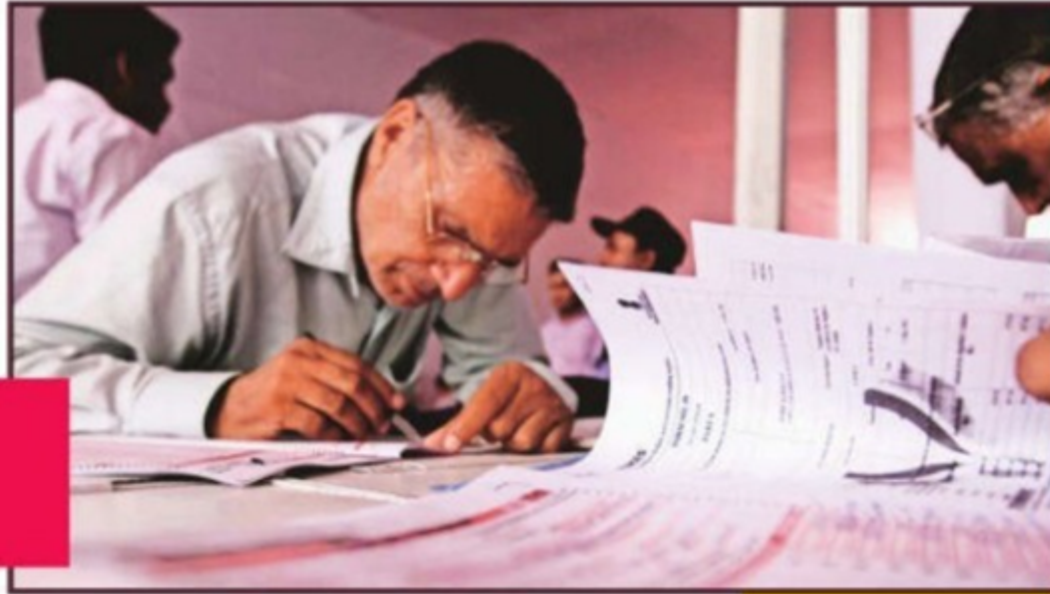
Has Section 80C lost its sheen?

Few provisions in the tax laws are 'ubiquitous' and 'antiquated' at the same time. Section 80C is one such. As exemptions and deductions are being phased out, it seems to be at odds with the policy direction. ***Vishwas Panjiar*** and ***Shubham Jain*** explain its provisions, and see reasons for its survival



TAX SAVING

What does 80C provide for?

SECTION 80C OF the Income Tax Act allows individuals (whether salaried or self-employed) and Hindu undivided families to avail tax deductions of up to ₹1.5 lakh of investments made by them as part of their long-term/retirement planning. Taking advantage of tax benefits under Section 80C can significantly reduce an individual's tax burden. In order to claim such deduction, taxpayers must invest in eligible investment instruments or spend the specified amount on designated expenses within the financial year.

Some of the main deductions available are payment for unit-linked insurance plan, National Savings Certificates, and Provident Fund contribution, equity-linked savings scheme, repayment of principal component of home loan, tax saving fixed deposit, etc. There are specific conditions associated with each items, which need to be complied with in order to be eligible for the deduction. With the help of these deductions, taxpayers can not only lower their tax liabilities but also make prudent financial decisions that contribute to long-term savings and investment goals.

Surge in personal income tax collections

THE GOVERNMENT'S COLLECTION from personal income taxes has been increasing sharply over the past few years (a growth of ~25% was registered in FY2023-24 alone) so much so that it is now over 50% of the total direct tax collection. Three key factors are commonly attributed to this: improved tax administration; rising income level; increased use of artificial intelligence and machine learning to check tax evasion.

An important factor, which is equally significant but not part of the public discourse, is the new optional tax regime that the government introduced in 2020 for individual taxpayers. The new tax regime reduces the applicable tax rate of individuals if he/she foregoes tax deductions available under the Act.

~25%

PERSONAL INCOME TAX COLLECTIONS IN FY23-24, OVER 50% OF TOTAL DIRECT TAX COLLECTION

NEW TAX REGIME (2020) REDUCES APPLICABLE TAX RATE OF INDIVIDUALS IF ONE FOREGOES DEDUCTIONS

₹1.5 lakh

INVESTMENT-LINKED TAX DEDUCTIONS ALLOWED UNDER 80C, UNAVAILABLE IN THE NEW TAX REGIME

How to review before investing?

BEFORE COMMITTING TO investment in any of the financial instruments, taxability under all three stages needs to be evaluated: Investment of capital; yearly income (growth or accrued interest); and maturity value. One can claim deduction under Section 80C only at the first stage (investment). There may be taxability at the other two stages depending on the instrument. While 80C items typically include EET instruments (investment and accrued interest are exempt, but maturity value is taxable), in certain instruments EEE (tax exemption in all three stages) and ETE (investment and maturity value eligible for exemption, but accrued interest taxable) is available. It is therefore important to evaluate before committing to invest. Also, various financial instruments have lock-in periods of five to 15 years, curbing access to funds and reducing liquidity. Thus, taxpayers should balance their portfolios with both liquid and long-term investments to ensure adequate liquidity for unforeseen circumstances.

How govt views tax deductions

THE GOVERNMENT HAS time and again stated its intention to promote the new tax regime among individual taxpayers. While this policy position is to promote ease and simplicity in taxing norms, it ostensibly also discourages (read "does not explicitly promote") savings and long-term investment, by not allowing deductions under Section 80C. This is in contrast to a typical Indian societal system that puts a premium on savings.

The 80C limit of ₹1.50 lakh per year, which was last increased a decade ago (in 2014), has not kept pace with inflation. Increasing this limit could nudge taxpayers to invest more in the specified savings instruments, potentially boosting overall household savings and investment rates. Encouraging higher investments through an updated 80C limit aligns with the social and economic goals of promoting financial security and robust retirement planning for Indian households.

What is the future of 80C?

AS THE SERVICE SECTOR in the country grew, more and more salaried people joined the workforce thereby making Section 80C one of the most ubiquitous tax provisions. The Section also often gets credited with formalising India's long-term investment habits. The government would surely want this trend to continue in the future as most of the Indian workforce is currently below the average age of 30 years and are taking investment decisions based on their retirement goals. One of the main casualties of the introduction of the new tax regime is that investment-linked deduction (80C deduction) of up to ₹1.5 lakh is not available if one chooses the new regime. One would hope that the government introduces a new avatar of 80C deduction to the new tax regime as well.

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