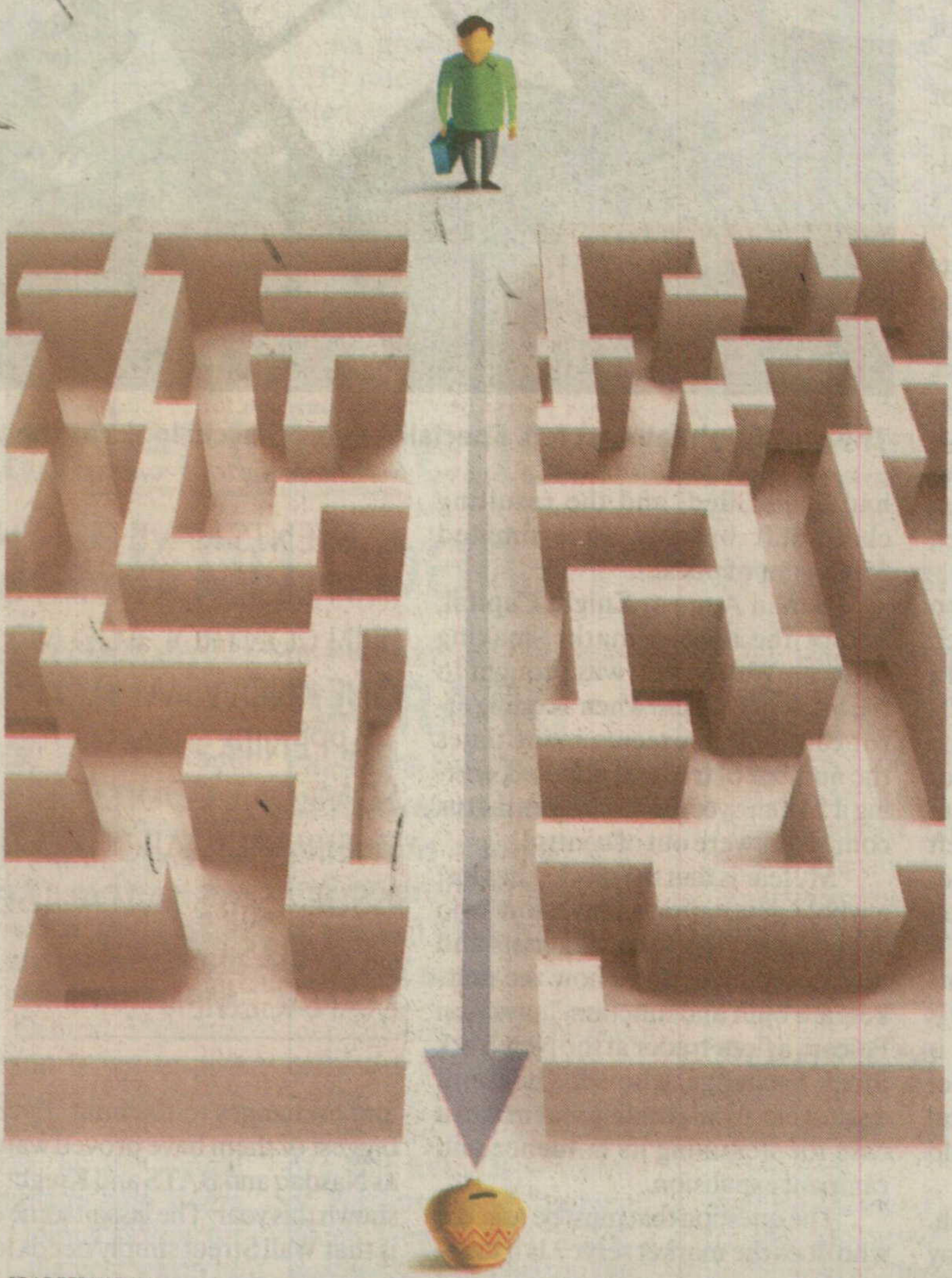
CHANGING TIMES

RGESS: High on hopes, low on delivery

While the scheme may emerge as a new tax saving category, the actual benefit may not be good enough to motivate investors toward equity investing, says Ritu Kant Ojha

THIS is that time of the year when most tax payers start evaluating various tax saving options. While public provident fund, employees' provident fund, home loan and insurance have traditionally been some of the popular tax saving options, there is a new scheme available for saving tax now — Rajiv Gandhi Equity Savings Scheme (RGESS).

Over the years, the dependence of Indian equity markets on foreign capital has increased. Foreign investors are known for their quick entry and exits which create volatility in the market and make investing into equity that much riskier. This also means that the investor has to track most of the external factors along with keeping an eye on the domestic issues, which is a complex task. RGESS is an attempt by the government to channelise part of the domestic savings into the equity markets which would help reduce the volatility in the market. Experts, however, believe that while the intention of the government is in the right direction, it is unlikely to yield any significant result due to its rigid provisions.



PRADEEP YADAV

WHAT IS RGESS?

The then finance minister, Pranab Mukherjee, had said in his Budget (2012-13) speech that "to encourage flow of savings in financial instruments and improve the depth of domestic capital market, it is proposed to introduce a new scheme called RGESS..." While the scheme was announced in the Budget this year, details of the scheme were announced just last month. Some of its salient features are:

- A person with a taxable income of less than ₹10 lakh can avail benefits under this scheme, with a permissible investment of ₹50,000 and the exemption is available for ₹25,000, ie 50 per cent of the invested amount under Section 80 CCG of the Income Tax Act.
- It is available only for the new retail investors who have not invested in stocks/ derivatives.
- This exemption is available to an individual over and above the exemption available under Section 80 C of ₹1 lakh.
- Investors can make these investments in instalments over the year.
- There is a three-year lock-in period. For the first 12 months, investor will not be allowed to sell but after that it can be done to realise gains. However, investor would have to maintain the initial level of investment, for a total period of 3 years.
- Investments can only be made in companies that are under BSE 100 index; NSE's CNX 100; public sector Navratnas, Maharatnas and Miniratnas; and IPOs of public sector units that have sales of at least ₹ 4,000 crore in the preceding three years. Exchange traded funds (ETFs) and mutual funds whose portfolio consists of stocks that are in the above list will also be eligible.

"We are waiting for the final details from Securities and Exchange Board of India on the scheme. Still there are some clarifications needed. However, a restrictive scheme will definitely lead to lower collections," said Sankaran Naren, CIO of ICICI Prudential MF.

SHOULD YOU INVEST?

At the outset, the scheme looks to be an attractive option for the investors as it provides tax benefit over and above the present tax saving options under the Income Tax Act. It indeed sounds like a serious attempt to induce more people to invest in equity. One of the benefits of investing in this scheme, which is not available in any other tax saving instrument, is that after a year, one can realise gains arising out of the investments in RGESS. The profit realised would be tax free on account of being long-term capital gains. However, the only caveat is that the total amount initially invested must remain same. For example, if an investor invests ₹ 50,000 in a year and that amount becomes ₹ 65,000 after a year, ₹ 15,000 worth of securities can be liquidated as profits (₹ 65,000 minus ₹ 50,000).

However, a hard look at the provisions tells us that the tax benefit that one can derive from the scheme is not much. There are around ₹ 3 crore tax payers in the country below ₹ 10 lakh taxable income. Out of this, approximately 90 per cent belong to the below ₹ 5 lakh taxable income category which comes under the 10 per cent income tax slab.

This effectively means that over 90 per cent of the people can avail only 10 per cent tax deduction on RGESS. So on an investment of ₹ 50,000, the maximum savings will be only ₹ 2,500 as only 50 per cent of the amount invested is available for deduction. Even for those in the 20 per cent tax bracket, the maximum savings will only be to the tune of ₹ 5,000. The worst part, according to the experts, is that the scheme is available only once in a lifetime which means that the investor can take the benefit of tax deduction on this scheme only in a single financial year.

"I hope that in the years to come, the government extends the one-time limit in the RGESS. Even if it can't be made permanent like 80C or other tax-breaks, perhaps it can be extended to three or five years. People get initiated into something and gradually get used to it. One single year may not be enough for the government's goal of establishing an equity investment culture, to be met," said Dhirendra Kumar, managing director, Value Research.

In short, the scheme may emerge as a new tax saving category, but the actual benefit may not be good enough to motivate investors towards equity investment. ♦

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