THE ECONOMIC TIMES wealth

MAKE MOST OF CREDIT CARD REWARD POINTS
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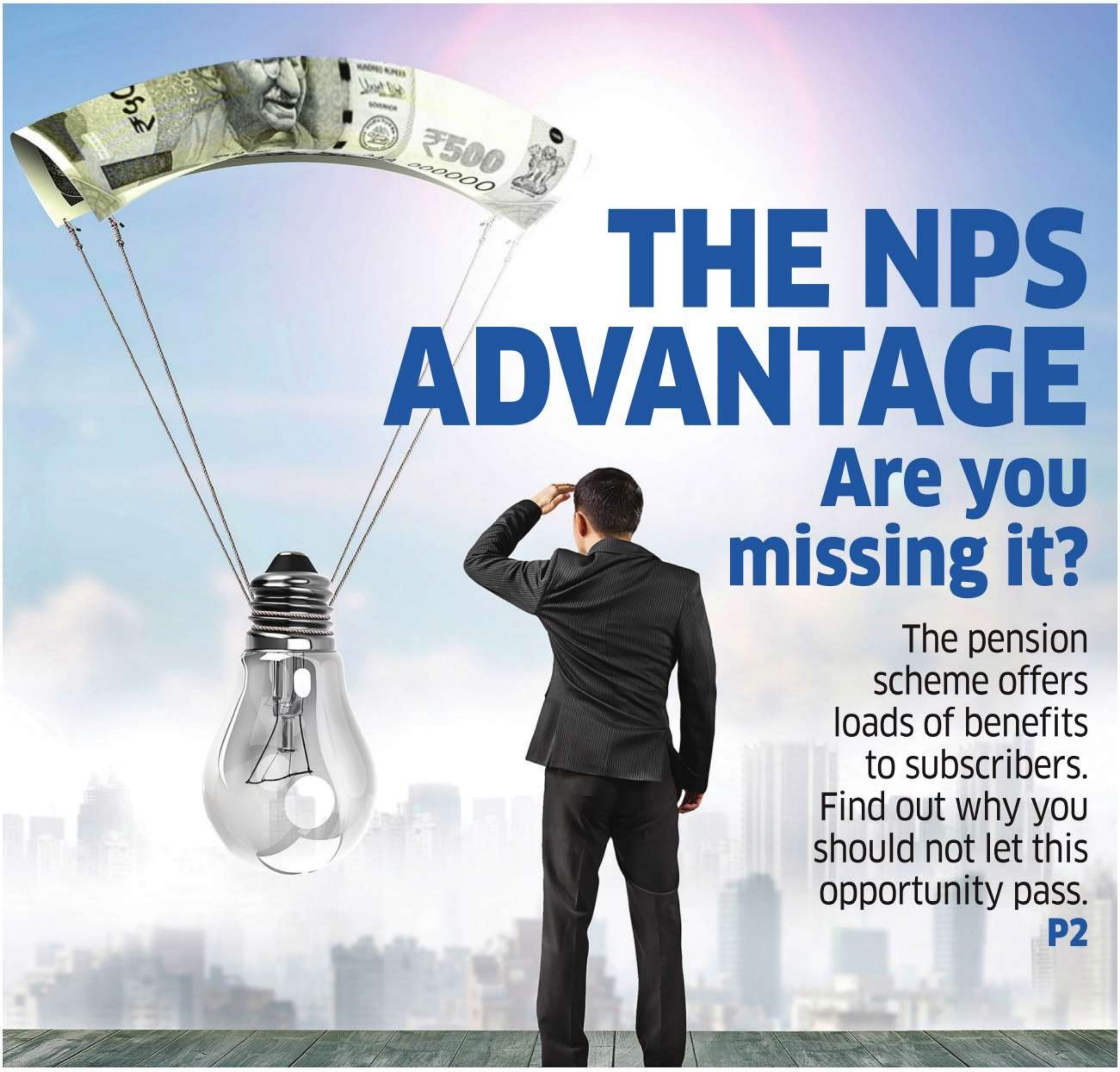

THE NPS ADVANTAGE

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PHOTOS & ILLUSTRATION: GETTY IMAGES

Changes in NPS tax rules and features

These tweaks have made the pension scheme more attractive.

- **Apr 2015** Additional deductions under Sec 80CCD(1b) and Sec 80CCD(2).
- **Jun 2018** Cap on equity exposure raised from 50% to 75%.
- **Jul 2019** Budget makes 60% of NPS maturity corpus tax free.
- **Jun 2021** Full corpus can be withdrawn at 60 if amount below ₹5 lakh.
- **Aug 2021** Maximum ages for entry and exit raised to 70 years.
- **Apr 2022** Two more pension fund managers join NPS.
- **Jul 2022** Allocation can be changed four times in a year.
- **Oct 2022** Reduction in 75% equity exposure after 51 no longer mandatory.
- **Mar 2023** Investments can be across multiple fund managers.
- **May 2023** Investor can purchase multiple annuities if amount above ₹10 lakh.

By **Babar Zaidi**

Their salary is roughly the same level, but last year Gurpreet Sethi paid nearly ₹1 lakh more in tax than some of his co-workers. Shocked by the high tax outgo, the Delhi-based product manager wrote to *ET Wealth*, searching for ways to reduce his tax liability. Tax filing portal Taxspanner analysed his tax details and found that Sethi was not availing many of the deductions available to him, including the NPS benefit offered by his company and investing in the scheme on his own. "The NPS alone could have reduced his tax by more than ₹51,000," says Sudhir Kaushik, Founder and CEO of Taxspanner.

Changes in tax rules, introduction of investor-friendly features and greater flexibility have combined to make the NPS more attractive during the past decade. The pension scheme offers everything one may look for in a retirement product. Contributions are eligible for exclusive tax breaks that are not available to any other investment option. The growth during the accumulation period is also not taxed, switching in and out of funds has no tax implication and 60% of the corpus is tax free on maturity.

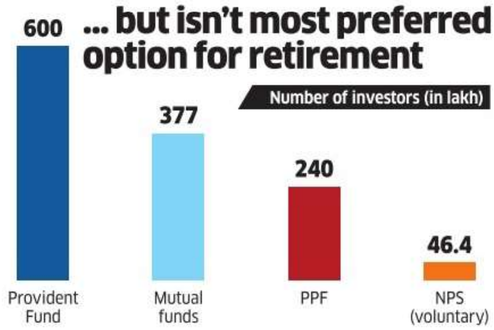
The NPS has also become more flexible in recent years. Individuals can now change their asset mix up to four times in a year. They can also invest in funds of multiple pension fund managers. Subscribers who are not very investment savvy can go for any of the three Lifecycle funds that continuously change the

So, NPS has grown manifold...

Voluntary subscribers (in lakh)

... but isn't most preferred option for retirement

Number of investors (in lakh)



asset mix as the person ages. Also, if the corpus on maturity is less than ₹5 lakh, the entire amount can be withdrawn without putting 40% in an annuity. If the amount being put in annuities is more than ₹10 lakh, the subscriber can opt for multiple annuities. In a recent interview to a newspaper, PFRDA Chairman Deepak Mohanty said the regulator is considering a proposal to roll out systematic withdrawal plans. Under SWPs, the investor can withdraw a fixed sum at a predefined interval without the need to buy an annuity.

These changes and investor-friendly tweaks have led to explosive growth, with the number of voluntary subscribers in NPS growing more than 12 times in the past 10 years. But despite this spectacular growth, the pension scheme is still not the most preferred option for retirement savings in India. The Provident Fund has some six crore active subscribers, while mutual funds have 3.77 crore unique folios. Even the staid PPF has an estimated subscriber base of 2.4 crore. With just 46.4 lakh voluntary subscribers, the NPS has barely tapped 10% of the total investing population in India.

Interestingly, while the tax breaks on NPS have progressively increased, other retirement savings and other investment options have seen their benefits shrink. Long-term capital gains from stocks and equity-oriented mutual funds beyond ₹1 lakh in a financial year are now taxable. If the premium of Ulips and insurance policies exceeds ₹2.5 lakh, the maturity proceeds will be taxed. Gains from debt funds and debt-oriented hybrid funds will now be taxed at the slab rate. Even the Provident Fund interest will be taxed if the subscriber puts more than ₹2.5 lakh in a year.

Tax benefits that NPS offers

There are three ways to save tax through NPS.

Sec 80C	Sec 80CCD(1b)	Sec 80CCD(2)
Contributions to NPS are eligible for deduction in the overall ₹1.5 lakh limit under Sec 80C.	Additional tax deduction of ₹50,000 for contributions to NPS. Can be done on own.	Up to 10% of basic salary put in NPS by employer is tax free. Can be done only through employer.

Gurpreet Sethi
44 years, Gurgaon

Though his company introduced the NPS benefit in 2016-17, Sethi was not aware how it can reduce his tax till he approached ET Wealth for tax optimisation. He has now opted for the NPS benefit under Section 80CCD(2) wherein his company will put 10% of his basic salary in the scheme.

"Had the HR person explained to me the tax benefits of NPS, I could have saved almost ₹2.5 lakh in tax in the past seven years."

What keeps investors away

Why are investors staying away from an option that offers greater tax efficiency? The biggest impediment for the NPS is the abject lack of awareness about the features and benefits of the scheme. His company rolled out the NPS benefit almost seven years ago, but Sethi was clueless how it could help him. He also didn't utilise the additional ₹50,000 deduction under Sec 80CCD(2). "The HR person did not fully explain how the scheme works. I could have saved almost ₹3 lakh in tax since 2016," he says glumly.

Millions of taxpayers like Sethi have let this opportunity pass. Even though NPS can save a big chunk of tax, not many employees sign up for the scheme. That's surprising, because saving tax has traditionally been the biggest driver of investment decisions in India. "The tax benefits and features of the NPS are unmatchable. It can't get any better for investors," says Nehal Mota, co-founder of wealth advisory platform Finnovate. Hyderabad-based financial adviser Nitin Vyakaranam, who provides financial wellness advice to employees of corporates, says barely 5-6% employees opt for the NPS benefit.

Another reason for the lukewarm re-

"There is very low awareness about NPS benefits. Even finance professionals don't know of them, leave aside HR people and common investors."

NEHAL MOTA
CO-FOUNDER, FINNOVATE

"Saving for a goal that stretches too far into the future is not always a priority. Young people can't visualise themselves in that situation."

NITIN VYAKARANAM
FINANCIAL WELLNESS ADVISOR

NPS is ultra cheap

NPS charges are a fraction of what mutual funds charge for fund management

Maximum fund management charges by NPS (per year)	0.09%
Fund management charge of ₹5,000 crore mutual fund	1.5%

MFs can charge 30 bps more if new inflows from retail investors beyond 30 big cities are at least 30% of gross inflows or 15% of average AUM.

Charges can have big impact in long run

If you invest ₹5,000 per month in a fund that gives 9% a year, here's what the fund management charges will be.

At 0.09%	₹1.47 lakh
At 1.5%	₹21.77 lakh

The NPS corpus will be bigger by more than ₹20 lakh after 25 years.

sponse to NPS is that retirement figures low on the priority of young investors. "For some people, saving for a long-term goal that stretches too far into the future is not a priority. They cannot visualise themselves in that situation when they are young," says Vyakaranam.

For some investors, the compulsory annuitisation of 40% of the corpus on maturity is the deal breaker. "The mandatory annuity takes away the optionality from the investor. Individuals want to be in control of their money and don't want to put it in an inflexible option," says Vyakaranam.

"Fund management charges of the NPS are the lowest in the industry. Even a small difference can have a big impact over 20-25 years."

RAJ KHOSLA
MANAGING DIRECTOR, MYMONEYMANTRA

Can NPS beat mutual funds?

Some people stay away from NPS because they believe they can earn better returns from other investments. Meet Rishi Ahuja (*see picture*), a Delhi-based software professional who has made good money from investing in stocks and equity funds. Ahuja is not enthused by the tax benefits offered by NPS because he has opted for the new tax regime and wants to continue investing in stocks and mutual funds.

But he can still opt for the NPS benefit under Sec 80CCD(2), wherein 10% of his basic salary put in the NPS will be tax free. This deduction is available even under the new tax regime. If Ahuja opts for this benefit, the ₹4,166 (10% of his basic salary) his company will put in the NPS every month will reduce his annual tax by ₹15,600. If the tax benefit is factored in, the net outgo will be only ₹2,866 per month.

There are other reasons why investors like Ahuja should consider investing in NPS. Mutual funds levy fund management charges. The fund management fees of 1.5% a year might seem small. After all, what's ₹1,500 a year on an investment of ₹1 lakh. But it can add up to a sizeable amount over the long term. Consider this: if you do a ₹10,000 SIP in a mutual fund that charges 1.5% a year, over 25 years you would have paid a whopping ₹22 lakh in fund management charges. We have used 1.5%, whereas some funds charge upwards of 2.5% a year. What's more, they are allowed to charge 30 bps more if new inflows from retail investors beyond 30 big cities are at least 30% of gross inflows or 15% of average AUM.

In stark contrast, the NPS charges a fraction of what mutual funds cost. The maximum charge on funds of up to ₹10,000 crore is 0.09%. That is ₹90 per ₹1 lakh invested in the scheme. Compared to ₹22 lakh fee paid on a mutual fund SIP for 25 years, the charges on NPS will be only ₹1.47 lakh (*see graphic*). "The pension scheme has one of the lowest fund management charges in the industry. Even a small difference can have a massive impact over 20-25 years," says Raj Khosla, Managing Director, MyMoneyMantra.

The NPS has another advantage over mutual funds. Long-term capital gains above ₹1 lakh from equity funds are now taxable. If you do SIP of ₹10,000 in MF and earn 9% return, after 25 years the corpus value would be roughly ₹1.13 crore. Of this, ₹30 lakh would be principal and ₹83 lakh would be the capital gain. "The investor will pay 10% tax on this capital gain. But in NPS, ₹68 lakh (60% of corpus) will be tax free while the remaining ₹45 lakh will be annuitised," points out Mota.

Rishi Ahuja
38 years, Delhi

Ahuja has no plans to invest in the NPS because he wants to opt for the new tax regime that offers fewer tax deductions. His company offers him the NPS benefit which will be eligible for deduction under the new tax regime, but Ahuja is not interested. He believes he can earn higher returns by investing through mutual funds.

"The compulsory annuitisation of 40% of the maturity corpus is very restrictive. My mutual funds offer me greater flexibility and possibly higher returns."

Sonalika Jaiswal
31 years, Hyderabad

Jaiswal invests ₹50,000 in the NPS under Sec 80C, but is clueless how the NPS benefit from employer under Sec 80CCD(2) works. After ET Wealth explained to her how her tax outgo can be reduced, she readily agreed to opt for it.

"The contribution to NPS will reduce my take-home salary, but it will bring down my tax by almost ₹25,000."

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