ALL UG COURSES

FINANCIAL LITERACY

VALUE ADDITION COURSE (VAC)

SEMESTER-I, II, III & IV COURSE CREDIT-2

DEPARTMENT OF DISTANCE AND CONTINUING EDUCATION
UNIVERSITY OF DELHI
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UNIT - I

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LESSON

1

Financial Literacy and Financial Planning

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STRUCTURE

1.1 *Learning Objectives*
1.2 *Introduction*
1.3 *Savings*
1.4 *Time Value of Money*
1.5 *Management of Spending and Financial Discipline*
1.6 *Summary*
1.7 *Answers to In-text Questions*
1.8 *Self-Assessment Questions*
1.9 *References*
1.10 *Suggested Readings*

1.1 Learning Objectives

- Develop a basic understanding of saving.
- Brief introduction to time value of money.
- Management of spending and financial discipline.

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1.2 Introduction

1.2.1 *Financial Literacy*

Financial literacy refers to the knowledge and skills that enable individuals to make informed decisions about managing their finances. It involves understanding concepts such as budgeting, saving, investing, and managing debt. Having a good level of financial literacy is essential in today's world, where financial decisions can have a significant impact on an individual's life. It can help individuals make informed decisions about spending, saving, and investing their money. Unfortunately, many people lack financial literacy, which can lead to poor financial decisions. This can result in financial stress, debt, and even bankruptcy. To improve financial literacy, it is important to educate individuals on basic financial concepts and provide them with the tools they need to manage their finances effectively. This can include financial literacy classes, online resources, and financial counseling services. In conclusion, financial literacy is a critical skill that everyone should have. By improving financial literacy, individuals can make informed decisions about their finances, reduce financial stress, and achieve their financial goals.

The S&P Global FinLit Survey indicates that there is a significant lack of financial awareness among 76% of Indian adults. "Only 24% of Indian respondents adequately understand key financial concepts, including risk diversification, inflation and compound interest" - S&P Global FinLit Survey (2014).[1] There are several reasons for this low level of financial literacy in India. One reason is the lack of access to formal financial services in many parts of the country, particularly in rural areas. Another reason is the limited availability of financial education and resources. However, in recent years, there have been efforts to improve financial literacy in India. The government and various financial institutions have launched initiatives aimed at educating people about financial concepts and products. For example, the RBI has launched a national financial education campaign to raise awareness about financial literacy and improve financial inclusion. In addition, there has been a significant increase in

[1] See 3313-Finlit_Report_FINAL-5.11.16.pdf (gflec.org)

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digital financial services in India, which has made it easier for people to access financial products and services. This has led to an increased focus on digital financial literacy. Overall, while there is still a long way to go, there are positive signs that financial literacy in India is improving. With continued efforts to educate people about financial concepts and increase access to financial services, it is hoped that financial literacy in India will continue to improve in the coming years.

1.2.1.1 *Importance of Financial Literacy*

- Financial literacy helps individuals make informed decisions about managing their money
- Financial literacy helps protect individuals from fraud and scams
- Financial literacy can promote economic stability and growth
- Financial literacy can reduce the burden on social welfare systems
- Financial literacy can improve overall societal well-being

1.2.2 *Financial Planning*

Financial Planning provides you with a blueprint which helps you realize all your dreams in life in a very systematic and planned manner without causing you any sleepless nights. Remember, financial planning is a process, not a product. It gives you the confidence that you know you are on the right track and in safe hands and that you will have the money when you need it - when you want to buy a house or a car or when you want to get your daughter married or send her off for education. Or when you retire. Financial Planning combines the elements of risk management, investment planning, tax planning and retirement planning to comprehensively plan for your future needs.

1.2.2.1 *Need for Financial Planning.*

- Need for personal financial planning to look at your complete financial situation, including your assets, liabilities, cash flows, financial goals, risk appetite, life situation, family background, etc.
- To plan systematically for your financial goals and objectives, including life insurance, health insurance, retirement, child planning – education & marriage, house purchase, estate planning, investment planning, etc.

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- To make your financial life better and secured for yourself and your family and ensuring that all financial goals are achieved.
- To better understand and learn about your financial situation and understand the reasoning and logic behind all recommendations made. Also, to better understand the different asset classes and financial products and their suitability to you.
- To regularly review the progress of financial plans and/or to revise the financial plans to accommodate any major change in personal life or financial situation.

1.2.3 *Financial Goals/Personal Finance*

Financial planning involves analysing the current financial position of individuals to formulate strategies for future needs within financial constraints. Personal finance is specific to every individual's situation and activity; therefore, financial strategies depend largely on the person's earnings, living requirements, goals, and desires. Individuals must save for retirement, for example, which requires saving or investing enough money during their working lives to fund their long-term plans. Personal financial planning provides you with a long-term strategy for your financial future, taking into consideration every aspect of your financial situation and how each affects your ability to achieve your goals and objectives. For example

- Buying a family health cover
- Managing debt
- Planning for retirement
- Investing to save taxes in efficient manner
- Creating wealth for future generation
- Saving to buy your favourite vehicle
- Saving for purchasing dream home
- Investing for higher education of children, marriage and other purpose

1.2.4 *Financial Planning Strategy*

A good financial planner should express verbally and in written form the detail financial plan to the client so that he/she is aware of how that

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person will achieve his/her financial plan. Some of the points of strategy are as follows:

(a) **Risk Management:** This involves minimizing the risk involve finances like health insurance, life cover, investment cover, income protection in order to provide income security to oneself and family.

(b) **Proper Asset Allocation:** This involves investment in proper asset in order to achieve financial goals like debt, equity, mutual fund, bond, commercial paper. Thumb rule for this is investment in debt should be equal to one's age and remaining amount should be in equity. For example, a 30-year-old person should invest 30% in debt and the remaining 70% in equity. It also dependent upon the risk appetite and income level of client. Adequate amount of money should be kept as liquid asset like cash to meet unexpected expenses.

(c) **Tax Consideration:** assessing proper tax planning so as to reduce tax burden effectively. It will help in accumulation of wealth. Following taxes should be considered: - Wealth tax, entertainment tax, Property tax, Income tax, Gift tax, Corporate tax, Security transaction tax. Debt which attracts more tax should be reduced. All details of financial plan should be made clear to the client.

(d) **Estate Planning:** Estate planning is the preparation of tasks that serve to manage an individual's asset base in the event of their incapacitation or death. The planning includes the bequest of assets to heirs and the settlement of estate taxes. Most estate plans are set up with the help of an attorney experienced in estate law. Assets that could make up an individual's estate include houses, cars, stocks, artwork, life insurance, pensions, and debt. Individuals have various reasons for planning an estate, such as preserving family wealth, providing for a surviving spouse and children, funding children's or grandchildren's education, or leaving their legacy behind to a charitable cause. The most basic step in estate planning involves writing a will. Other major estate planning tasks include the following:

(i) Limiting estate taxes by setting up trust accounts in the names of beneficiaries.

(ii) Establishing a guardian for living dependents.

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(iii) Establishing annual gifting to qualified charitable and non-profit organizations to reduce the taxable estate.

(iv) Setting up a durable power of attorney (POA) to direct other assets and investments.

1.3 Savings

Savings is the money a person has left over when they subtract their consumer spending from their disposable income over a given time period. Savings can be used to increase income through investing. The extent to which individuals save is affected by their preferences for future over present consumption, their expectations of future income, and to some extent by the rate of interest. There are two ways for an individual to measure his savings for a given accounting period. One is to estimate his income and subtract his current expenditures, the difference being his savings. The alternative is to examine his balance sheet (his property and his debts) at the beginning and end of the period and measure the increase in net worth, which reflects his savings.

Total national saving is measured as the excess of national income over consumption and taxes and is the same as national investment, or the excess of net national product over the parts of the product made up of consumption goods and services and items bought by government expenditures. Thus, in national income accounts, saving is always equal to investment. An alternative measure of saving is the estimated change in total net worth over a period of time.

For example: Saving is the amount left after a person met his/her expenditure for example if you have 10, 000 after incurring an expenditure of 8,000 you are left with 2,000. This 2,000 will be termed as your savings.

Benefit of Savings:

1. It acts as a Safety net
2. Less Stress
3. Enables you to Travel
4. Financially Independent
5. No worry from Unexpected Expenses
6. Comfortable Retirement

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Safety Net: It helps you to meet the unexpected expenses like car repair, expensive medical bills, or a sudden job loss. If you were to lose your job, you'd be thankful you socked away a good amount of money into your emergency fund to tide you over until you found a new job. There by acting as safety net. Saving should ideally be equivalent to three to six months of expenses.

Less Stress: Savings helps to get rid of your tensions like will I be able to pay my educational expenses on time, or will I be able to meet my medical expenses? stop worrying as now you have good amount of savings to meet your obligation, thereby saving reduces your stress level.

Enable you to Travel: Your savings account isn't only for things you need—it can be for things you want, too. Saving up for a big purchase beforehand means you won't pay extra in finance costs such as interest and fees, you can also use that money to plan your desired vacation like visit to Paris, France - the city of lights, Peru, the Grand Canyon etc.

Financially Independent: Freedom gives us the ability to pursue our dreams, so it is equally important to create such independence in our finances too, this is accomplished by saving and investing. As all of us have desire to have material possession like house, car white goods and spend lifestyle like watches jewellery and clothes it is important to save and invest in return that are higher than rate of inflation. We should understand the difference between nominal and real returns. When you invest in a 6 percent fixed deposit, the return that you get is "nominal". If inflation is 4 percent, the "real" return is just 2 percent. And, in higher tax brackets, even this 2 percent may go away in taxes. Therefore, not taking risks at all may be alright to protect your savings but it may not allow your savings to grow after adjusting for inflation and taxes.

To achieve financial independence, it is therefore paramount that you invest in high yielding assets. But, with small sums of money at our disposal, the only viable option is to invest in equity markets through institutional vehicles like mutual funds. Creating financial independence requires a lot of discipline. As a thumb rule, one should save at least 25 to 30 percent of one's monthly earnings. Also, the younger you are, the higher percentage should be allocated towards equity investments.

Comfortable Retirement: Retirement is an important reality for everyone. When planning for retirement, it's always better to start as early as

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possible for best compounding returns and not to rely heavily on one source of savings. Because there are always emergencies in old age. So, having a sufficient corpus to deal with all these is crucial. You can opt for unit linked insurance plan (ULIPs), ULIP are designed in a way that offers you both protection and investment benefit, till the age of 99 to 100 years. These are the plans which not only take care of providing your beneficiaries with death benefit but also take care of your living needs, during your retirement. You have the flexibility to enter into Whole Life ULIPs at any age between 18 and 100 years and can exit at any age. You can also choose till what age you want to save money or accumulate money. This could be till your retirement.

1.4 Time Value of Money

- **Time Value of Money:** The time value of money (TVM) is the concept that money you have now is worth more than the identical sum in the future due to its potential earning capacity. This core principle of finance holds that provided money can earn interest, any amount of money is worth more the sooner it is received.
- **Time value of Money in Personal Finance:** Here the person wants to receive money today rather than in the near future. Now the question arises why? This is simply because the person is aware of the time value of money. If the person has money today in hand, then he can earn interest by investing that money, this is referred to as earning capacity of money. Say, if you invest Rs. 100 today – the returns will be more compared to the same investment made 2 months from now. Moreover, there is always a risk that the borrower might delay even more or not pay at all in the future. Example: if a friend of yours offers you to lend 20,000 today and 20,500 after 2 years and you have option to choose the one. Then clearly the second option i.e., 20,500 may or may not fructified and with first option you would have money today and you could invest and earn return or interest on that money.

1.4.1 *Present Value*

Present value is the current value of future payments in lump sum, or several part payments discounted at certain interest rate. Present value

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of one-time investment**:** To calculate the present value of a one-time investment, you'll need to know the amount of the investment, the interest rate, and the number of years until the investment matures. The formula to calculate present value when future value is given.

$PV = FV/(1 + R)^n$, where: FV = future value, R = rate of return, n = number of periods.

For example, let's say you're considering investing $10,000 in a bond that matures in 5 years and has an interest rate of 4%. Using the present value formula, you can calculate that the investment's present value is approximately $8,557. This means that the investment is worth $8,557 today, taking into account the time value of money and potential inflation.

1.4.2 *Future Value*

Future value is the sum of money that any saving scheme with a compounded interest will build to by a pre-decided future date. It applies to both lumpsum as well as recurring investments like SIP.

Future investment for one-time investment- The formula for calculating future value where investment earning simple interest: $\boldsymbol{FV = I \times (1 + (R \times T))}$ and where investment earning compound interest: $FV = I \times (1 + R)^T$

where: **I** = Investment amount, **R** = Interest rate, **T** = Number of years

Questions based on future value.

Q.1. You are scheduled to receive Rs. 14000 in two years. When you receive it, you will invest it for six more years at 8 percent per year. How much will you have in eight years?

Ans. $FV = I \times (1 + R)^T = 14000 \times (1 + 8\%)^6 = 22{,}216.240$

Q.2. You invest Rs. 10,000. During the first year the investment earned 20% for the year. During the second year, you earned only 4% for that year. How much is your original deposit worth at the end of the two years?

Ans. For 1st yr : $10000(1 + 20\%)^1 = 12000$

For 2nd yr:$12000(1 + 4\%)^1 = 12800$

Worth at the end of 2 yr = 4643.28

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1.4.3 *Effective Annual Interest Rate*

The effective annual interest rate is the real return on a savings account or any interest-paying investment when the effects of compounding over time are considered. It also reveals the real percentage rate owed in interest on a loan, a credit card, or any other debt.

***Effective Annual Interest Rate* = $(1 + i/n)^n - 1$**

where: i = Nominal interest rate, n = Number of periods

For example, consider these two offers: Investment A pays 10% interest, compounded monthly. Investment B pays 10.1% compounded semi-annually. Which is the better offer?

In both cases, the advertised interest rate is the nominal interest rate. The effective annual interest rate is calculated by adjusting the nominal interest rate for the number of compounding periods the financial product will experience in a period of time. In this case, that period is one year. The formula and calculations are as follows:

- For investment A, this would be: 10.47% = $(1 + (10\%/12))^{12} - 1$
- And for investment B, it would be: 10.36% = $(1 + (10.1\%/2))^2 - 1$

Investment B has a higher stated nominal interest rate, but the effective annual interest rate is lower than the effective rate for investment A. This is because Investment B compounds fewer times over the course of the year.

IN-TEXT QUESTIONS

1. The money you have now is worth more than the identical sum in the

(a) Future *(b)* Present

(c) Past *(d)* None of the above

2. ____________ is the current value of future payments in lump sum or several part payments discounted at certain interest rate.

(a) A Present Value *(b)* Future Value

(c) Compounded Value *(d)* None of the above

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3. Mr. Ram borrowed 10,00,000 from a bank on a one year 16% term loan, with interest compounded quarterly. Determine effective annual interest rate on loan?
   (a) 12% (b) 16.9%
   (c) 13% (d) 14%
4. The formula for calculating future value where investment earning simple interest = I × (1 + (R × T), here I represents:
   (a) Interest rate (b) Investment
   (c) Index value (d) None of the above

1.5 Management of Spending and Financial Discipline

1.5.1 *Management of Spending*

Management of spending can easily be achieved by following the financial planning strategies. This involves following steps:

1. Devising a budget.
2. Cutting down of unnecessary expenditure.
3. Retirement planning.
4. Find ways to save: Mode of savings.
5. Track your spending.
6. Make plan to pay off your debt.
7. Pay your bills timely.

Devising a Budget

Budgeting and saving money don't come naturally to many people for obvious reasons. Spending money on nonessentials is so easy, even if you're committed to a well-laid spending plan. Budget, which can help you reorganize your finances, prioritize spending, and manage debt, thus allowing you to make progress toward your long-term financial goals. Making a budget involves the following:

- List all your income after taxes—for example, employee and freelance income, investment income, and interest earned on any savings

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accounts. Then list all expenses—for example, rent or mortgage payments, credit card payments, instalment loan payments, grocery receipts, and utility bills.

- Subtract the expense from the income to get a general picture of your financial health. If your income total is larger than your expense total—congratulations—you just found more money for saving, investing, and paying down your debt. But If your expense total is larger than your income total, all is not lost, but you'll have to make some choices about where you spend some of your money going forward if you want to balance your budget.
- Reduce your expenditure by categorising them into fixed expenses, discretionary expenses and variable expenses. Fixed expenses are those which have to be incurred like rent, medical expenses, you can do nothing with them, they remain constant. The variable expenses can be controlled to an extent by bringing behavioural changes like turning of light can reduce electricity bills. Discretionary expenses can effectively be controlled and generate opportunity for savings.
- Adopt a 50-20-30 approach where 50% of your after-tax income on housing, food, and other necessities.

  20% on paying down debt or increasing savings.

  30% on whatever you want—discretionary spending.
- Put your budget to work, means you must strictly follow the budget prepared by you in order to achieve financial goal.

Cutting Down Unnecessary Expenses

Start by cutting spending on items you don't need. For example, do you need a $5 coffee every morning? Could you make do with a smaller, older car? Instead of an expensive vacation, would you be willing to try a stay-at-home vacation (staycation)?

These types of choices are very personal, so there's no right or wrong answer. But laying them out on the table can at least help you understand your priorities and some of the options you may not have realized you had for saving money.

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Retirement Planning

Saving for retirement always sounds like a good idea in theory, but it isn't always easy in practice. It involves following steps:

- Start saving early, Sign up for your retirement plan as soon as you're able to. The sooner you start taking advantage of this benefit, the more you'll start to save. For example, if you save at 25 v/s you save at 35, the earlier you start, your savings will be benefited of the power of compounding.
- **Know your Retirement Goal:** Your expenses during retirement might not be the same as they are when you're working. But that doesn't mean you won't have any expenses. You'll probably need somewhere between 70% to 90% of your current income to cover yourself in retirement. It's a good idea to plan now for what you need later. If you'd like to maintain your current living standards, try to make sure you're contributing enough to cover those costs later in life. If you think you won't have as many expenses in retirement, you'll still need to save, but you can adjust your goals accordingly.
- **Tax Efficacy:** Once you reach retirement age and begin taking distributions, taxes become a big problem. Most of your retirement accounts are taxed as ordinary income tax. That means you could pay as much as 37% in taxes on any money you take from your traditional 401(k) or IRA. That's why it's important to consider a Roth IRA or a Roth 401(k), as both allow you to pay taxes upfront rather than upon withdrawal. If you believe you will make more money later in life, it may make sense to do a Roth conversion. An accountant or financial planner can help you work through such tax considerations.
- **Insurance:** A key component of retirement planning is protecting your assets. Age comes with increased medical expenses, and you will have to navigate the often-complicated Medicare system. Many people feel that standard Medicare doesn't provide adequate coverage, so they look to a Medicare Advantage or Medigap policy to supplement it. There's also life insurance and long-term-care insurance to consider.

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Find ways to Save: Mode of Savings

Savings Schemes are investment options for Indian citizens launched by the government as well as other public sector financial institutions. These saving schemes were introduced as an incentive to cultivate healthy saving and investing habits in India. This is also a way to increase the inflow of money into the Indian economy. In earlier times Indians used to keep their money with themselves and this caused poor circulation as well as stagnation of wealth. By means of saving schemes, which are backed by the government, Indian citizens can allow their wealth to appreciate at higher interest rates and reap benefits such as tax exemption that certain savings schemes offer. Savings schemes cater to a wide demographic and encourage individuals to invest for various milestones of life such as retirement, children's higher education, their marriage etc. They are ideal for long-term wealth creation as they come with a certain lock-in period and offer good returns. Since they are not impacted by market volatility, they are safer investment options, ideal for the conservative investor. Furthermore, the interest rates on various saving schemes are revised on a quarterly or half yearly basis, keeping up with the rising costs of living and inflation.

- Different saving schemes are depicted in the flow chart given below:

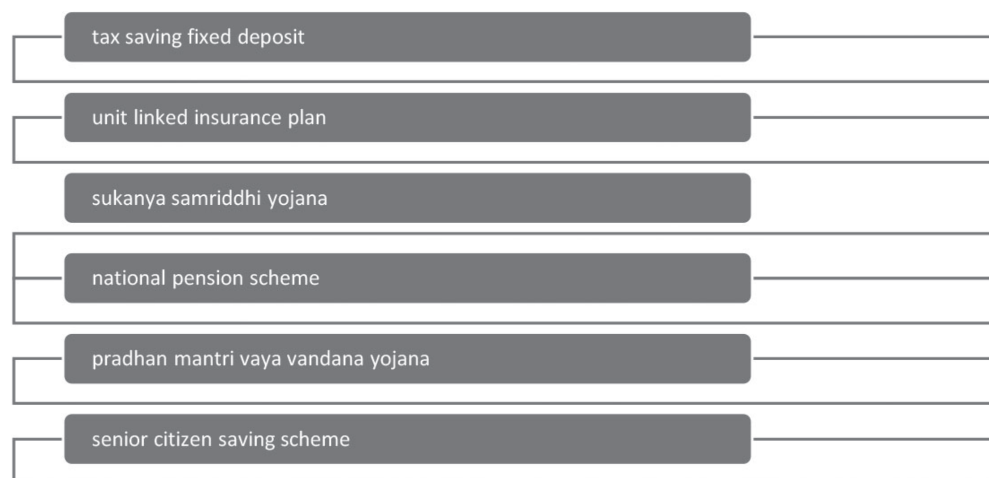

Figure 1.1

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1.5.2 *Financial Discipline*

Financial discipline involves control of money, inculcating the habit of saving and avoiding excessive expenditure. One should consider following steps to harness financial discipline to achieve our financial goal.

- Prepare a monthly spending budget and stick to it.
- Invest with a goal. Goals give direction and help you in selecting right product.
- Avoid loans for your desires. Better do a financial planning check before going in for a big purchase.
- Invest monthly to become regularise in your savings and this will also help you maintain consistency.
- Motivate yourself by visualising the goals and the end result for which you are working for.

1.6 Summary

In this chapter, we delve into the intricacies of financial planning and management. We discussed the importance of setting financial goals and creating a budget that aligns with those goals. We also discuss the various types of savings accounts, investment options, and retirement plans available. Furthermore, we explore the concept of time value of money, which is the idea that the value of money changes over time due to inflation and interest rates. This gives a brief outline of how to calculate the present and future value of your money, and how to use this knowledge to make informed financial decisions. In addition, this chapter provides you with useful tips on how to manage your spending effectively and achieve financial discipline. You also learn about different methods of budgeting, how to prioritize your expenses, and how to avoid common financial pitfalls. This chapter gives a comprehensive understanding of financial planning and management and is equipped with the knowledge and skills necessary to make smart financial decisions that will help you achieve your goals.

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1.7 Answers to In-Text Questions

1. *(a)*
2. *(a)*
3. *(b)*
4. *(b)*

1.8 Self-Assessment Questions

1. Briefly explain about the time value of money.
2. Discuss the benefits of savings.
3. Explain the management of spending.
4. What is financial planning?

1.9 References

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UNIT - II

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LESSON

1

Banking Products and Services

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STRUCTURE

1.1 *Learning Objectives*
1.2 *Introduction*
1.3 *Types of Banks*
1.4 *Banking Products and Services*
1.5 *Types of Bank Deposit Accounts*
1.6 *Documentation*
1.7 *Various Types of Loans*
1.8 *Summary*
1.9 *Answers to In-Text Questions*
1.10 *Self-Assessment Questions*
1.11 *Reference*
1.12 *Suggested Readings*

1.1 Learning Objectives

- Recall the different types of banks.
- Understand and distinguish the different types of services by banks.
- Get knowledge on the different types of bank deposit accounts.
- Explain the various types of loans.

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1.2 Introduction

Another important topic that you would have gained knowledge on would be the meaning, importance and need for financial planning along with learning about the budget and its different types and the various terms associated worth it. In this unit you will be given detailed classification about the types of banks and the kinds of service that banks offer to their customers. After going through this Unit, you will also be able to identify the different types of bank deposits and gain knowledge about the different types of loans.

1.3 Types of Banks

In the previous unit you have been made aware of the term bank and its different functions. There are different types of banks, some of which are discussed below:

- **Reserve Bank of India (RBI):** It is the Central bank of the country and is also called as the Banker's bank. Its functioning is regulatory in nature as it regulates the functioning of all other banks operating in India. Hence supervises the functioning of the entire banking sector in India. It has a key role to perform information of monetary policies and foreign exchange mechanism. Some of the key issues it has assay in are related to customer care, disclosure of financial position etc. There are no dealings with the general public unlike all the other banks. Only RBI is entrusted with issuing currency.
- **Commercial Banks:** According to the traditional definition of a commercial bank, it is a financial institution that primarily engages in the acceptance of deposits from individuals and offers various lending and financial services. Commercial banks offer fundamental banking services to their customers, including consumers and enterprises of small to medium scale.

  A commercial bank is a type of financial institution that offers a range of services to its customers, including loans, certificates of deposits, savings bank accounts, and bank overdrafts. These financial institutions generate revenue by providing loans to individuals and charging interest on the borrowed amounts. A commercial bank

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offers a range of lending products, including company loans, vehicle loans, housing loans, personal loans, and school loans. In other sense these are companies established under special Acts. These can be domestic or foreign in nature.

Primarily commercial banks can be divided into two categories: Scheduled Banks and Non-Scheduled Banks.

Scheduled Banks: Banks mentioned in the list in the 2nd Schedule of the Reserve Bank of India Act, 1934 are scheduled banks. These are further categorised into Private, Foreign and Multinational banks. Cooperative banks too fall in this category if they fulfil certain criteria.

Non-Scheduled Banks: Those that are not listed in the above are obviously non-scheduled banks. There are a total of 1458 non-scheduled banks in India as per the latest information available at the time of preparing this lesson.

- **Regional Rural Banks (RRBs):** Regional Rural Banks (RRBs) in India are financial institutions that have been designated as scheduled commercial banks. These banks are specifically established to cater to the banking needs of rural areas within each state. The Regional Rural Banks (RRBs) are financial institutions that specifically address the financial requirements of those residing in rural areas and those who are socioeconomically disadvantaged. These banks operate at a regional level, serving several states within the country. These are established by the Govt- be it national, state or at the union territory level. Their operations are limited and local to the state or UT in which they are established. Hence their area of operation is predefined.
- **Public Sector Banks:** Public sector banks (PSBs) are financial institutions characterized by majority government ownership, with the government holding more than 50% of the bank's capital. The government regulates the financial standards of these institutions. The general view among depositors is that their funds are more secure when trusted by public sector banks, mostly due to their government ownership. Consequently, a significant proportion of public sector banks possess a substantial number of customers. The State Bank of India (SBI) is recognized as India's largest public sector bank.

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- **Private Sector Banks:** In addition to 3 and 4 above are private sector banks, owned and managed privately. Unlike public sector banks, their priority is not the economic welfare but their own profitability and the objective of formation of such banks. Nevertheless, they too have to follow the RBI rules and regulations in force. Some of them are ICICI, HDFC etc.
- **Cooperative Banks:** The word cooperative means autonomous association of people aspiring to meet their own economic, social and/or cultural objectives through an entity jointly controlled and owned. The binding factor is mutual trust. These banks operate on the same lines as other banks but on no profit no loss basis. These are registered under Cooperative Societies Act, 1912 and these too are RBI regulated. These can be rural or urban in nature. As these are often backed by different states in India the word cooperative is often fixed before the word cooperative. Rajasthan State Cooperative Bank and Maharashtra State Cooperative bank are some examples.
- **Foreign Banks:** As the name suggests, these banks re incorporated in foreign land. The big difference is that they have to abide by the rules and laws of their home country as well as those in force in India (RBI). In a nutshell. They are neither govt owned nor registered in India e.g., HSBC, Barclay's Standard Chartered etc.
- **Development Banks:** Immediately after independence the need was felt to promote the lagging sectors of the economy and hence Development Banks came into being. There are 4 types-Industrial, Agricultural, Export Import and Housing. Thus, they are known as Specialised Financial Institutions. Development banks are financial institutions that provide extended funding for projects that need significant capital investment and have extended repayment periods. These projects typically include the development of irrigation systems, mining and heavy industry, as well as urban infrastructure.
- **Export-Import Bank:** These banks came into existence for the sole purpose of providing finance specifically for promotion of foreign trade. Export-Import Bank of India was established as an apex bank to finance entities in the field of export and import through commercial banks.

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- **Housing Bank:** These provide finance for the housing sector and related activities associated with the housing sector like construction of houses, plots, house repairs, etc. National Housing Bank was established to provide housing finance through commercial banks and other agency.

IN-TEXT QUESTIONS

1. ____________ is authorized to print currency notes by Government of India.
2. ____________ is established by Special Act.

1.4 Banking Products and Services

The main task of the scheduled banks is attracting deposits from investors and utilising it to run their organisations.

Let us See an Example: A person deposits some money with a bank and gets interest on it. Another takes a loan from the bank and pays interest on it. The difference of the interest becomes the primary income for that bank. So primarily the bank is the custodian of other people's money. Over the last few years, the banks have redeveloped themselves and are offering a wide range of services, some of which are mentioned below:

- **Facility of Loans:** Other than accepting deposits for different time durations, banks deal in advancing loans to different types of entities ranging from individuals to large multinational companies. The interest that they earn from giving these loans in their main source of income. They fulfil the requirement of funds of the different sections of the society.
- **Overdraft Facility:** The provision of an overdraft facility within a Current Account allows the account holder to make withdrawals even in cases where the account balance is low. Overdraft is a financial arrangement provided by banks that allows customers to exceed a predetermined limit, resulting in a negative balance referred to as an overdrawn amount.
- **Discounting of Bills:** Bill discounting is a viable alternative that allows businesses to speed up payment for their services and fulfil operational obligations without relying on outside sources for funding.

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- **Encashing Cheques:** Banks extend this service to both savings and current account holders. Cheques can today be encashed across any bank branch esp. in case where the bank offers Core Banking Solution or CBS which is usually written on the face of the cheque. Some banks offer the facility of multi-city cheque books to their account holders.
- **Collecting and Paying Instruments of Credit:** Services like collecting Credit instruments such as promissory notes and bills, As mentioned earlier the bank provides this facility as a custodian on behalf of its customers.
- **Exchange of Foreign Currency:** Another service offered by banks is to convert local foreign currency to local currency needed for account holders dealing in trade outside India.
- **Consultancy:** It started off as a service provided to High-Net-worth Individuals or HNIs and today most banks offer financial consultancy service to those customers who are interested in enhancing their wealth by investment in different instruments, stock market, bank assurance and even tax management.
- **Utility Bills Payment:** The bank may facilitate payment of bills and even taxes such as telecom bills, water and electricity bills.

ACTIVITY

How many public sector banks, private sector banks, foreign banks, regional rural banks, urban cooperative banks and rural cooperative banks are there in India?

1.5 Types of Bank Deposit Accounts

There are various types of accounts that banks offer for different types of customers. Some of them are discussed below:

1.5.1 *Savings Bank Account*

It is the nest account for Indian individuals with limited income but striving for a better and secure future. This can be opened with a limited initial amount. A minimum balance in this account needs to be

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maintained. The account holder also earns a quarterly interest which varies from one bank to another and also per the directive's issues by the RBI from time to time. Savings account is a basic account type that lets you deposit money safely with a bank. It ensures safety and access to your money whenever you need. You can withdraw your funds, either digitally or in person, at any point in time. Even foreign individuals can open an account but in joint capacity with an Indian. KYC norms need to be fulfilled.

1.5.2 *Term Deposit*

A term deposit is another name for fixed deposit that includes funds deposited into an account at a bank for a fixed period. Term deposit investments usually carry short-term maturities ranging from one month to about 3 years and will have varying levels of required minimum deposits. These deposits can be made by people who wish to save funds for longer periods. Hence a higher interest rate as compared to that applicable for savings account is given by the bank because the bank is reasonable sure that the specific fixed amount cannot be withdrawn by the depositor. During this time no withdrawals are allowed. These deposits are utilised by the bank to lend to other entities.

1.5.3 *Current Account*

This account is utilised by large entities such as business houses, companies and other commercial institutions. As there are restrictions on the number of times withdrawals can be made in a savings account, and these above entities need to make multiple withdrawals to run their organisations, therefor the need to have separate accounts, here, using a cheque book or even online, the institution or its authorised representative can make multiple withdrawals and deposits. Due to its nature, there is no interest earned due to the fluidity. The number of transactions that can be performed on current accounts is usually not limited. Other interested parties can get information about the creditworthiness of the account holder. EFT, wire transfer, net banking and even doorstep banking services are offered by the bank to these account holders.

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1.5.4 *Recurring Deposit*

This type of account is most suitable for those who are desirous of earning a fair return on their deposit. The depositor hands over a pre-decided amount monthly for a specified time period. They will get a lump sum amount at the end of the specified period. Interest is calculated on quarterly compounded based.

ACTIVITY

Visit a nearby bank branch of any bank and find out the range of products and services on offer.

IN-TEXT QUESTIONS

3. Documentation for operating current account is much easier as compared to savings account (True/False)

4. Full form of ATM is Any Time Money. (True/False)

5. Term Deposit is used as synonym for Fixed Deposit (True/False)

1.6 Documentation

To make it easy for the banks and their customers specific documents are required be it for opening an account, applying for loans or any other transaction with the bank for the first time, hence it is important that you familiarize yourself with these terms.

1.6.1 *PAN Card*

Permanent Account Number (PAN) is a ten-digit alphanumeric number, issued on a laminated card, by the Income Tax Department, to identify taxpayers in the country. Through these different transactions are tracked and cross verified by the IT authorities. PAN was introduced to facilitate linking of various documents, taxes, assessment, tax demand, tax arrears etc. relating to any entity This has helped to curb tax evasion and to widen the number of people paying taxes.

https://incometaxindia.gov.in/booklets%20%20pamphlets/tpi_pan-book.pdf

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1.6.2 *Address Proof*

Prior to opening an account, the bank asks for address proof as one of the conditions to verify the identity of the customer wishing to deal with the bank and avail of its services.

Any of the documents mentioned can be furnished as valid address proof.: Passport, Driving License, Voter ID Card, Job card issued by NREGA duly signed by an officer of the State Government, Aadhaar Card issued by UIDAI, Utility Bill, less than two months old, Bank account or Post Office savings account statement for 3 calendar months prior to four months along with Account Opening Cheque, Property Tax bill or Municipal Tax receipt not more than one year old, others.

1.6.3 *KYC Norms*

Short for Know your customer it is a mechanism to verify their customer's identity prior to opening an account. The genuineness of the customer can be identified through this. It also required frequent updating and the banking sector periodically contacts the customer to get updates.

1.7 Various Types of Loans

After accepting deposits from their customers, the banks earn interest subsequently by offering them as loans. You need to get knowledge of some of the popular types:

1.7.1 *Education Loan*

With education in general and higher education in particular becoming expensive, students need to fund their education. Thus, the need to apply for education loan to meet the shortfall in fees and other expenses to fund their education. Financial institutions as well as NBFCs attract borrowers by offering attractive interest rates on repayment. The borrower can also avail tax benefits under 80E. To apply, the borrower needs to submit the loan application along with the above documents to the financial institution and the process of loan disbursal will start if all things are found in order. Normally a grace period of 6 months after the

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completion of the course is given before the repayment process of the loan starts. The maximum time allowed for repayment is 8 years from the date of taking the loan.

1.7.2 *Consumer Durable Loans*

A consumer durable loan is a loan offered for the purpose of buying consumer durable products. These are products which have a life of at least 3 years. It is not backed by any security or collateral. The credit history of the borrower is not significant. The ability to payback, i.e., the income of the borrower is more important. Eligibility for this loan: (1) Age: Usually between 21 to 60 years. (2) Credit: as mentioned earlier the borrower's credit worthiness is not important, the borrower's income is seen.

To qualify for the loan, the individual's monthly income must range from 18,000–20,000 INR or above. The Rate of Interest on these loans is very high and are quickly approved. The maximum limit is Rs 5 lakhs and the maximum period of 36 months.

- **Types**
  - **Instalment Loans:** These are very common and paid back in periodic instalments according to a present timetable. These can be further divided into **Fixed and variable rate consumer durable loans.**
  - **Secured Consumer Durable Loans:** For availing thee, a security or collateral is needed Secured loans are those which are secured against assets as collateral.
  - **Unsecured Consumer Durable Loans:** For this more common type of loans, no security or collateral needs to be provided. Interest rates for unsecured loans are higher than for the secured loans.

1.7.3 *Vehicle Loan*

These can be classified into personal vehicle loan and commercial vehicle loans. The eligibility conditions and the interest and charges for these vary**.** Personal Vehicle Loan: Personal vehicle range from new and used

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bikes, scooters to cars required for personal use by individuals. This type of loan does not need any guarantor. These can be taken from banks and finance companies at attractive and competitive rates, both offline and online options for processing of such loans are available. For filling the form to avail the loan, vehicle make and model, manufacture date and attaching the necessary documents for the same. Such loans are available for up to 60 months. Loan is disbursed on the basis of the value of the personal vehicle be it new or used vehicle.

1.7.4 *Home Loans*

These loans are taken for owning a dwelling in one's own name. Critical savings of the individual can be utilised for other important tasks such as for education**.**

The loans come with a host of benefits and features. However, before applying for home loans, you should be aware of every aspect. So, here you will find some aspects related to the housing loans so that you become aware.

Features and Benefits of Home Loans:

- **Easy Availability:** All the financial institutions and NBFCs are offering attractive housing loan schemes. One can avail of the home loan after checking their eligibility to meet his/her requirements. It helps to create a win situation for both the lender and the borrower and also benefits the economy as more cash reaches those who need it- directly as well as indirectly.
- **Multi-purpose:** Housing loans are multi-purpose loans that are available for various purposes such as buying a new residential flat or building, constructing a new house on a plot, home renovation, or extending your current house.
- **Lower Interest Rat**e**:** Being a secured loan, home loans are generally subject to lower rates of interest as compared to other financing options. In case of problems there is the facility of top up loans.
- **Fast Loan Processing:** Home loans involve lenient eligibility criteria and minimal documentation. This enables financial institutions and NBFCs to process the loan amount faster. In case the borrower

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fulfils the basic eligibility criteria, the lending agency goes for quick registration and verification thereby hastening the disbursal process.

- **Long Tenure:** Since the loan amount involved in housing loans is high, the tenure to repay that loan can go up to as high as 30 years. This allows the borrower to choose an affordable EMI and ensure that his monthly budgets are not under any kind of pressure.
- **Tax Benefits:** You can claim a tax deduction of Rs. 1.5 lakhs on the principal repayment under Section 80C and Rs. 2 lakhs on the interest repayment under Section 24B. You can also claim a home loan tax deduction when you pay for the registration fees and stamp duty charges under Section 80C.

1.7.5 *Short-term, Medium Term and Long-Term Loans*

Loans can also be trifurcated as under:

- **Short-term:** Loans up to a period of 1 year are termed as short-term loans.
- **Medium Term:** Loans i.e., loans and advances granted for a period of above 1 year and up to and inclusive of 3 years.
- **Long Term:** Loans i.e., loans and advances granted for a period of above 3 years.

All loans need to be repaid with interest within the agreed upon period or as decided in the written agreement between the borrowing and lending entity. Short-term loans are needed to tide over an immediate need for funds or for meeting capital expenditure. The period of term is up to a year. It carries a lower interest rate as compared to other term loans. Long-term loans can last from just over a year to 25 years. Some short-term loans don't specify a payment schedule or a specific due date. They simply allow the borrower to pay back the loan at their own pace.

1.8 Summary

In the above unit you have read about the different types of banks operating in India, fulfilling the needs and requirements of different sections of society. They offer a wide range of products and services not only

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to satisfy the needs of customers and account holders but also enhance their income and meet the stakeholder objectives. You have learnt that banks mobilize funds by offering different types of deposits with differing benefits and interest rates focusing on the types of customers they get. Banks also customize their service by offering tailor made loans to different types of customers, meeting the demand for loans related to education to consumer durables to housing etc.

1.9 Answers to In-Text Questions

1. RBI
2. RBI
3. False
4. False
5. True

1.10 Self-Assessment Questions

1. Why is the Reserve Bank of India called as the Banker's Bank?
2. What role do banks perform between those with extra funds and those needing funds?
3. What are the different types of Banks?
4. Give one example each of commercial, cooperative and development bank.
5. Name the different types of Accounts.
6. How do you differentiate between Term Deposit and Recurring Deposit?
7. Differentiate between used and new commercial vehicle loans.
8. Why are all loan seekers not given loans?
9. What are the key features of savings account?
10. For whom is current account more suited?
11. Differentiate between current account and savings account.

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L E S S O N

2

Digitisation of Financial Transaction, Ponzi Scheme and Online Frauds

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STRUCTURE

2.1 *Learning Objectives*
2.2 *Introduction*
2.3 *Digitisation of Financial Transactions*
2.4 *Ponzi Schemes*
2.5 *Online Frauds*
2.6 *Protection Against Online Frauds*
2.7 *Handling Banking Complaints*
2.8 *Summary*
2.9 *Answers to In-text Questions*
2.10 *Self-Assessment Questions*
2.11 *References*
2.12 *Suggested Readings*

2.1 Learning Objectives

- Understand the digitisation of financial transactions (debit cards, credit cards, net banking etc.).
- Understand Ponzi schemes and Online frauds.

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2.2 Introduction

Upon the successful completion of this lesson, you will acquire a detailed understanding of the latest initiatives and technologies in the banking domain. In light of the Indian economy's rapid transition towards a cashless society, it is of paramount importance to acquaint oneself with the various modes of online transactions that are available to individuals through banks and other online platforms. This lesson provides an in-depth overview of these online transaction platforms, including best practices for their effective utilization. Furthermore, it elucidates the potential risks associated with online transactions, such as Ponzi schemes and online frauds, and provides guidance on how to identify and avoid these fraudulent activities. It is imperative that individuals exercise caution during online transactions, particularly those that offer short-term gains. This lesson imparts valuable precautions that individuals can take to ensure the safety and security of their online transactions. In conclusion, this lesson will provide the requisite knowledge to navigate the digital landscape of banking and online transactions with confidence and proficiency.

2.3 Digitisation of Financial Transactions

2.3.1 *Cashless Banking*

Cash, be it coins or currency, manufacturing as well as handling them, is a costly affair. There are inherent risks associated with cash handling and transfer and the costs overrun the benefits. To promote and empower the economy, the GoI has introduced Cashless Banking more so in Bank-to-Bank dealings. It has now trickled down to the other strata of society. It includes Plastic money like Debit Cards and Credit Cards, Mobile Wallets etc. You need to be aware and below you will get basic knowledge of some of the tools that has helped in the growth of cashless banking in India.

Bank Cards, like Debit Cards and Credit Cards are the most popular cashless payment methods. Unstructured Supplementary Service Data (USSD) is tailormade for those without a smartphone. Payment can be made without smartphone or internet. QR Code- The term QR stands for

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Quick Response through which consumers scan the QR code of the merchant to complete the transaction. It's a square grid containing pattern of black squared and is read by imaging devices like smartphone cameras.

Mobile Wallet- They are fast, risk free and convenient, through which people are able to transact and store e-money by simply linking it to their respective bank account. The user can make any kind of payment by simply entering phone number, email, unique code or scanning QR code (explained earlier).

2.3.2 *E-Banking*

Banking using electronic mode is called electronic banking or E-Banking for short. It is synonymous with virtual baking, online banking. Here the telecom network is utilized for bank related work via computes or even mobiles

Through E banking banks offer services like mobile banking, ECS, Smart Cards. EFTs, Telebanking, mobile banking etc.

Mobile Banking: Mobile banking (otherwise called M-banking) is a name utilized for performing account exchanges or transactions, bill payments, credit applications, balance checks, and other financial exchanges through a mobile phone like a Personal Digital Assistant (PDA) or cell phone.

Electronic Clearing System (ECS): The Electronic Clearing System is a creative provision for occupied individuals. With this provision, an individual's credit card bill is consequently charged from the same individual's savings bank account, so one doesn't have to stress over missed or late payments.

Smart Cards: A smart card is a card that stores data on a microchip or memory chip or a microprocessor in lieu of the magnetic stripe found on debit cards and credit cards. Smart cards are not utilized for transferring or moving monetary data alone, but also, they can be utilized for an assortment of identification grounds. Exchanges made with smart cards are scrambled or encrypted to shield the exchange of data from one party to another. Each encoded exchange can't be hacked and doesn't transmit any extra data past what's required for finishing the single exchange or transaction.

Electronic Fund Transfers (ETFs): Electronic fund transfer (EFT) is the electronic exchange of cash starting with an individual account in

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the bank to another individual account of the same bank, or within or with other financial institutions or with multiple institutions, by means of personal computers-based frameworks, without the immediate intercession of bank staff.

Telephone Banking: Telephone banking is an assistance given by a bank or other monetary foundation or other financial institutions, that empower clients to perform via telephone a scope of monetary exchanges which don't include cash or financial instruments, without the need to visit an ATM or a bank branch.

Home Banking: Home banking is the most common way of transacting from your own house as compared to the inconvenience of visiting a bank's branch. You are able to make account requests, deal in cash, pay bills, apply for credits, by just pushing a few buttons at your time and pace. The benefits are convenience, easy access, 24X7 availability, physical visit and interaction avoided. It is less costly for the bank as paperwork gets reduced, physical transfer and risk.

2.3.3 *Net Banking*

Net Banking: Internet banking, also known as online banking or e-banking or Net Banking is a facility offered by banks and financial institutions that allow customers to use banking services over the internet. Customers need not visit their bank's branch office to avail each and every small service. The person needs to register themselves with the concerned banks in order to avail net banking services.

Features of Net Banking

- Check the account statement online.
- Open a fixed deposit account.
- Pay utility bills such as water bill and electricity bill.
- Make merchant payments.
- Transfer funds.
- Order for a cheque book.
- Buy general insurance.
- Recharge prepaid mobile/DTH.

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Advantages of Net Banking

- **You can Avail Services Round the Clock:** Most of the services offered are not time-restricted; you can check your account balance at any time and transfer funds without having to wait for the bank to open.
- **It is Simple and Easy to Operate:** Using the services offered by online banking is simple and easy. Many find transacting online a lot easier than visiting the branch for the same. One need not stand in long queues.
- **It is Convenient and Efficient as you Can Complete Transaction within Minute:** You can complete your transactions from wherever you are. Pay utility bills, recurring deposit account instalments, and others using online banking. You can complete any transaction in a matter of a few minutes via internet banking. Funds can be transferred to any account within the country or open a fixed deposit account within no time on net banking.
- **You Can Keep a Track on all Your Transactions as they all are Recorded:** When you make a transaction at the bank branch, you will receive an acknowledgement receipt. There are possibilities of you losing it. In contrast, all the transactions you perform on a bank's internet banking portal will be recorded. You can show this as proof of the transaction if need be. Details such as the payee's name, bank account number, the amount paid, the date and time of payment, and remarks if any will be recorded as well.

Disadvantages of Internet Banking

- **Require Good Internet Connection:** An uninterrupted internet connection is a foremost requirement to use internet banking services. If you do not have access to the internet, you cannot make use of any facilities offered online. Similarly, if the bank servers are down due to any technical issues on their part, you cannot access net banking services.
- **There is Concern for Security as Online Transactions Are Susceptible to Hacker:** No matter how much precautions banks take to provide a secure network; online banking transactions are still susceptible to hackers. Irrespective of the advanced encryption

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methods used to keep user data safe, there have been cases where the transaction data is compromised. This may cause a major threat such as using the data illegally for the hacker's benefit.

- **Difficulty for Beginner:** As there are people who are far away from the web of internet. It is a whole new deal for them to learn how net banking works. Worse still, if there is nobody who can explain them on how internet banking works and the process flow of how to go about it. It will be very difficult for inexperienced beginners to figure it out for themselves.
- **Securing Password:** Every internet banking account requires the password to be entered in order to access the services. Therefore, the password plays a key role in maintaining integrity. If the password is revealed to others, they may utilise the information to devise some fraud. Password is one of the important things as password theft may occur so one must frequently change our password to avoid any possible fraud.

2.3.4 *RTGS*

As the name suggests, immediate transfer of funds and/or securities takes place. RTGS means Real Time Gross Settlement. This too is an electronic route of funds transfer. It is actually a continuous process of settling the payments. Transactions are handled individually and not grouped together. It is primarily for huge bank to bank transfers, operated under the watchful eyes of the central bank. Once the transactions are completed, they cannot be reversed.

2.3.5 *NEFT*

The full form of NEFT is National Electronic Funds Transfer. As the name suggests, it is a nationwide platform for making payment. It is quite easy to use, and no physical transfer is involved so the risk and inconvenience associated with it are avoided. Due to the penetration of online banking in the country it is also gaining in popularity. To avail this service the bank IFSC code needs to be mentioned along with the name of the account holder, account number and the name and branch of the bank to which the funds need to be transferred.

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2.3.6 *IMPS*

Also called as Immediate Payment System, it is a service by the bank. It was a pilot mobile payment system initially and offers quick electronic funds transfer service through mobiles.

Mobile banking or SMS are utilized for this, and accounts can be accessed using mobiles. To use this service the customer must first register with the IMPS service of the bank. It is very convenient for the user and a quick method of fund transfer.

2.3.7 *ATM*

Popularly called in layman's language as Any Time Money, it actually stands for Automated Teller Machine. As the name means, it is a machine that helps to manage the money of the account holder. Payments and Deposits can be made through this without visiting the bank branch. The user individually can gain access to his account to get updated about the latest amount in his account, For money transactions either a debit card or credit card is used, and PIN authentication might be needed in certain cases.

2.3.8 *Debit and Credit Cards*

A debit card is a cashless route of making payment. It debits money from a customer's account directly when it is used. It may be used to buy products and services and to make payments or for cash withdrawing form ATMs. Unlike credit cards the customer cannot use more than what is available in their account. So, that limitation is there and is an advantage or disadvantage as per the view of the customer.

To use these unlike credit cards, the user does not have to pay any fees or charge.

Credit Cards on the other hand are cards used for payment like debit cards, but the user has to promise the card issuing authorities that payment and other charges levied will be processed. The card issuing authority gives a line of credit to the card user through which the payment can be made

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for purchase of products and services. The issuing authorities also enter into agreements with sellers to accept these cards as mode of payment. Through electronic verification the seller can verify that the card is valid and acceptable as a mode of payment

2.3.9 *APP Based Payment System*

You have seen the rise in the number of consumers using Apps on their mobiles or computers for making payments, be it everyday articles like ready-to-eat food, stationery etc. or durables like footwear, mobiles etc. It is interesting to note how this work. While using the app to send your card information through the App to the payment gateway, which in turn sends the information to the card issuing bank, which sends the request to your payment system like Mastercard, VISA etc. After that your reputation is analyzed along with terms and conditions. Then an authorization code is sent to complete the payment and if all goes well, money is transferred to the seller's bank account.

All this takes place in a few seconds, subject to internet speed. You are also able to track the status of your purchase online.

Figure 2.1

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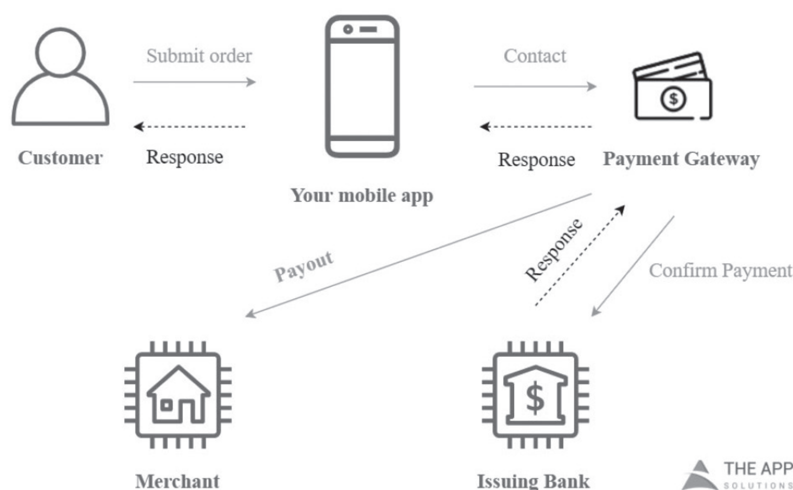

Figure 2.2

Two kinds of products are on offer - virtual goods and physical goods. Also, with this money can be transferred from one account to another as well as services can be availed.

2.3.10 *UPI*

UPI refers to unified payment interface. It allows smartphone to be used as virtual debit card. It allows instant money transfer. Real-time bank-to-bank payments can be made using a mobile number or virtual payment address (UPI ID).

UPI is an initiative taken by the National Payments Corporation of India (NPCI) together with the Reserve Bank of India and Indian Banks Association (IBA). NPCI is the firm that handles RuPay payments infrastructure, i.e., similar to Visa and Mastercard. It allows different banks to interconnect and transfer funds. Immediate Payments Service (IMPS) is also an initiative of NPCI. UPI is considered as the advanced version of IMPS.

UPI ID is unique identification of bank account that can be used to send and receive money. UPI pin is 4-digit number that can be chosen by account holder.

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How UPI Works?

UPI uses existing systems, such as Immediate Payment Service (IMPS) and Aadhaar Enabled Payment System (AEPS), to ensure seamless settlement across accounts. It facilitates push (pay) and pull (receive) transactions and even works for over-the-counter or barcode payments, as well as for multiple recurring payments such as utility bills, school fees, and other subscriptions.

Once a single identifier is established, the system allows mobile payments to be delivered without the use of credit or debit cards, net banking, or any need to enter account details. This would not just ensure greater safety of sensitive information, but connect people who have bank accounts via smartphones to carry out hassle-free transactions. Overall, UPI implies fewer cash transactions and potentially reduces the unbanked population.

Services offered by UPI are Users can access balances and transaction histories along with sending and receiving money. To send money, users need an account number, the Indian Financial System Code (or IFSC, which is an alphanumeric code that facilitates electronic transfers), the mobile number of the recipient, and a virtual ID or Aadhaar number (which is like a Social Security number).

Benefits of UPI Benefits for Banks:

- Single-click Two Factor authentication
- Universal Application for transaction
- Leveraging existing infrastructure
- Safer, secured and innovative
- Payment basis Single/Unique Identifier
- Enable seamless merchant transactions

Benefits for End Customers:

- Round-the-clock availability
- Single Application for accessing different bank accounts
- Use of Virtual ID is more secure, no credential sharing
- Single click authentication
- Raise Complaint from Mobile App directly

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Benefits for Merchants:

- Seamless fund collection from customers - single identifiers
- No risk of storing customer's virtual address like in Cards
- Tap customers not having credit/debit cards
- Suitable for e-Com & m-Com transaction
- Resolves the COD collection problem
- Single click 2FA facility to the customer - seamless Pull
- In-App Payments (IAP)

UPI transactions are highly secure and cannot be tempered. It uses a two-factor authentication method, similar to OTP, for verifying every transaction. There are many apps coming up every day that supports UPI payments, such as Google Pay, PhonePe, and others. You need to verify your bank account information to generate UPI ID on the app before you begin transactions.

2.3.11 *Digital Wallets*

A digital wallet (or e-wallet) is a software-based system that securely stores users' payment information and passwords for numerous payment methods and websites. By using a digital wallet, users can complete purchases easily and quickly with near-field communications technology. They can also create stronger passwords without worrying about whether they will be able to remember them later.

Digital wallets can be used in conjunction with mobile payment systems, which allow customers to pay for purchases with their smartphones. A digital wallet can also be used to store loyalty card information and digital coupons.

E-wallet is a type of electronic card which is used for transactions made online through a computer or a smartphone. Its utility is same as a credit or debit card. An E-wallet needs to be linked with the individual's bank account to make payments. An E-wallet is protected with a password. With the help of an E-wallet, one can make payments for groceries, online purchases, and flight tickets, among others. E-wallet has two component software and information, software component store information related to password, encryption etc whereas information contain information such

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as billing address, payment method, mode of payment etc. some of top digital wallets are Due, Apple Pay, Google Wallet, Samsung Pay, PayPal, Venmo, AliPay, Walmart Pay, Dwolla, Vodafone-M-Pesa. Recently, Google combined its two essential payment streams (Android Pay and Google Wallet) into a single service called Google Pay. Apple on the other hand entered into a strategic partnership with Goldman Sachs to issue Apple credit cards and expand its Apple Pay services.

2.4 Ponzi Schemes

Ponzi Schemes

- A Ponzi scheme is a fraudulent investing scam promising high rates of return with little risk to investors. Companies that engage in a Ponzi scheme focus all of their energy into attracting new clients to make investments.
- A Ponzi scheme is an investment fraud that pays existing investors with funds collected from new investors. Ponzi scheme organizers often promise to invest your money and generate high returns with little or no risk. But in many Ponzi schemes, the fraudsters do not invest the money. Instead, they use it to pay those who invested earlier and may keep some for themselves.
- With little or no legitimate earnings, Ponzi schemes require a constant flow of new money to survive. When it becomes hard to recruit new investors, or when large numbers of existing investors cash out, these schemes tend to collapse.
- Ponzi schemes are named after Charles Ponzi, who duped investors in the 1920s with a postage stamp speculation scheme.

Features of Ponzi Schemes

1. **A Guaranteed Promise of High Returns with Little Risk:** Every investment carries some degree of risk, and investments yielding higher returns typically involve more risk. Be highly suspicious of any "guaranteed" investment opportunity**.**
2. **A Consistent Flow of Returns Regardless of Market Conditions:** Investments tend to go up and down over time. Be sceptical about an investment that regularly generates positive returns regardless of overall market conditions.

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3. **Investments that have not been Registered with the Securities and Exchange Commission (SEC):** Ponzi schemes typically involve investments that are not registered with the SEC or with state regulators. Registration is important because it provides investors with access to information about the company's management, products, services, and finances.
4. **Investment Strategies that are Secret or Described as too Complex to Explain:** Avoid investments if you don't understand them or can't get complete information about them.
5. **Clients not allowed to View Official Paperwork for their Investment:** Account statement errors may be a sign that funds are not being invested as promised**.**
6. **Clients Facing Difficulties Removing their Money:** Be suspicious if you don't receive a payment or have difficulty cashing out. Ponzi scheme promoters sometimes try to prevent participants from cashing out by offering even higher returns for staying put.

Security and Precaution against Ponzi Schemes

1. **Be Cautious:** If someone tries to sell you on an investment that has huge and/or immediate returns for little or no risk, it could well involve some sort of fraud.
2. **Be Aware:** Someone contacting you unexpectedly, perhaps inviting you to an investment seminar, is often a red flag. Investment scams often target elderly people, or those close to or in retirement**.**
3. **Check out the Seller:** verify the professional licence of investment proposal seller and cautious about any negative information.
4. **Verify the Investment Register:** Ponzi schemes are often unregistered at security and exchange commission of India.
5. **Understand the Investment:** Never invest in scheme that you do not understand or having doubt about it. Don't write a check to – or open an account with – anyone who won't fully answer your questions.
6. **Report any Wrongdoing:** If you come across any fraudulent scheme do report it to regulatory authority like SEBI i.e., securities and exchange board of India, Investment regulatory authority of India, the Reserve Bank of India.

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2.5 Online Frauds

Online Frauds

Fraud that is committed using the internet is "online fraud." Online fraud can involve financial fraud and identity theft. Online fraud comes in many forms. It ranges from viruses that attack computers with the goal of retrieving personal information, to email schemes that lure victims into wiring money to fraudulent sources, to "phishing" emails that purport to be from official entities (such as banks or the Internal Revenue Service) that solicit personal information from victims to be used to commit identity theft, to fraud on online auction sites (such as eBay) where perpetrators sell fictional goods.

Type of Online Frauds

Some of online fraud are explained below:

Phishing

Phishing attacks attempt to gain sensitive, confidential information such as usernames, passwords, credit card information, network credentials, and more. By posing as a legitimate individual or institution via phone or email, cyber attackers use social engineering to manipulate victims into performing specific actions—like clicking on a malicious link or attachment—or wilfully divulging confidential information. In addition, some phishing scams can target organizational data in order to support espionage efforts or state-backed spying on opposition groups. Because these sites often look "official," they hope you'll be tricked into disclosing valuable information that you normally would not reveal. This often times, results in identity theft and financial loss.

Spyware and viruses are both malicious programs that are loaded onto your computer without your knowledge. The purpose of these programs may be to capture or destroy information, to ruin computer performance or to overload you with advertising. Viruses can spread by infecting computers and then replicating. Spyware disguises itself as a legitimate application and embeds itself into your computer where it then monitors your activity and collects information.

Fraudulent "Pop-up Windows" are a type of online fraud often used to obtain personal information. They are the windows or ads that appear

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suddenly over or under the window you are currently viewing. Fraudulent websites or pop-up windows are used to collect your personal information. Other terms for the fraudulent process of gathering your personal information include "Phishing or "Spoofing." Additional links to real websites can be incorporated into the email to lead you to believe the email is legitimate.

Credit Card Cloning or Skimming

Credit card cloning means unauthorised copying of credit cards. It also refers to as skimming and requires copying information at a credit card terminal using an electronic device or software, then transferring the information from the stolen card to a new card or to rewrite an existing card with the information. Unfortunately, cloning and related forms of theft have become increasingly widespread in recent decades. Thankfully, security improvements such as the use of personal identification numbers (PINs) and chip cards have helped to protect against these types of attacks.

Modern chip cards—which have embedded microchips that contain their sensitive information—are much harder to compromise because the data they contain is encrypted within the chip itself. This means that even if the thieves successfully access the chip card, they would not be able to use the information they stole some examples of cloning are installing hidden scanners onto legitimate card-reading devices such as gas station pumps, automated teller machines (ATMs), or the point-of-sale (POS) machines common in most retail stores.

Fraudulent Websites, e-mails or pop-up Windows will Often:

- Ask you for personal information (Account number, Social Security Number, Date of Birth, etc.).
- Appear to be from a legitimate source (Retail Stores, Banks, Government agencies, etc.).
- Contain prizes or other types of certificate notices.
- Link to other real or counterfeit websites.
- Contain fraudulent phone numbers.

Pop-up windows are often the result of programs installed on your computer called "adware" or "spyware." These programs look in on your Web viewing activity and regularly come hidden inside many free downloads, such as music-sharing software or screen savers. Many of these programs

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enable harmless advertisements, but some contain "Trojan horse" programs that can record your keystrokes or relay other information to an unauthorized source.

2.6 Protection Against Online Frauds

With proper precaution you can protect yourself from these frauds:

1. Know the Scam

(a) Phishing, Spoofing, Pop-up Fraud – Types of online fraud used to obtain personal information.

(b) Trojan Horse – Virus that can record your keystrokes. It can live in an attachment or be accessed via a link in the email, website or pop-up window.

(c) Counterfeit Websites – URLs that forward you to a fraudulent site. To validate a URL, you can type or cut and paste the URL into a new web browser window and if it does not take you to a legitimate web site or you get an error message, it was probably just a cover for a fraudulent web site.

2. Activate a pop-up Window Blocker

There are free programs available online that will block pop-up windows. Be sure to perform an Internet search for "pop-up blocker" or look at the options provided by major search engines. You will need to confirm that these programs are from legitimate companies before downloading. Once you have installed a pop-up blocker, you should determine if it blocks information that you need to view or access. If this is the case, you should consider turning off the blocker when you are on Web sites you know use pop-up windows to provide information you need or want to view.

3. Scan your Computer for Spyware Regularly

You can eliminate potentially risky pop-up windows by removing any spyware or adware installed on your computer. Spyware and adware are programs that look in on your Web viewing activity and potentially relay information to a disreputable source. Perform an Internet search for "spyware" or "adware" to find free spyware removal programs. As with

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a pop-up blocker, you will want to be sure that your removal program is not blocking, or removing, wanted items, and if it is, consider turning it off for some websites.

- **Avoid Downloading Programs from Unknown Sources:** Downloads may contain hidden programs that can compromise your computer's security. Likewise, email attachments from unknown senders may contain harmful viruses.
- **Keep your Computer Operating System and Internet Browser Current Safe.**
- **Keep your Passwords Secret:** Change them regularly, using a mixture of numbers and characters.

4. Measure Taken by Government to Tackle Online Frauds

Central Government has taken steps to spread awareness about cybercrimes, issue of alerts/advisories, capacity building/training of law enforcement personnel/ prosecutors/judicial officers, improving cyber forensics facilities etc. to prevent such crimes and to speed up investigation. The Government has launched the online cybercrime reporting portal, www. cybercrime.gov.in to enable complainants to report complaints pertaining to Child Pornography/Child Sexual Abuse Material, rape/gang rape imageries or sexually explicit content. The Central Government has rolled out a scheme for establishment of Indian Cyber Crime Coordination Centre (I4C) to handle issues related to cybercrime in the country in a comprehensive and coordinated manner.

5. Further Steps Taken by GOI:

(i) Establishment of National Critical Information Infrastructure Protection Centre (NCIIPC) for protection of critical information infrastructure in the country.

(ii) All organizations providing digital services have been mandated to report cyber security incidents to CERT-In expeditiously.

(iii) Cyber Swachh Kendra (Botnet Cleaning and Malware Analysis Centre) has been launched for providing detection of malicious programmes and free tools to remove such programmes.

(iv) Issue of alerts and advisories regarding cyber threats and counter-measures by CERT-In.

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(v) Issue of guidelines for Chief Information Security Officers (CISOs) regarding their key roles and responsibilities for securing applications/ infrastructure and compliance.

(vi) Provision for audit of the government websites and applications prior to their hosting, and thereafter at regular intervals.

(vii) Empanelment of security auditing organisations to support and audit implementation of Information Security Best Practices.

(viii) Formulation of Crisis Management Plan for countering cyber-attacks and cyber terrorism.

(ix) Conducting cyber security mock drills and exercises regularly to enable assessment of cyber security posture and preparedness of organizations in Government and critical sectors.

(x) Conducting regular training programmes for network/system administrators and Chief Information Security Officers (CISOs) of Government and critical sector organisations regarding securing the IT infrastructure and mitigating cyber-attacks.

IN-TEXT QUESTIONS

1. What is Net Banking?

(a) Internet Shopping

(b) Online Banking

(c) Social Media Networking

(d) Video Streaming

2. Which of the following is a primary advantage of Net Banking?

(a) Limited Access to Funds

(b) Convenience of 24/7 Banking

(c) Manual Transaction Processing

(d) No Security Features

3. What is the purpose of a One-Time Password (OTP) in Net Banking?

(a) To reset the computer

(b) To access social media accounts

(c) To authenticate transactions

(d) To unlock the Internet browser

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4. Which of the following is NOT typically a feature of Net Banking?

(a) Fund Transfer

(b) Bill Payment

(c) In-Person Branch Visits

(d) Account Balance Inquiry

5. Which financial activities can be performed through Net Banking?

(a) Ordering Pizza

(b) Booking Movie Tickets

(c) Loan Approval

(d) All of the Above

6. What is the purpose of a Virtual Keyboard in Net Banking?

(a) Playing Online Games

(b) Enhancing Security During Login

(c) Virtual Shopping

(d) Sending Emails

7. What does the term "Phishing" refer to in the context of Net Banking?

(a) A type of fishing

(b) Unauthorized access to online accounts

(c) Sending fake emails to obtain sensitive information

(d) Buying online products

8. What should users do if they suspect unauthorized access to their Net Banking account?

(a) Share the details on social media

(b) Ignore it, as it may be a mistake

(c) Immediately contact the bank and change passwords

(d) Delete the Net Banking account

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2.7 Handling Banking Complaints

If any customer is not satisfied with any service of the bank, a complaint can be filed on plain paper or on the portal. For this the banking Ombudsman needs to be contacted. The complaint should have the contact details of the complainant, and the bank, facts as per the complainant, loss if any suffered, and if any relief is required. This needs to be done only when the bank has rejected the complaint or has not responded to the complaint, or if the complaint is not satisfied by the bank's response or there is a delay as specified by the RBI. In this case the complainant or an authorized representative can contact the Ombudsman. Customers can contact the Digital Complaint Management System Portal for any banking, NBFC or even digital related issues.

Banking Ombudsman

In 1995, to protect the consumers against unfair practice by the banks, the RBI introduced the Banking Ombudsman scheme. The RBI has appointed officers to act as banking Ombudsman for speedy resolution of complaints against banks. If in case the reply from the bank is not received within 30 days or the complaint is rejected by the bank the customer can file, the complaint with the banking Ombudsman.

2.8 Summary

In the current age of digitalization, banks are swiftly moving towards online and mobile platforms to offer an enhanced banking experience to their customers. Consequently, it is becoming increasingly vital for consumers to familiarize themselves with the latest banking terminologies and cutting-edge technologies to stay abreast of these advancements. It is equally crucial for customers to understand their rights and responsibilities when it comes to addressing any issues they may face with the bank's services and filing complaints if necessary. By staying informed and proactive, you can ensure a seamless and hassle-free banking experience that meets all your needs and expectations. Thus, this chapter provides detailed information about the digitalization of financial transactions, their types (UPI, digital wallets, net banking, debit card, credit cards etc.). It also gives a brief overview of online frauds and precaution required.

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2.9 Answers to In-Text Questions

1. *(b)* Online Banking
2. *(b)* Convenience of 24/7 Banking
3. *(c)* To authenticate transactions
4. *(c)* In-Person Branch Visits
5. *(c)* Loan Approval
6. *(b)* Enhancing Security During Login
7. *(c)* Sending fake emails to obtain sensitive information
8. *(c)* Immediately contact the bank and change passwords

2.10 Self-Assessment Questions

1. What do you understand by cashless banking?
2. What are the features of net banking and its disadvantages?
3. Differentiate credit cards from debit cards.
4. What is UPI?
5. Discuss the Ponzi Schemes and online frauds.

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UNIT - III

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L E S S O N

1

Investment Opportunity and Financial Products

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STRUCTURE

1.1 *Learning Objectives*
1.2 *Introduction to Investment*
1.3 *Direct and Indirect Investing*
1.4 *Investment in Equity and Debt Instruments*
1.5 *Financial Derivative*
1.6 *Mutual Funds*
1.7 *Latest Developments Regarding Mutual Funds*
1.8 *Summary*
1.9 *Answers to In-Text Questions*
1.10 *Self-Assessment Questions*
1.11 *References*
1.12 *Suggested Readings*

1.1 Learning Objectives

- Understanding the concept of Investment.
- Understanding the difference between Real and Financial Investment.
- Learning the features and objectives of Investment.
- Understanding the different types of financial instruments: equity, debt, financial derivative, mutual funds, ETF etc.

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1.2 Introduction to Investment

Investment is backbone of any economy. Saving of an economy must be channelised into productive investment to increase income level. The higher investment will positive outcome like higher gross national income and economic growth. A good business environment is prerequisite for higher investment and for boasting the morale of investor. The primary investment is channelised through household saving. These are channelised into more productive investment to get higher income. An individual can put his money into saving account or invest into financial market product like equity, debt, mutual fund, or real estate. Therefore, an individual must be financial literate. This chapter will provide an insight to it.

An investment is an asset or item acquired with the goal of generating income or appreciation. Appreciation refers to an increase in the value of an asset over time. When an individual purchases a good as an investment, the intent is not to consume the good but rather to use it in the future to create wealth. An investment always concerns the outlay of some asset today—time, money, or effort—in hopes of a greater payoff in the future than what was originally put in. Investment not always guarantee higher return but at time we also incur losses, investment environment is quite uncertain. We are in fact facing VUCA (volatility, uncertainty, complex, ambiguous) environment in context of investment.

For example, in 1986 Microsoft corporation offer its first stock and in 10yr it has grown 5000% on the other hand worlds of wonder also offer stock in same year and 10 years later the company become defunct.

1.2.1 *Financial Investment v/s Real Investment*

Financial assets are tangible assets that you can quickly convert into cash. Stocks, bonds, cash reserves, bank deposits, trade receivables, notes receivable and shares are all common examples of financial assets. These are tangible or liquid assets that actually represent claims on the underlying value of the other types of assets such as real estate and properties.

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The main characteristic of a financial asset is that it has some type of monetary value, but that value is not tangible until it's exchanged for cash. Financial assets also have classifications such as equities and fixed income securities. Equities are shareholding rights to a business, and they are issued either as common shares or preferred stock. Unlike preferred stock, common shares carry voting rights. Fixed income securities are instruments of borrowing that earn fixed rates of interest over a specified duration. Public institutions issue some types of fixed income securities, while others are issued by private entities. Examples include treasury, municipal and corporate bonds. And when you invest in these assets it is referred to as **financial investment.**

The real assets definition refers to value-generating physical assets that your business owns. Common examples include land, buildings, inventory, precious metals, commodities, real estate, land and machinery. These physical assets are important for your business because they carry some type of intrinsic value. Intrinsic value is defined as the exact value of an asset as determined by factors such as location, function and acquisition costs. When you invest in this type of asset it is referred to as **real investment**

1.2.2 *Objective of Investment*

A person make investment in order to accomplish certain objective. People forego current consumption in order to avail higher return. Ultimate objective of investment is to minimize risk and maximize return. Nothing can be risk free in this world, risk and return goes hand in hand, higher the risk higher will be return. Some of the objective that is kept in mind before making an investment are as follows:

- **Capital Appreciation:** Capital appreciation is concerned with long-term growth and is most common in retirement plans where investments work for many years inside a qualified plan, such as a 401(k) or IRA. However, investing for capital appreciation is not limited to qualified retirement accounts. This objective involves holding stocks for many years and letting them grow within your portfolio while reinvesting dividends to purchase more shares.

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For example: Let's imagine that you make an initial $1,000 investment and add $100 monthly for the next 20 years. The total amount contributed during that period would be $25,000. However, if your investments generate an 8% return annually, compound interest will place your total savings at $59,575.31. Investors using the capital appreciation strategy are not concerned with day-to-day fluctuations. However, they keep a close eye on the fundamentals of the company for changes that could affect long-term growth. A typical strategy involves regular purchases.

- **Current Income:** The current income involves investing in stocks that pay a consistent and high dividend, as well as some top-quality real estate investment trusts (REITs) and highly rated bonds because these products produce regular current income. People concerned with current income should consider investing in blue-chip stocks, which are shares in large, prominent corporations that have shown a long history of growth and consistent dividend pay outs**.** Many people who focus on current income are retired and use the income for living expenses. In contrast, others take advantage of a lump sum of capital to create an income stream that never touches the principal yet provides cash for certain current needs—such as college tuition.
- **Capital Preservation:** Capital preservation is often associated with retired or nearly retired people who want to make sure they don't outlive their money. For this investor, safety is critical—even if it involves giving up return potential for security. The logic for this safety is clear: A retiree who loses money through unwise investments is unlikely to get a chance to replace it. Younger investors can have a stock-dominated portfolio because they have many years to recover from any losses that may occur due to market changes or economic downturns. This isn't the case for older individuals. Investors who want capital preservation tend to invest in bank CDs, U.S. Treasury issues, and savings accounts because they offer modest returns but possess much less risk than stocks.
- **Speculation:** The speculator is not a true investor, but a trader who enjoys jumping in and out of stocks for capital gain. Speculators

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or traders are interested in quick profits and use advanced trading techniques like shorting stocks, trading on the margin, options, and other special methods. Speculators have no real attachment to the companies they trade, and they may not know much about the underlying business except that the stock is volatile and ripe for a quick profit.

Many people try speculating in the stock market with the misguided goal of getting rich, and the overwhelming majority fail at doing so. If you want to try your hand, make sure you are using money you can afford to lose without jeopardizing your livelihood or retirement ambitions. It's easy to get a false sense of competence after initial success, so thoroughly understand the real possibilities of losing your investment. However excessive speculation is bad as it takes away from their true fundamental values. Therefore, SEBI keeps check on excessive speculation under SEBI act 1992.

Table: Speculation vs Investment

S. No.	Basis of difference	Investment	Speculation
1.	◆ Time horizon	◆ Long, generally exceeding one year.	◆ Short may be as short as intra-day.
2.	◆ Risk	◆ Low to moderate.	◆ Very high.
3.	◆ Funds	◆ Here own funds are used for investment.	◆ Speculator also borrow funds and/or do margin trading.
4.	◆ Return (expected)	◆ Low to moderate and consistent.	◆ Very high and inconsistent.
5.	◆ Income	◆ Dividend, interest etc.	◆ Change in price of asset.
6.	◆ Source of information	◆ Fundamental factor of the company is analysed.	◆ Herd instincts, inside information.

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1.3 Direct and Indirect Investing

Direct Investing involves purchase and sale securities by investors themselves. In this case the investor has entire control over the investment decision that is which security is need to be purchased or sold as well as when to purchase or sell. The securities may be securities of capital market (such as equity share, bonds or debentures) or derivative market (such as treasury bills, certificate of deposits, commercial papers). The investor is required to perform all task of investment decision making process. Therefore, direct investing involves expertise and investing skills. Moreover, it is a time-consuming process of investing. In case of direct investment, the cost of analysis and monitoring is incurred by the investor directly.

Indirect Investing involves investing in mutual funds (open ended as well as close ended funds), exchange -traded funds or collective investment schemes including alternative investment funds (such as venture capital fund, hedge funds, REITs SME fund). In this case, the investor does not invest directly in various securities. He has no control over the composition of the fund's investment, investor only controls whether to buy or sell the shares or units of fund. Therefore, investor only decide in which mutual fund or investment company to invest in the finale investment decision is made by the fund or investment company in case of indirect investing. The investor buys or sell units (shares) of fund, which in turn makes investment in securities and build up portfolio as per the investment objective of fund or scheme. The investor becomes unit holder in the fund and has ownership interest in the asset of the fund or investment company and is entitled to interest or dividends and price appreciation or decline. Thus, indirect investing in a mutual fund, ETF or investment company or even in alternative investment funds, is an alternative route for investor to invest.

It is convenient and ideal form of investing for investor who are not skilled enough or who do not have time to perform security analysis and portfolio management process, in case of investment in mutual fund or any other type of investment company, the investment costs are incurred by fund or company but ultimately these costs are passed on to investor in terms of management fee or expenses. These expense or fees reduces the value of portfolio or investment done by fund or company.

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Tabular Presentation of Difference between Direct and Indirect Investing

	Direct investing	Indirect investing
Meaning	◆ Direct investing involves purchase or sale of securities by the investors themselves.	◆ Indirect investing means investment in mutual funds or other investment companies rather directly in securities.
Instruments of investment	◆ Capital market such as equity, shares, bonds, debentures etc. Money market such as treasury bills, certificates of deposits, commercial paper etc. Derivative market such future and option.	◆ Mutual funds-open ended and close ended. Exchange traded funds. Collective investment schemes. Alternative investment funds-such as venture capital funds, hedge funds, ME funds, Real Estate Investment Trusts (REITs) etc.
Control	◆ Investor has entire control over investment decision i.e., which securities are need to be purchased or sold.	◆ Fund or investment company has direct control over the investment decision i.e., which securities need to be purchased and sold as well as when to purchase or sold.
Costs	◆ Cost of monitoring and analysis is born by investor directly.	◆ Cost is incurred by fund houses or investment company but they are ultimately transferred to investor in the form of management fee.

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	Direct investing	Indirect investing
Skills and time	◆ Direct investing requires investing skills and expertise. Moreover, it is time consuming process of investing by individual investor.	◆ Indirect investing does not require investing skills and expertise by the individual investor. The fund or investment company where investor invests is expected to provide such expertise and professional fund management. They have professional fund managers.
Convenience	◆ Direct investing may not be convenient to small investors who do not possess requisite investing skills and who do not have much time to perform security analysis.	◆ Indirect investing is very convenient and preferred mode of investment to small investors who do not possess requisite investing skills and do not have much time to perform security analysis.

1.4 Investment in Equity and Debt Instruments

Investment in equity and debt instruments in India can be a lucrative opportunity for those looking to grow their wealth. Equity instruments include stocks, shares, and mutual funds, while debt instruments include fixed deposits, bonds, and government securities. When investing in equity instruments, it's important to carefully research and analyze the companies and funds you're considering and to diversify your portfolio to minimize risk. On the other hand, debt instruments are generally considered to be lower risk, but also offer lower returns.

It's important to note that investing in any instrument involves risk, and it's important to consult with a financial advisor before making any investment decisions. Additionally, it's important to stay up to date with

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the latest market trends and news to make informed investment decisions. The main difference between equity investment and bond investment lies in the type of instrument being invested in and the manner in which the investor earns returns. Equity investment involves buying ownership in a company by purchasing stocks or shares. When you invest in equity, you become a part owner of the company and have a claim on its profits. The returns on equity investments are typically in the form of dividends and capital gains, which are dependent on the performance of the company. Equity investments are generally considered to be higher risk, but also offer potentially higher returns.

Bond investment, on the other hand, involves buying debt securities issued by a company or government. When you invest in bonds, you are essentially lending money to the issuer and earning interest on your investment. Bonds are typically considered to be lower risk investments compared to equity, but also offer lower returns. It's important to note that both equity and bond investments involve risk, and the returns are subject to market fluctuations. It's important to consult with a financial advisor and conduct thorough research before making any investment decisions.

1.5 Financial Derivative

Derivatives are financial instruments whose value depends upon or derived from some underlying asset. The underlying asset can be real asset such as commodities, gold etc. or financial asset such as index, interest rate etc. A derivative does not have its own physical existence. It emerges out of a contract between buyer and seller of derivative instrument. Its value depends upon the value of the underlying asset. Hence the return from derivative instrument depends upon the return from underlying assets. Nowadays we find derivatives based on other derivatives. The derivative itself is merely a contract between two parties.

Derivative Includes:

(a) A security derived from a debt instrument, share, loan, whether secured or unsecured, risk instrument or contract for differences or any other form of security

(b) A contract which derives its value from the prices or index of prices, of underlying securities

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1.5.1 *Classification of Derivative*

Derivatives can be classified into broader category based upon underlying asset, nature of derivative contract or the trading of derivative contract.

- **Commodity Derivative or Financial Derivative:** Derivative can be classified into financial derivative or commodity derivative based upon the underlying asset. In case of commodity derivative, the underlying asset is physical or real asset such as wheat, rice, jute, pulses, or even metal such as gold, silver, copper, etc.

  In case of financial derivative, the underlying asset is financial asset such as equity share, bonds, debenture, stock index etc. The financial derivative is more popular around the world. The commodity derivative is traded on multi commodity exchange (MCX) and the national commodities and derivatives exchange (NCDEX) In India.

  Financial derivatives are traded on BSE, NSE, United stock exchange (USE) and MCX-SX in India.
- **Elementary Derivatives and Complex Derivatives:** Elementary derivative are those derivatives which are simple and easily understandable. Such derivative are futures and options. Complex derivative has complex provisions and features which make them difficult to understand by investor. Complex derivatives include exotic options, synthetic futures and options.
- **Exchange Traded Derivatives and Over the Counter (OTC) Derivative:** Derivative may be traded on exchange, or they may be privately traded over the counter (OTC), exchange traded derivative are standardised derivative product traded as per rules and regulations of exchanges of the exchange. For example, stock index future, stock index options and stock futures. OTC derivative are private bilateral contracts between two parties and are non-standardised. These derivatives are specific to the needs of parties involved. For example, forward contracts in foreign exchange market are OTC derivatives.

1.5.2 *Participants (or Trader) in Derivatives Market*

There are many parties in derivative market and make it liquid and smooth market. Derivative were initially developed to provide hedging

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against price risk. There are three kind of traders in derivative markets: hedgers, speculators and arbitrageurs.

Hedgers: Investors having long position in market are exposed to price risk i.e., the risk that asset prices will go down. On the other hand, the investor having short position in asset are exposed to price risk i.e., the price of asset may go up. Hence, they want to hedge their position against price risk. Hedgers use financial derivatives to reduce or eliminate the risk associated with the price of an asset. In hedging risk is actually transferred from hedger to the speculator. Options are widely used by hedgers to reduce their risk exposure.

Speculators: Speculators use derivatives to get extra leverage and earn quick gain on the basis of future movements in price of asset. They can increase both the potential gain or potential losses by usage of derivatives in a speculative venture. Futures are widely used by speculator. If a speculator expects that stock price will go up, he buys futures and vice versa.

Arbitrageurs: Arbitrageurs are those who take advantage of any discrepancy in pricing and exploit it to bring equilibrium. They take advantage of price discrepancy in two markets.

1.5.3 *Type of Financial Derivative*

Financial derivatives are those whose underlying asset is the financial asset or instrument such as index, stock, bonds, currency etc. Financial derivative are generally classified as forward, futures, options and swaps.

1.5.3.1 *Forwards*

A forward contract is a private bilateral agreement between two parties to buy and sell a specified asset at a specified price on specified future date.

For example, Mr. X grows 6000kg of wheat. He can sell this wheat at any price in future, but he has an option of getting the price fixed now by selling a forward contract that obligate him to sell 6000kg of wheat to Aashirvaad Atta after harvest for a fixed or specified price. By locking price now, he can eliminate the risk of falling price in near future, but if the prices rise in near future, then he stands at loss. Here Mr. X played safe and secure himself against the falling prices.

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Features of Forward Contract

- **Customised** – Each contract is customised designed, and parties may agree upon the contract size, expiration date, the asset type, quality etc.
- **Underlying Asset** – Underlying asset can be a stock, bond, commodity, foreign currency, interest rate or any combination thereof.
- **Symmetrical Rights and Obligation** – Both the parties to a forward contract have equal rights and obligations. The buyer is obliged to buy and seller is obliged to sell at maturity. They can also enforce each other to perform the contract.
- **Non Regulated Market** – Forward contract is usually made by private and large non – regulated consisting of banks, government, corporations and investment banks. It is not regulated by exchange.
- **Counter Party Risk or Default Risk** – This is risk of non-performance of obligation by either party as regard to payment (buyer) or delivery (seller). Being a private contract, there are chance of default or counter party risk.
- **Held Till Maturity** – The contract is generally held till maturity. A forward contract cannot be squared up at the wish of one party. It can be cancelled only with the consent of one party.
- **Liquidity** – Liquidation is low as contracts are customised catering to needs of parties involved. They are not traded on exchange.
- **Settlement of Contract** – Settlement of derivative can be in two ways- through delivery or through cash settlement. Most of forward contract are settled through delivery.

1.5.3.2 *Futures*

A future is a redefined or modified forward contract. A futures contract is a contract to buy or sell a specified asset (physical or financial asset) at a specified price at a specified date. It is traded on an exchange, and it is a standardised contract.

Features of Future Contract

- **Standardised Contract** – Terms and conditions of future contract are standardised. They are specified by exchange where they are traded.

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- **Exchange Based Trading** – Trading takes place on formal exchange which provides a place to engage in these transactions and sets a mechanism for parties to trade in these contracts.
- **No Default Risk** – The clearing house protects the parties from default by requiring the parties to deposit margin and settle gain or loss (mark to market their positions) on daily basis.
- **Liquidity** – Future contracts are highly liquid contracts as they are continuously traded on exchange. Any party can square off position any time.
- **Before Maturity Settlement Possible** – An investor can offset his future position by engaging in an opposite transaction before the stipulated maturity of contract.
- **Margin Requirement** – All the future contract have margin requirements. Margin money is required to be deposited with exchange by both the buyer as well as seller at the time of entering into contract. There are two type of margins – initial margin and maintenance margin. The margin account is settled on daily basis i.e., mark to market settlement. If margin amount falls below maintenance margin, then the variable call is made to replenish the margin amount to the level of initial margin.
- **Settlement Mechanism** – Settlement of derivative contract can be in two ways – through delivery or cash settlement.

Future Contract Terminology

- **Spot Price –** The price at which underlying asset are traded in the spot market.
- **Future Price –** The price which is agreed upon at the time of future contract for delivery at specified date.
- **Contract Cycle –** It is the period over which the contract trades on the exchange.
- **Expiry Date –** It is the last date on which the finale settlement takes place. Last Thursday of every month is expiry date for futures contracts if that day is holiday, then previous working day.
- **Contract Size or Lot Size –** The quantity of asset that has to be delivered under one contract.
- **Price Steps** – The minimum difference between two price quotes.

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- **Price Band –** The minimum and maximum price change allowed in a day is termed as price bands. It is generally ±10%. There are no day minimum/maximum price range applicable for CNX nifty futures contracts.

Comparison between Forwards and Futures

Basis	Forwards	Futures
Standardisation of Contract	◆ Forward contracts are private agreements between two parties and are non-standardised.	◆ Future contracts are exchange traded and standardised contracts are set in advance.
Trading and Regulation	◆ Forwards are not traded on stock exchange. They are not regulated.	◆ Futures are traded on stock exchange and are regulated.
Counter party Default Risk	◆ There is always a possibility that party may default.	◆ Clearing houses guarantee the transaction, thus minimising the default risk.
Liquidity	◆ Liquidity is low, as contracts are tailor – made contracts catering to the needs of parties involved. Further, they are not easily accessible to other market participants.	◆ Liquidity is high as contracts are standardised exchange- traded contracts.
Price Discovery	◆ Price discovery is not efficient as market are scattered.	◆ Price discovery is efficient as market are centralised.
Settlement	◆ Settlement of the forward contract occurs at the end of the contract i.e., settlement date only.	◆ Futures contracts are marked – to market on daily basis which means that they are settled day by day until the end of the contract.

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Basis	Forwards	Futures
Hedging/ Speculation	Forward contracts are popular among hedgers.	Futures are popular among speculators.
Margin Requirement	There is no requirement for depositing margin money by either party.	Both the buyer and seller have to deposit margin money with the exchange.
Example	Foreign currency market in India.	Commodities futures, index futures and individual stock futures in India.

1.5.3.3 *Options*

An option is a contract which gives the buyer (holder) a right (but not obligation) to buy or sell a specified asset at specified price (exercise price) on or before a specified future date. An option is a contract sold by one party (option writer) to another party (option holder). The holder of option can exercise the option at a specified price or may allow it to lapse.

This specified price is also known as strike price or exercise. The option contract gives right to buyer. The seller has obligation but no right. If the option holder exercises the option, then the writer or seller is obliged to perform. When option holder has right to sell, then option writer has obligation to buy. The option buyer has a privilege position. Since the buyer has right but no obligation, he has to pay some price, known as option premium to seller or writer of option. No right comes free of cost.

Comparison Between Futures and Options

Basis	Futures	Options
Right	◆ Both the parties have right to ask for performance of the contract.	◆ Only the buyer (or holder) of the options has a right to buy or sell. Seller do not have any right.
Obligation	◆ Both parties are obliged to perform the contract.	◆ Only the seller is obliged to perform the contract.

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Basis	Futures	Options
Premium payment	◆ No premium is paid by either party.	◆ The buyer pays the options premium to seller.
Margin requirement	◆ Both parties have to deposit some initial margin as per the requirement.	◆ Only the option writer has to deposit the initial margin with the exchanges as only seller is exposed to price risk. No margin is to be deposited by the option holder, as he has right but no obligation.
Profit and loss potential	◆ The gain to buyer is loss to the seller and the loss to the buyer is gain to the seller. There is unlimited gain and loss possibility for both the parties.	◆ The option holder's loss is limited (to the extent of premium paid) but has potential for upside profits. The seller's gain is limited to the amount of options premium, but he is exposed to all the downside risk.
Realisation of profit/ losses	◆ Profit and loss are 'marked to market' daily, meaning the change in the value of the position is attributed to the accounts of the parties at the end of every trading day-but a future holder can realise profits/ losses by going to the market and taking the opposite position.	◆ The gain of option can be realised in following ways: ◆ 1. Exercising the option at expiry. ◆ 2. Going to market and taking the opposite position. ◆ 3. Waiting until expiry and collecting the difference between asset price and the strike price.

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1.5.3.3.1 Types of Option

(a) **Call Option –** An option contract that gives its holder the 'right to buy' a specified asset at a specified price on or before a specified future date, is termed as call option. The seller has obligation to sell. A call option is bought when buyer has a rise in underlying asset's price. In such as the holder of the call option can buy the stock or asset at the exercise price which is lower than the market price. For example: assume current market price of SBI share is 120. Mr A expects that the price of share will go up, hence he buys a call option for SBI share at a price of 125. The expiry date is 2 months, and after two months the market price of SBI share is more then 125, say 130, then Mr A will exercise option at price of 125 and make a gain of RS 5.

(b) **Put Option** – A put option provides a right to sell. An option contract that gives its holder the 'right to sell' a specified asset at a specified price on or before a specified future date, is termed as put option. The seller has the obligation to buy. A put option is bought when the buyer of the put option fears a decline in underlying asset's price. A put option is exercised when the stock price is lower than the exercise price. For example: let us assume current SBI shares is Rs. 120. Mr. A assume that current price of SBI shares is Rs. 119. Mr A expects that price of SBI share will go down, hence he buys a put option on SBI at exercise price of Rs. 120. The expiration date is after 1 month. Further assume that option can be exercised only on the expiry date and note before that. Now on expiration date the market price of SBI is less than 120 say 117 then Mr A will exercise option.

1.5.3.3.2 Style of option

(a) **European Option –** A European style option can only be exercise on expiration date only**.**

(b) **American Option –** An American option can be exercised at any time before expiration or on the expiration date.

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IN-TEXT QUESTIONS

1. What is a financial derivative?

(a) A physical commodity

(b) A contract whose value is derived from an underlying asset

(c) A type of stock

(d) A government bond

2. Which of the following is a characteristic of a forward contract?

(a) Traded on organized exchanges

(b) Standardized terms

(c) Customizable terms between the parties

(d) Settled daily

3. What can be a common underlying asset for futures contracts from the followings?

(a) Real estate

(b) Foreign exchange

(c) Antique collectibles

(d) Rare gemstones

4. What is the primary purpose of using financial derivatives?

(a) To transfer risk

(b) To eliminate profits

(c) To increase volatility

(d) To encourage speculation

5. Which party has the right, but not the obligation, to buy or sell an underlying asset at a specified price in an options contract?

(a) Buyer of the option

(b) Seller of the option

(c) Both parties

(d) Government regulator

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6. What is the expiration date of a future contract?

(a) Set by the government

(b) Determined by the exchange

(c) Decided by the buyer

(d) Anytime the parties agree

7. In options trading, what is the premium?

(a) The maximum loss

(b) The upfront cost of the option

(c) The underlying asset

(d) The strike price

8. How do options differ from futures contracts?

(a) Options involve buying or selling of rights to one party only, while in future contract both parties have the obligation to complete the contract.

(b) Options contracts have standardized terms, while futures contracts are customizable.

(c) Options are traded on organized exchanges, while futures are traded over-the-counter.

(d) Options have no expiration date, while futures contracts do.

1.6 Mutual Funds

Mutual fund is financial intermediary that collects funds from individual investor and invests those funds in wide range of assets or securities. The individual investor has claim to the portfolio established by the mutual fund in the proportion of the amount invested, thereby becoming a part owner of assets of mutual funds. The fund employs professional experts and investment consultants who invest money in different stocks, bonds or other securities so as to meet the objective of the fund. The mutual fund manager charges fees from unit holder for administering the fund and managing the portfolio of investment. In India the mutual fund is required to get registered with Securities and Exchange Board of India (SEBI).

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1.6.1 *Establishment of Mutual Funds in India*

SEBI (Mutual Fund) Regulation, 1996 defines mutual fund as under:

Mutual fund means fund established in the form of trust to raise monies through the sale of units to the public or section of the public under one or more securities including money market instruments or real estate assets. Thus, mutual fund is established in the form of trust and this trust has following major constituents:

- **Sponsor:** It means any person who, acting alone or in combination with another body corporate, establishes a mutual fund. Sponsor is similar to promoter of a company.
- **Board of Trustees:** The board of trustees of the mutual fund hold its property for the benefit of unit holders. The board is vested with general power of superintendence and direction over asset management company. They are required to monitor the performance of mutual fund and ensure SEBI regulation by them. SEBI regulations require that at least two-thirds of trustee company must be independent i.e., that is they should not be associated with sponsor.
- **Asset Management Company (AMC):** AMC is a company established under company's act, 2013 and it is required approval of SEBI to be asset management company of mutual fund. SEBI require that 50% of the directors of AMC must be independent.
- **Custodian:** Custodian is required to be registered with SEBI. Custodian is appointed to keep custody of the securities or gold and gold related instrument or other related instrument of mutual fund and provide such other custodial services as may be authorised by the board of trustees.

1.6.2 *Advantages of Investing in Mutual Fund*

- **Professional Management:** The service of highly experienced and skilled professionals is backed up by a dedicated investment research team which first analyses the performance and prospects of companies and then invests accordingly.
- **Diversification:** Mutual fund invests in vide range of companies of different industries and sectors. Thus, investor enjoy the benefit

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of diversification with less money and less risk. However, it must be noted that sectoral funds such as IT funds, pharma funds etc. may not provide the benefit of diversification as all the stock in the portfolio of sectoral schemes belong to a particular sector.

- **Convenient Administration:** It reduces the amount of paper work. It helps investor to avoid many problems - like bad deliveries, delayed payment and unnecessary follow-up with brokers and companies.
- **Return Potential:** Mutual fund may provide higher returns in medium to long-term ass they invest in wide range of securities which is not possible to attain by small investor.
- **Low Costs:** Mutual fund is less expensive way of investing in comparison with direct investing. Indirect investing via mutual funds offers the scale in brokerage, custodial and other fees. All these benefits translate into low cost for investor.
- **Liquidity:** In open ended schemes, investor can get the money back instantly at the prevailing NAV. Also, in close – ended schemes, investors can sell their unit on stock exchange at the prevailing market price.
- **Transparency:** Investor regularly gets information about the value of their investment.

1.6.3 *Limitation of Investing in Mutual Fund*

- **No Direct Choice of Securities:** Mutual fund represents indirect mode of investment; hence investor does not have a say in securities selection. They cannot select a security in which they wish to invest.
- **Relying on Mutual Fund Manager's Performance:** Investor has to rely on fund manger for receiving any earning made by the fund. Further, if manger's pay is linked with the fund's performance, then in the zest of earning more, he may go for short-term goals ignoring the long-term. There is always a possibility that mutual fund deviate from its investment objective and serve the interest of its management.
- **High Management Fee and other Expenses:** All mutual fund does not run efficiently. Mutual funds at times charge management fee so as to pay high compensation to the fund manager.

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- **Lock in Period:** Many mutual funds scheme especially tax saving scheme have strict lock in period. The mutual fund units cannot be redeemed during lock in period. Hence during lock in period, the units of mutual funds become illiquid.

1.6.4 *Mutual Fund Schemes*

- **Open Ended Mutual Fund:** It allows entry and exit of investor at any point of time. The capital of fund is unlimited and there is no fixed maturity date. An investor can buy or sell unit at any time.
- **Close Ended Mutual Fund:** It has fixed maturity period and the investor can only invest only during the initial launch period known as the IPO period. The investor can make an exit from scheme by selling his units in the secondary market or at the end of maturity period or during repurchase period.
- **Interval Funds:** These are hybrid fund and combine the features of open ended and close ended schemes. These schemes are open for

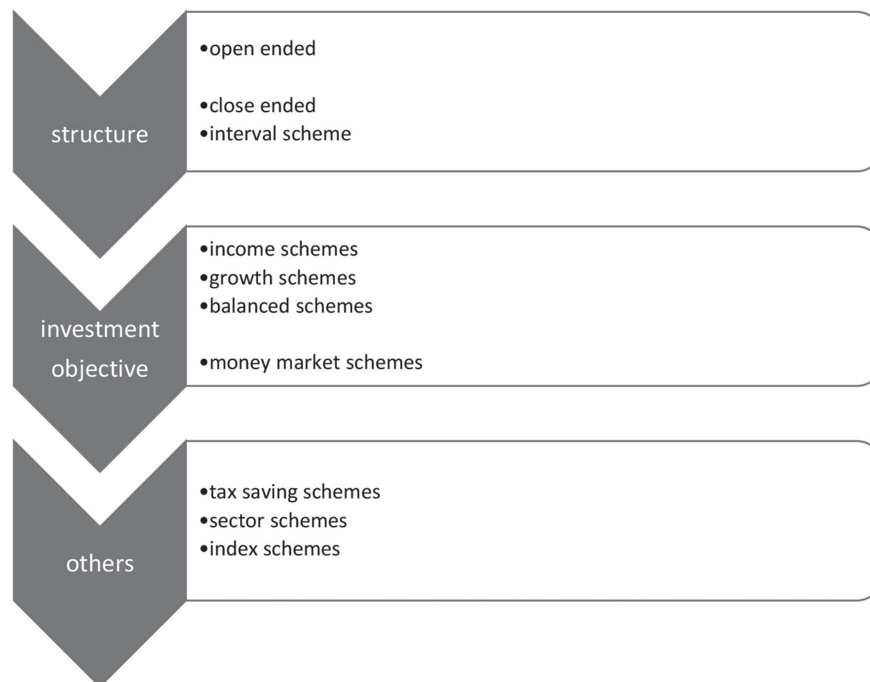

Figure 1.1

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purchase and redemption during pre-specified intervals (monthly, quarterly, annually etc. at NAV related prices.

- **Load Funds:** Load in context of mutual fund means charge or fee. A load fund charges a percentage of NAV as entry or exit fee. The charge ranges from 4% to 8% of the amount invested or it could be a flat fee. For example, if you invest 1000 into a 5% load fund, the actual investment would be 950 as Rs. 50 will be charge going to the company.
- **No load Fund:** Under this category there is no charge for entry or exit.
- **Domestic Fund:** There fund is open for investment in the company where the mutual fund is registered. Most of the mutual fund in India are domestic funds.
- **Off-shore Mutual Fund:** These are open for subscription by foreign investors only. These funds channelise foreign investment in mutual fund in a country, at present number of off shore fund launched by mutual funds in India. For example, ICICI Prudential US blue chip equity fund.
- **Growth Fund:** Scheme which offers capital appreciation and dividend opportunity to the investor. The major investment in such fund is in equity. The main idea behind such fund is to provide capital gain rather than regular income.
- **Income Fund:** These funds promise a regular income to its investors. Majority of funds are channelised towards fixed income securities such as debentures, government securities and other debt instruments. This is relatively low risk-low return investment avenue. This scheme is ideal for investor seeking capital stability and regular income
- **Balanced Fund:** The combination of growth fund and balanced fund. A balance fund invests about 50:50 in equity shares and bonds. They invest in shares for growth and invest in bonds for regular income. These are ideal for investors who are looking for a regular income source and moderate growth over a period of time.
- **Gilt Funds:** Those funds which invest exclusively in government securities; therefore, these funds provide low return at a very low

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risk. They are preferred by risk averse and conservative investors who wish to invest in the shadow of secure government bonds. Almost every mutual fund operating in India has launched a gilt fund. SBI magnum gilt is a gilt fund operating in India.

- **Money Market Funds:** These funds provide easy liquidity and moderate income. These schemes invest in short-term debt i.e., money market instrument and seek to provide reasonable returns for the investors. Investment in money market instrument such as treasury bills, certificate of deposit, commercial paper and inter-bank money.
- **Tax Saving Schemes [or Equity Linked Savings Scheme (ELSS)]:** These schemes offer tax benefits to its investors under specific provision (section 80c) of the Income Tax Act, 1969. This helps the investor in reducing tax liability. These also invest in equities, thus offer long-term growth opportunities. However, these schemes have 3-year lock in period.
- **Index Schemes:** Index funds or index schemes attempt to replicate the performance of benchmark market index such as BSE SENSEX OR NSE NIFTY. The collected funds are allocated on the basis of proportionate weight of different securities as stated on the benchmark index and earn the same return as earned by market.
- **Sectoral Funds:** These funds invest exclusively in the stock of companies belonging to a specific set of companies or sector. The idea is to reap the benefit of the sector or industry cycle. If industries are going through good times these schemes offer good returns to the investors.
- **Ethical Fund:** Ethical fund make investment on the basis of certain ethics or values especially shariah value. These funds used a screening criterion to decide about a company or stock which are suitable for investment. There are two ethical funds operating in India. They are TATA ETHICAL FUND TAURAS ETHICAL FUND. The investment in this fund is based on fundamental of shariah or shariat, which are guided by Islamic investment philosophy which invests in companies based on certain screening norms.

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1.7 Latest Developments Regarding Mutual Funds

1.7.1 *Exchange Traded Fund*

ETFs are baskets of securities that are traded on a stock exchange like individual stock. They track an index and money is invested in securities of index in same proportion, thus has similarity with index mutual fund. However, unlike the mutual fund's ETFs can be bought and sold throughout the trading day like any stock. These funds charge lower expenses then an index mutual fund, but investor has to pay the brokerage to buy and sell ETF units.

1.7.1.1 *Advantages of ETFs*

ETFs provide exposure to an index or a basket of securities that trade on exchange like single stock. The following are the advantages of ETFs.

- While redemption of index fund takes place at a fixed NAV price (usually end of day), ETFs offer the convenience of intra-day purchase and sale on the exchange, to take advantage of prevailing price, which is close to actual NAV of the scheme at any point in time.
- They are low-cost investment options than traditional funds.
- Since an ETF is listed on an exchange, costs of distribution is lower and the reach is wider.
- ETFs protect long-term investors from inflows and outflows of short-term investor. This is because the fund does not incur extra cost for buying/selling the index shares due to frequent subscription and redemption.

1.7.2 *Funds of Funds*

A fund of funds scheme means a scheme which invests in other mutual fund schemes. In other words, a scheme where the subscription proceeds are invested in other mutual funds, instead of investing in equity or debt instruments. Since these funds invest in other mutual funds, they offer and achieve greater diversification than traditional mutual funds. Expense and fee for such fund is higher as they need to pay to underlying fund.

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1.7.3 *Systematic Investment Plan*

A systematic investment plan or SIP is a smart mode for investing money in mutual funds. SIP allows an investor to invest a certain pre-determined amount at a regular interval (weekly, monthly, quarterly, etc.). A SIP is planned approach towards investment and helps to inculcate the habit of saving and build wealth for future. SIPs are ideal for retail investor who do not have the resources to pursue active investments.

Following are the benefits of SIP.

- **Rupee-cost Averaging** – An investor invests a fixed amount irrespective of NAV, so he gets fewer units when NAV is higher and more units when NAV is lower. This smooth out the market ups and downs thereby reducing the risk of investment when markets are volatile. Thus, SIP allows its investors to achieve.
- **Power of Compounding** – Albert Einstein once said "compound interest is the eighth wonder of the world. He who understand it, earns it… he who doesn't ... pays it'' "the sooner you start investing, the more time your money has to grow".
- **Disciplined Saving** – When investment is made through SIP, investor commits to himself to save regularly. This leads to discipline in saving and investment.
- **Flexibility** – While it is preferred to invest in SIP for a long-term, there is no compulsion. Investor can discontinue the plan at any time. Moreover, one can also increase/ decrease the investment amount.
- **Long-term Gains** – Due to rupee- cost averaging and the power of compounding SIPs have the potential to deliver attractive return over long investment horizon.
- **Convenience** – SIP is a hassle-free mode of investment One can issue a standing instruction to his bank to facilitate auto debits from bank account.

1.7.4 *Systematic Withdrawal Plans*

Systematic withdrawal plan or SWP Permit the investor to make an investment at one go and systematically withdraw at periodic interval,

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at the same time permitting the balance amount to remain invested. Withdrawal can be done either on monthly basis or on a quarterly basis, based on need and investment goal of investor. SWP includes convenient pay out options and has several tax advantages. Under SWP, neither tax is deducted nor is dividend distribution tax applicable. Moreover, there is no entry or exit loads in SWP.

1.8 Summary

This chapter is designed to provide individuals with a comprehensive understanding of the investment opportunities available in the market. It begins by outlining the objectives of investing, such as generating income, preserving capital, and achieving capital growth. It then delves into various types of investments. The chapter also provides a detailed analysis of financial products such as derivatives and mutual funds along with their advantages and limitations. For example, derivatives are financial instruments that allow investors to speculate on the price movements of an underlying asset, while mutual funds are investment vehicles that pool money from multiple investors to invest in a diversified portfolio of securities. Overall, this chapter provides individuals with a comprehensive understanding of the various investment opportunities available in the market, helping them make informed decisions.

1.9 Answers to In-Text Questions

1. *(b)* A contract whose value is derived from an underlying asset
2. *(c)* Customizable terms between the parties
3. *(b)* Foreign exchange
4. *(a)* To transfer risk
5. *(a)* Buyer of the option
6. *(b)* Determined by the exchange
7. *(b)* The upfront cost of the option
8. *(a)* Options involve buying or selling of rights to one party only, while in future contract both parties have the obligation to complete the contract

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1.10 Self-Assessment Questions

1. Briefly explain about the difference between financial investment and real investment.
2. Discuss the benefits of investment in MFs.
3. How SIP is better than other investment options.
4. Explain the difference between futures and options.
5. What is the objective of an investment?

1.11 References

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1.12 Suggested Readings

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L E S S O N

2

Insurance Planning

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STRUCTURE

2.1 *Learning Objectives*
2.2 *Introduction*
2.3 *Concept of Insurance*
2.4 *Principles of Insurance*
2.5 *Life Insurance*
2.6 *Comparison of Policies Offered by Various Life Insurance Companies*
2.7 *Term Insurance*
2.8 *Endowment Policy*
2.9 *Summary*
2.10 *Answers to In-Text Questions*
2.11 *Self-Assessment Questions*
2.12 *References*
2.13 *Suggested Readings*

2.1 Learning Objectives

- Develop a basic understanding of the insurance sector.
- Understand the working and functioning of the insurance sector.
- Explain the principles and provisions that govern the Life as well as General Insurance Contracts.
- Compare the various types of life insurance policies available in the market.

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2.2 Introduction

When we are young, healthy, have diverse sources of income, and are living our best life possible, we generally don't think much about our uncertain future. The future, by its nature, is always uncertain. Man, being a social animal and risk-averse, always tries to mitigate the risk. Therefore, it becomes necessary for every individual to safeguard his/her future, regardless of how much money they make, how well their business is going, or how robust and healthy they are today. Sharing risk through economic cooperation is one of the most popular ways to reduce the risk that results from unknown future events, and this practice eventually gave rise to the idea of 'insurance'.

Insurance does not prevent the occurrence of uncertain events; however, it reduces the risk through the collective bearing of risk by a large number of people. Thus, it may be defined as a scheme of covering large risks of a few people among a large number of people by spreading the risks in exchange for a small, fixed amount, which is termed as *Premium*. The basic premise of 'collective bearing of risks' rests upon individuals exposed to similar risks pertaining to similar assets contribute to a common pool of funds to mitigate the individual risk by paying a small, fixed amount at regular intervals, to compensate the affected party/parties among themselves out of the common pool.

2.3 Concept of Insurance

In legal sense, an insurance may be defined as a contract (in a form of policy) between two parties- the insurance company (called Insurer), and an individual (called Insured), wherein the insurer promises to indemnify for financial losses, on the occurrence of particular event, due to insured in return for the premiums paid at regular intervals. The 'insurer' and 'insured' are also known as 'assurer' and 'assured' respectively.

In a nutshell, insurance is a risk transfer mechanism in which an individual transfers his or her risk to an insurance company in exchange for financial protection against unforeseen events. And the amount paid for this arrangement is known as the premium. There is insurance available for a wide range of risks, from your life to the mobile phones you use. Finally, it is critical to safeguard what is "important" to you.

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The idea of insurance operates under the principle of "risk pooling." One must pay recurring payments (also known as premiums) toward the cost of the insurance when an individual purchases a specific type of insurance policy from an insurance provider for a predetermined time with a predetermined level of coverage. Similar to this, an insurance company will collect premiums from all of its customers (also known as insured) and combine the funds to pay for losses caused by an insured on the occurrence of specified event(s). If the covered event occurs and one files a claim, the insurance company will use a pool of premiums paid by policyholders to cover his/her losses. As mentioned earlier, an insurance policy is offered by the insurer for a pre-determined period of time. Therefore, some insurance will not pay back, any compensation or the premiums paid during the policy periods, if the policyholder never suffers from the loss during the policy period. To overcome this problem, insurers have introduced various kinds of insurance products which also involve savings elements into it.

EXAMPLE

Ram bought a car for Rs. 20 lakhs. He purchased car insurance — third-party insurance plus comprehensive insurance with the add-on of roadside assistance and zero depreciation. Along with that, he bought health, medical, and term insurance to safeguard his future from any unforeseen emergencies. While another car buyer named Sanjay bought a new sedan and purchased car insurance - a third-party policy because it is compulsory, he thinks purchasing any other insurance policy is a waste of money. A few months later, due to some unforeseen circumstances, Ram and Sanjay met with an accident. Ram got a claim for his car damage, and the health and medical insurance companies took care of his hospitalization bills. Whereas Sanjay has to pay for almost everything from his pocket because he only has a third-party insurance policy that only covers injuries of third parties due to accidents. There are many people like Sanjay who think investment in insurance is a waste. It is crucial to have some/specific insurance products in life.

Insurance is the most effective risk management tool, allowing individuals and businesses to be protected from financial risks arising from a variety of contingencies. The emotional and psychological losses can never be

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replaced, but the financial losses can be reimbursed by insurance. Though there are some uncertainties in life that cannot be avoided, insurance can help you transfer the financial risk associated with them. There are numerous kinds of insurance products available in the market such as **life insurance,** health insurance, accident insurance, term insurance, retirement plan, vehicle insurance, property insurance, etc. however, these different products may be classified into two categories:

- Life insurance products
- General insurance products

Life insurance covers individuals against the risk of death. There are many different types of life insurance policies, including term, endowment, whole, money-back, and unit-linked investment plans. Numerous life insurance plans combine protection with savings, making them excellent tools for long-term savings. Whereas General insurance policies provide coverage for monetary losses caused by events other than death. General insurance policies are available in a variety of forms and cover a wide range of risks, including health, vehicle, marine, liability, travel, and commercial risks.

The main goal of any insurance policy is to provide protection and relieve the 'insured' from a substantial financial burden on the happening of future events, which may be certain or uncertain.

IN-TEXT QUESTIONS

1. Insurance helps to:

(a) prevent the occurrence of adverse events.

(b) mitigate the financial impact of adverse events.

(c) Neutralize all repercussions of unfavourable conditions.

(d) Maintain the productiveness of assets.

2. A social Device that reduces or eliminates the risk of loss of life and property is ____________________.

3. The duration of an insurance policy's coverage is known as the

(a) Policy term

(b) Policy loan

(c) Policy mode

(d) None

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2.4 Principles of Insurance

The concept of insurance is risk distribution among a group of people. Hence, cooperation becomes the basic principle of insurance. To ensure the proper functioning of an insurance contract, both the insurer (Insurance Company) and the insured (policyholder) must adhere to the seven insurance principles listed below:

2.4.1 *Principle of 'Uberrimae Fides' or Principle of Utmost Good Faith*

This principle states that both parties in an insurance contract must act in good faith toward each other, which means they must provide clear and concise information about the contract's terms and conditions. In other words, the insured must provide all the relevant information about the subject matter, whereas the insurer must provide precise contract details. This principle signifies full disclosure or maximum truth to each party from each other. The absence of this principle makes the insurance contract voidable.

This principle is applicable in both types of insurance i.e., Life insurance as well as General Insurance

EXAMPLE

Mr. X took a health insurance policy. At the time of taking insurance, he (insured) concealed the fact of his smoking habit and failed to disclose this fact to the insurer. Later, he got cancer. In such a situation, the Insurance company will not be liable to indemnify to Mr. X on the ground of concealed material fact.

2.4.2 *Principle of Proximate Cause*

The doctrine of proximate cause is based on the cause-and-effect principle, which states that once the effect has been proven and the cause has been traced, it is not necessary to go any further, i.e., cause of the cause. In other words, the nearest and primary cause of the loss, or the proximate cause, should be taken into account when determining the claim for a loss.

Though it is a vital factor in all types of insurance, this principle is not used in Life insurance.

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EXAMPLE

A surveyor surveying a factory damaged in a fire concluded after a thorough investigation that the fire was caused by negligence as well as defective design and that both of these causes played a role in the damage. The insurance policy covered negligence, but not defective design, so the claim was denied.

2.4.3 *Principle of Insurable Interest*

According to this principle, the insured person must have an insurable interest in the subject matter (life or property). The term "insurable interest" refers to a subject that, if a specific event occurs, significantly alters the insured's position; but, if the specific event does not occur, the insured stays in the same position. An individual cannot buy a life insurance policy for a person on whom he/she has no insurable interest. However, in case of spouses, no proof of insurable interest is required. It is worth to note that in order to claim the insurance amount, the insured must be the owner of the subject matter both at the time of contracting and at the time of the accident.

EXAMPLE

An owner of a bookstore sells his/her book in cartons, has an insurable interest in the cartons because he is generating revenue from it. However, if he sells the cartons only, he will no longer have an insurable interest in the things available in the cartons.

Mr. X takes a life insurance policy for his neighbor. In this case, Mr. X will not get any claim from the insurer, on the death of his neighbour as he has no insurable interest.

2.4.4 *Principle of Subrogation*

This principle states that, following the settlement of claims for losses incurred on the insured subject matter, the insurer has the authority to act in place of the policyholder. In essence, the insurer, or firm, receives ownership rights to the insured property. This principle gives the insurer

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the right to recover any loss payments paid to the insured from a negligent third party, and thus, prevents the insured from collecting twice for the loss.

EXAMPLE

If the goods kept in the factory of the insured gets destroyed by fire, due to negligence of the electric company (third party). The insurance company (insurer) will compensate to the insured for the losses caused by the fire and may also sue the electric company to recover the amount of loss paid to the insured.

2.4.5 *Principle of Indemnity*

According to this principle, the insured will only be completely compensated for their actual losses. Consequently, the insured is not entitled to make a profit from the loss suffered. The indemnification principle's goal is to put the insured back in the same financial situation he was in prior to the loss happening. For general insurance, the principle of indemnification is rigidly followed, whereas it is not relevant to life insurance contracts.

EXAMPLE

Mr. X took vehicle insurance for his car. A few months later, he met with an accident that caused him Rs. 14,500 as repairing charges. He claims indemnification for Rs. 15,000 (14,500 for repairing plus 500 for transportation cost). The insurance company (insurer) will indemnify only Rs. 14,500 as the loss caused due to accident is that much only.

2.4.6 *Principle of Contribution*

When an insured person purchases multiple insurance policies covering the same risk, the contribution principle is in effect. In other words, if a person has insurance from multiple companies, each insurer will share the loss according to the quantity of their individual coverage. One insurance company has the right to contact other insurance companies to request a comparable amount if it has made the full payment.

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EXAMPLE

A property worth Rs. 5 lakhs are insured for Rs. 3 lakhs with Company A and Rs. 1 lakh with Company B. In the event of property damage worth 3 lakhs, the owner can claim the full amount from Company A but not from Company B. Company A can now claim the proportional amount reimbursed from Company B.

2.4.7 *Principle of Loss Minimization*

According to this principle, the insurer is obligated as an owner to take the necessary steps to minimize the loss to the insured property. The principle forbids the owner from being irresponsible or negligent simply because the subject matter is insured.

EXAMPLE

If a fire breaks out in your factory, you must take reasonable measures to put it out. You can't just sit back and let the fire destroy the factory because you know the insurance company will cover it.

IN-TEXT QUESTIONS

4. The main cause of loss or damage is _____________

(a) Proximate cause

(b) Indirect Loss

(c) Consequential loss

(d) All of these

5. Insurance works on the principle of:

(a) Sharing of losses

(b) Probabilities

(c) Large numbers

(d) Randomness

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6. The _______________principle of insurance stipulates that the insured must have an insurable interest in the life or property insured.
7. The principle of _______________ makes sure that an insured person doesn't make profit by purchasing multiple insurance from more than one company.
8. In insurance, the......... principle means utmost truthfulness.
   (a) Subrogation
   (b) Causa Proxima
   (c) Insurable interest
   (d) Uberrima fides

2.5 Life Insurance

Let's take an Example: Rajeev is a young dynamic boy and works in a construction company. His work requires him to travel different Countries/cities to inspect various construction sites. Among them most of the buildings are under construction and hence these sites can be dangerous. The nature of his work exposes him to several risk and uncertainties. Rajeev is a solo earner of his family and having a wife and two children to feed on. So, Rajeev decided to secure his future. He realized that he needs to keep his family protected in case anything happened to him. Therefore, he decided to opt for life insurance policy to secure him against uncertainty of life. He visited to an insurance company and found out that there are various types of life insurance. And finally entered into a contract after choosing a right type of life insurance he wants. The contract will ensure that insurance company will protect Rajeev by paying a sum of money in case of any unexpected event in his life. In exchange for insurance, Rajeev will make payments to insurance company. Such payment is known as Premium. The payment can be made in one go or in regular instalments. In this case, Rajeev is taking life insurance and known as assured and the company is known as the insurer.

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Insurance policies provide protection against the various types of uncertainties that can occur in the life of an individual. There are various types of insurance in the market due to the presence of a large number of insurance companies. One of them is Life Insurance. Life insurance is a contract between an insurance policyholder and an insurance company (Insurer). It is a contract in which the insurer guarantees to pay a specific amount of money to the beneficiary (nominee) in exchange for a premium, upon the death of an insured person or at the end of a specified maturity period.

Our need for life insurance stems from our desire to protect our family. If you care about the needs of your family, you will surely consider insurance. Due to the Collapse of the prevalent joint family system, where generations coexisted in harmony and had sense of financial stability due to more earning members, insurance is now more vital than ever. The nuclear family has emerged as a result of the changing times. Therefore, you must also set aside some of your income for the future as well. This is a place, where insurance can assist us.

Fewer earning members, stress, pollution, increasing competitiveness, greater aspirations, etc., are some of the reasons why insurance has gained prominence and where it plays a significant role. Insurance gives both income and the sense of security. Buying insurance relieves an individual of an unnecessary financial stress. The individual is satisfied by the idea that he has a safety net.

From the starting of your life until the time you retire, insurance can meet all of your needs. It also helps your child to get quality education. Given the future uncertainty, insurance is a must. Event like Accidents, diseases, among other occurrences, can be tremendously devastating. Insurance helps to cover the costs of these unavoidable events.

In addition, retirement is the phase at which every individual has nearly completed his duties and looks forward to resting and can be painful if not properly planned. Have we considered the rising cost of living and taxes? Under such conditions, will our investment yield favourable returns? Will it provide for our family after we're gone? Surely, an insurance policy will cover these and much more. Nowadays, insurance is a requirement. It gives regular income as well as additional bonus. Life

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insurance has come a long way since its inception as a risk-covering medium for short periods of time.

Example: Amit is 42 years old and worked in the multinational company. His wife Nisha, who is a housewife, watches after their children. They reside in a rented apartment, whose monthly rent is 15,000 rupees. Amit has taken out a loan of Rs. 2 lakhs. His average monthly income is 40,000 rupees. Amit dies in a tragic automobile accident.

What are the financial consequences of his death for his family? There may be various implications for his family's finances. Some of these include:

- Monthly Income would cease.
- His spouse and children may require financial aid from other relatives.
- His wife might not have enough money to repay the Rs 2 lakh loan.
- The family may be forced to relocate to a cheaper residence.
- His widow may have to work to pay for their bills.
- His children's schooling may suffer.

This example highlights the impact of an immature and uninsured death of primary earner might have on a family. If Amit had bought life insurance, his family would not have endured such troubles in the event of his untimely demise. A simple life insurance policy may have supplied Amit's family with a lump sum that could have been invested to replace all or a portion of his income.

Categories of Life Insurance Plans

- ***Pure Protection*****:** A Pure Protection plan is designed to secure one's family's future by providing a lump sum amount, in his/her absence. Example of pure protection includes term insurance plan.
- ***Protection cum Savings*****:** A Protection and Saving plan is a financial tool that helps individuals to plan his/her long-term goals like purchasing a home, funding their children's education, and more while offering the benefits of a Life Cover. Money back policy, retirement plan and unit linked insurance plan are few examples of protection cum saving plan.

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HISTORY OF INDIAN LIFE INSURANCE

The history of insurance in India can be divided into two sections that is before and after 1912. Prior to 1912, India lacked insurance regulation legislation whereas later includes the part when Life Insurance Companies Act and the Provident Fund Act were passed.

1818: Life Insurance in its contemporary form came into India. Oriental Life Insurance Company was founded by Europeans in Calcutta as the first life insurance company in India. The Bombay Mutual Life Assurance Society was founded in 1870. This was the first life insurance firm in India.

The Life Insurance Companies Act was enacted in 1912. This act of 1912 mandated that actuaries certify the premium rate tables and periodic valuation of insurance firms (one who calculates the premium). However, this Act discriminated against foreign and Indian enterprises in a number of ways and gave priority to foreign firms, putting Indian firms at a disadvantage.

The Insurance Act was passed in 1938. It was the first law to regulate both Life and Non-Life Insurance. It was intended to provide rigorous state supervision over the insurance industry.

In 1944, the pressure for the nationalization of the life insurance sector accelerated and later it was sent to legislative assembly for amendments. After a numerous effort, nationalization was finally accomplished in 1956.

On January 19, 1956, the life insurance industry in India was nationalized. 245 Indian and foreign insurance companies and provident organizations were nationalized by the central government.

The Life Insurance Corporation Act was passed by the Indian Parliament on June 19, 1956, with a capital contribution of Rs. 5 crores from the Government of India., The Life Insurance Corporation of India was established on September 1, 1956.

2.5.1 *Key Characteristics of Life Insurance*

- Life insurance is a legally binding contract that pays a death benefit to the policy owner (nominee) when the insured dies.

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- For a life insurance policy to remain in force, the policyholder must pay a single premium upfront or pay regular premiums over the policy term.
- When the insured dies, the policy's named beneficiaries will receive the policy's life cover.
- Term life insurance policies expire after a certain number of years. Permanent life insurance policies remain active until the insured dies, or stops paying premiums, or surrenders the policy.
- A life insurance policy is only as good as the financial strength of the company that issues it. State guaranty funds may pay claims if the issuer can't.

2.5.2 *Pros of Life Insurance*

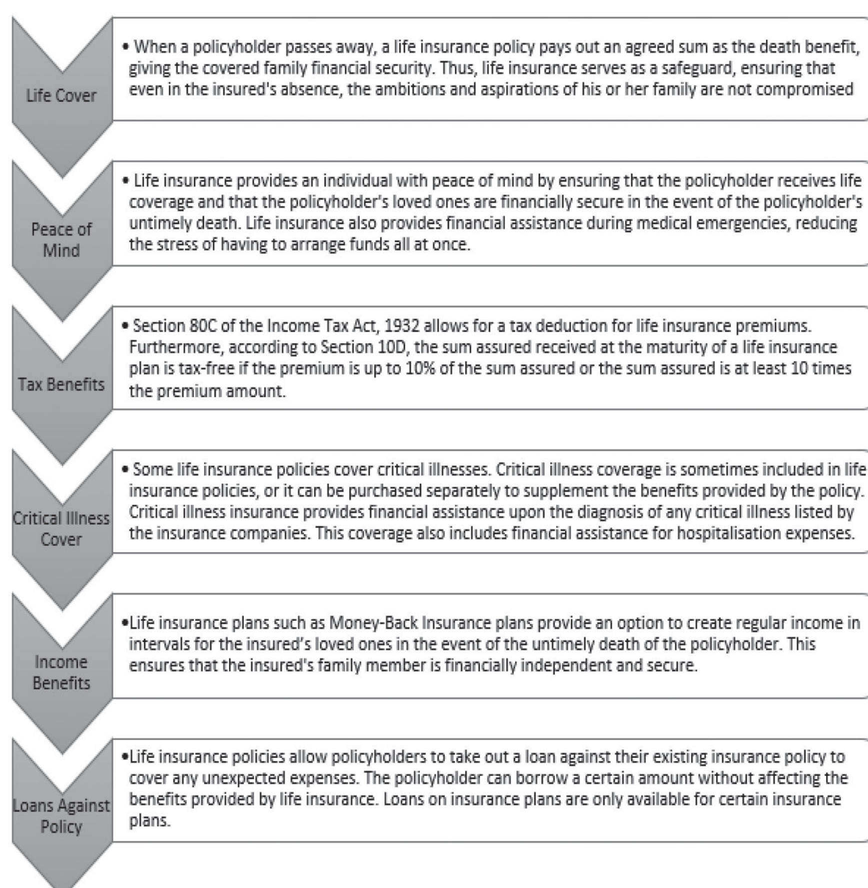

Figure 2.2

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2.5.3 *Principles of Life Insurance*

In India, we follow four basic principles of life insurance.

- **Insurable Interest:** This principle has been put in place to protect insurance policies against any kind of misuse. It refers to the level of interest that the potential policyholder is estimated to have in the insurance policy. This interest could be in the form of a personal relationship, family bond, etc. Based on this interest level, the insurance company approves or rejects the individual's application for a policy.
- **Minimal Risk:** Any company that provides life insurance is taking on some level of risk, since they would need to pay the assured sum at some point of time. Therefore, the company would prefer to keep the level of risk as low as possible. To ensure this, the insurer might check the applicant's medical status, smoking habits, etc. In addition, they might expect the policyholder to take good care of their health.
- **Good Faith:** As mentioned earlier, a life insurance policy is essentially a contract between the insurer and the policyholder. This contract is entered into on good faith that both parties are providing accurate relevant information, without hiding anything. If any information is withheld, it could lead to serious consequences. For instance, if the insurance provider discovers that the policyholder had a pre-existing heart condition but did not divulge the fact at the time of policy purchase, they could reject the claim made by the beneficiary, following the demise of the policyholder.
- **Law of Large Numbers:** This is a key principle of life insurance, which is based on a statistical theorem that states that with larger numbers, fluctuations tend to average out. This essentially means that since life insurance is a long-term investment, the losses and gains will average out over time, minimizing the risks for the policyholder

2.5.4 *Disadvantages of Life Insurance*

Life insurance disadvantages include:

- Life insurance has a high cost for older persons. Age increases life insurance premiums. Age increases risk, therefore, premiums do too.

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So, get life insurance early to avoid exorbitant premiums. Insurance firms may have refused to cover elderly persons with illnesses.

- Calculating returns is difficult. Life insurance returns are complex and hard to forecast. Life insurance returns are based solely on market performance. Unlike PPF and other fixed deposit plans, life insurance is hard to quantify.
- Policies: There are several life insurances firms in India. Your needs determine the appropriate life insurance plan. Different insurance policies have different characteristics, which can confuse customers. Some policies are easy, some aren't. Choosing life insurance might be difficult.
- Insurance firms may not pay benefits even after the policy matures, and they have resisted paying the sum promised or death benefit to the policyholder or nominee. They'd cite hidden fees or stipulations to reduce pay-outs. So, carefully read the policy and choose a provider with a good pay-out rate. Before signing a contract, discuss the pros and cons of life insurance with our agents.
- Any market-available financial product has exclusions and hidden terms. You must find the proper clauses and life insurance policy. Most insurance don't cover suicide in the first year, and virtually all exclude drug overdose or criminal activity.

2.6 Comparison of Policies Offered by Various Life Insurance Companies

There is a bundle of life insurance plans available in the market. Choosing the right type of life insurance policy is one of the most important requirements for a comfortable, hassle-free life. It purely depends on which one suits your need and requirement basis the benefits accrued or attached to a plan. There are different types of life insurance policies in India on offer to prospective policyholders.

- **Term Life Insurance or Term Plan:** Term life insurance provides a death benefit to the beneficiary only if the insured dies during the policy term. The insurance coverage terminates with no further benefit and there is no longer a basis for a pay-out or death claim

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if the policyholder survives to the end of the policy term. Term life insurance is the most popular type of life insurance and is widely considered to be the simplest and purest form of life insurance. The most distinctive feature of a term insurance plan is the high amount of coverage offered at extremely nominal premium rates. It is thus cheaper than other types of life insurance policies.

- **Whole Life Insurance Plan:** The Whole Life Plan is often known as a straight or regular life. As long as the premiums are paid, it remains for the duration of the insured person's lifespan. If the insured passes away, the nominee will get the aforementioned sum. The policyholder has the right to cancel or borrow against the policy at any moment. This policy's maturity period is one hundred years. The policy will turn into a matured endowment if the insured lives past the maturity age. The death benefit under this plan is tax free.
- **Unit Linked Insurance Plan (ULIP):** Unit Linked Insurance Plan or ULIP is a type of life insurance product that offers dual benefits of investment and life insurance. Among the different types of life insurance policies available, ULIPs enjoy a high amount of popularity owing to their versatile nature. A portion of the premiums paid towards ULIPs is directed towards ensuring insurance coverage, while the rest of the premium is invested into a bouquet of investment instruments, which can include market-backed equity funds, debt funds and other securities. ULIPs are extremely flexible instruments since investors can easily switch or redirect their premiums between the different funds available. ULIPs are also touted as having an edge over other market instruments in terms of tax-saving benefits, since their proceeds are exempted from LTCG (Long-term Capital Gains).
- **Endowment Policy:** Endowment Policy is a type of life insurance policy that acts as, both, an instrument for insurance and saving. Endowment plans aim to provide maturity benefits to the life insured, in the form of a lump sum payment at the end of the policy tenure, even if a claim hasn't been made. Endowment plan is the most suitable type of life insurance for people looking to get maximum coverage alongside having a sizable savings component. They help the policyholder inculcate the habit of savings, even while providing financial security to their family.

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- **Money Back Policy:** Being one of the best types of life insurance policies, a money-back policy offers policyholders a percentage of the total sum assured at periodic intervals in the form of Survival Benefits. Once the policy reaches maturity, the remaining amount of the Sum Assured is handed over to the policyholder. However, if the policyholder dies during the policy term, their dependents are given the entire Sum Assured without any deductions.
- **Retirement Plan:** A retirement plan is a type of life insurance that focuses on providing you financial stability and security post your retirement. After you retire, you lose your regular income from employment. Investing in retirement plans can help you create a stable regular income stream. If you continue to invest until retirement, the plan will help you take care of your expenses after retirement. A retirement plan requires you to invest a certain part of your income regularly during your working life. At the time you retire, the amount that you create over the years will be converted into a regular income stream. Retirement plans also involve death benefits. Thus, if the policyholder passes away during the course of the policy, their beneficiaries will be provided with an assured sum.

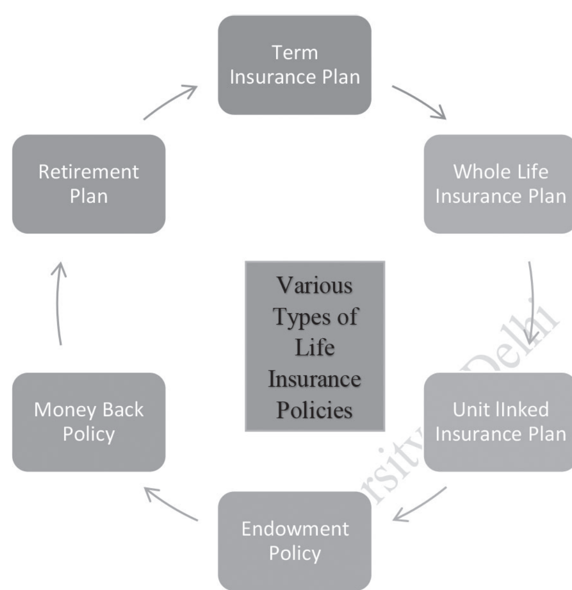

Figure 1.2: Various Types of Life Insurance Policies in India

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Table 1.1: Comparison of Policies Offered by Various Life Insurance Companies

Parameter	Term Plan	Whole Life Insurance Plan	Unit Linked Insurance Plan	Endowment Policy	Money Back Policy	Retirement Plan
Description	Provide risk cover against any type of eventuality.	Offer protection for life till age of 100 years.	Provide benefit of investment across multiple assets class with protection for life.	Ensure Combined benefit of life insurance and saving.	Provide periodic payments and full sum assured in case of a death of policyholder.	Help to create retirement corpus to cover post retirement costs.
Term of Policy	5 to 85 years.	Till 100 years.	10 to 20 years.	5 to 35 years.	5 to 25 years.	Entire Life.
Death Benefit	Life Cover.	Life Cover.	Sum Assured.	Sum Assured.	Sum Assured.	Regular Earring until survival.
Suitability	Family Financial Security to family at reasonable cost.	To Secure Family fortune.	Stress free planning with assured return on the investment.	High yield portfolio investment with life insurance.	Periodic income and life coverage.	Enables safe and secure retirement with steady income.

IN-TEXT QUESTIONS

9. Which insurance policy offers both insurance and investment under a single integrated plan?

(a) Endowment Plan

(b) Money Back Policy

(c) Unit Linked Insurance Plan

(d) Term Insurance Plan

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10. A person whose risk is covered by insurance is known as the

(a) Insured

(b) Merchandiser

(c) Marketer

(d) Agents

11. A nomination can be made only in favour of-

(a) Parents

(b) Spouse

(c) Spouse and children

(d) Any Individual

12. The major goal of life insurance is:

(a) long-term investment

(b) short-term investment

(c) tax benefits from savings

(d) None of them

2.7 Term Insurance

Term insurance offers a coverage for a fixed period of time. If the insured dies during the policy's term, the death benefit is paid to the nominee. Term plans protect your family in case of death or uncertainty. It gives a certain level of coverage for a specific time. Since the amount of premium is low, it allows you to insure a substantial amount. Therefore, an appropriate financial security can be provided to family without accumulating a huge wealth. The plan delivers an exceptional coverage which is not offered by any other investment plan. This coverage protects against premature death and financial consequences.

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EXAMPLE

Ajay is a 30-year-old, wishes to provide for his family in the unlikely event of his sudden death. He purchases a term insurance of Rs 50,00,000 for 10-year with monthly premium of Rs. 1000. The policy will pay 50,00,000 to Ajay's beneficiary if he dies within the 10-year term. If he dies after reaching the age of 40, when the policy has expired, his beneficiary will receive no benefit. If he renews the policy, the premiums will be higher than they were initially because now it will be based on his current age of 40 instead of 30.

If Ajay is diagnosed with a Critical illness during the original policy term, he will be not eligible to renew the policy.

2.7.1 *Types of Term Insurance*

Several types of term life insurance exist. The best choice will depend on the person's circumstances.

- **Level-Premium or Level-Term Policy:** These policies provide coverage for ten to thirty years. The amount of premium and death benefit is both fixed. Due to the fact that actuaries must account for the rising cost of insurance over the policy's duration, the premium is higher than that of annually renewable term life insurance.
- **The Yearly Renewable Term Policy (YRT):** Annually renewable term (YRT) policies have no set duration and can be renewed annually without requiring proof of insurability. The insured's premiums increase from year to year as they grow. There is no defined period, but as the insured matures, the premiums may become prohibitively expensive.
- **The Policy of Decreasing Terms:** Under this scheme, the death benefit of these plans decreases annually according to a predetermined schedule. The policyholder pays a fixed, level premium throughout the policy's duration.

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2.8 Endowment Policy

Endowments combine investment, insurance, and tax savings. This scheme provides you guaranteed return and stable income after retirement. This policy is an all-rounder because it also provides life insurance. It helps you reach all your financial goals. The benefit of an endowment plan enables the customer to safeguard their family from unforeseen occurrences. Unlike term insurance, endowment policies provide maturity rewards if the covered person outlives the policy period.

2.8.1 *Types of Endowment Policy*

- **Full-Endowments:** This plan also called with-profit endowment plans. Under these plans, the customer will get a sum assured on the maturity. If any unusual event occurs during this time, the insurance will pay the amount to the nominee. As this policy offers some extra benefit, therefore the amount paid at the maturity is often larger than the sum assured. It also helps youth to build wealth over time.
- **Unit-Linked Endowment Plan:** this plan is suitable for the people who are risk-takers and want big returns. Fixed-term plan premiums are used to buy investment fund units. Market performance determines fund ROI (Return on Investment). It also covers life insurance.
- **Non-Profit Endowment:** This policy pays a lump sum at maturity or to your nominee in a catastrophic (uncertain) event, whichever comes first. The compensation amount is fixed and static. This policy doesn't offer any bonuses. Therefore, these plans offer pure financial safety net to your family while you're abroad.
- **Unitized With-Profit Endowment Plans:** It combines ULIPs' earning potential with guaranteed returns to protect your money from market volatility. The capital market determines project profits. However, these plans reduce market downturns by ensuring a maturity payout. Payback is assured despite market volatility. Therefore, this product ensures a risk-free, high-return investment.

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- **Low-cost Endowment:** This plan demands lower premiums which allow the policyholder to save for future payments. The insurance guarantees the payment of the sum assured to your nominee in case of emergency. Annual Bonuses improve your retirement benefits. The purpose is to build up a fund in a certain time and be effectively used for loan repayments or some other specific goals.

IN-TEXT QUESTIONS

13. ____________ was the first Indian Insurance Company

(a) Bombay Mutual Assurance Society Ltd.

(b) Bombay Insurance Society Ltd.

(c) Insurance Regulatory Development Authority

(d) General Insurance Corporation

14. The ___________company was the first insurance company to be set up in India to help the widows of the European community.

(a) Life insurance corporation of India

(b) Oriental Life Insurance Company

(c) National insurance company

(d) Bajaj insurance

15. Compared to the premium for a Whole Life plan, the premium for an Endowment plan will be ____________ for the same age

(a) More

(b) The same

(c) Less

(d) Double

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2.9 Summary

- Insurance is an agreement between two parties—the person being insured and the company providing the insurance. The insurer agrees to help the insured with losses. In contrast, the insured pays the insurer a premium in return for the guarantee.
- The foundational principles upon which the insurer-insured contract rests are as follow: - Utmost Good Faith, Proximate Cause, Insurable Interest, Indemnity, Subrogation, Contribution and Loss Minimization
- Life insurance provides financial support to dependents following the insured's death. When the insured dies, the policy pays the recipient a "death benefit." People buy life insurance for many reasons: to replace lost income, to fund business or partnership buy outs in the event of death, to fund retirement plans, to indemnify a loan in the event of premature death, to pay for college, to provide dependency income for the family, and to protect future insurability.
- Life insurance can be classified as follows:
  - *(a)* Term insurance: Gives life coverage for a certain period.
  - *(b)* Whole life insurance offers lifetime coverage.
  - *(c)* Endowment policy: Part of premiums go toward the death benefit; rest is invested by insurer.
  - *(d)* Money-back policy: An insured receives a percentage of the sum assured in intervals throughout the term a policy as a survival benefit.
  - *(e)* Pension plans blend insurance and investing. A percentage of the premiums goes into the insured's retirement corpus, which is paid as a lump sum or monthly payment.
  - *(f)* ULIPs - Unit Linked Insurance Plans is Like an endowment plan, where part of premiums goes toward the death benefit and rest invested in mutual fund.
- Benefits of Life insurance includes family protection, Tax saving, long-term investment and peace of mind. Similarly, Life insurance can be quite costly, which is one of its greatest drawbacks. The cost of life insurance depends on factors such as age, health, and lifestyle.

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2.10 Answers to In-Text Questions

1. *(b)* mitigate the financial impact of adverse events
2. Insurance
3. *(a)* Policy term
4. *(a)* Proximate cause
5. *(a)* Sharing of losses
6. Principle of Insurable Interest
7. Principle of Contribution
8. *(d)* Uberrima fides
9. *(c)* Unit Linked Insurance Plan
10. *(a)* Insured
11. *(d)* Any Individual
12. *(d)* None of them
13. *(a)* Bombay Mutual Assurance Society Ltd.
14. *(b)* Oriental Life Insurance Company
15. *(a)* More

2.11 Self-Assessment Questions

1. Define Insurance and its Importance.
2. Explain briefly the principles of insurance with suitable examples.
3. What are the different types of life insurance policies that are available in India?
4. Explain the benefits that life insurance policies offer.
5. State the principles of Life insurance.
6. Distinguish Between Term Insurance and Endowment Policy.

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LESSON

3

Insurance Product

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STRUCTURE

3.1 *Learning Objectives*
3.2 *Introduction*
3.3 *Health Insurance*
3.4 *Property Insurance*
3.5 *Postal Life Insurance*
3.6 *Rural Postal Life Insurance*
3.7 *Pension Plan*
3.8 *Unit Linked Insurance Plan*
3.9 *Summary*
3.10 *Answers to In-Text Questions*
3.11 *Self-Assessment Questions*
3.12 *References*
3.13 *Suggested Readings*

3.1 Learning Objectives

- Develop a basic understanding of various kinds of life insurance as well as general insurance.
- Understand the relevant factors of health insurance and property insurance on one hand and life insurance on the other.
- Understand Postal Life Insurance and Rural Postal Life Insurance.

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3.2 Introduction

Daily, we hear about accidents and misfortunes. Some of them are:

- People fall ill suddenly.
- Motor cars are stolen, and individuals die or are hurt in car accidents.
- House and belongings are destroyed by fire.
- Large-scale deaths and property damage from cyclones and tsunamis.

Life is full of Uncertainties. Protecting oneself, one's family, and society against unpredictable events has been a concern for millennia.

Fortunately, there is something called "Insurance." It enables us to minimize the financial consequences of various risks and to financially protect ourselves. Despite the notion that an incident such as a death or a fire can lead a devastating economic blow to someone, when we consider the society as a whole, in any given year, only a handful of individuals would suffer in such manner. If a little contribution is gathered from each member of the community and pooled to create a common fund, the pooled sum can be used to compensate the few people who have suffered the loss. Thus, insurance is a financial instrument designed to lessen the financial impact of unforeseen disasters and provide financial security. Everyone who wants to protect himself from financial distress should think of buying the insurance. There is insurance available for a variety of items, ranging from art to pets, and one should get insurance based on their requirements and priorities. Some of them are discussed below

3.3 Health Insurance

3.3.1 *Meaning*

No one anticipates becoming ill or injured, but a major disease can strike at any time. The expense of treating the disease might place a significant burden on your savings. This means that you may have to choose between providing your child with an excellent education and making your mortgage payments. Today, the expense of medical care is steadily increasing.

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For example, a few cancer-related drugs cost around 50,000 rupees per bottle. Depending on their weight, patients typically require 17 to 19 bottles each year for therapy. The medication alone costs between Rs. 18 and Rs. 20 lakhs. With the addition of hospitalisation bills, medical consultation fees, chemotherapy expenditures, etc., your total expenses could surpass Rs. 25 lakhs. These costs, which are already quite high, increase annually. Most thoughtful people have taken measures to safeguard their health as soon as possible. Health insurance is a living benefit that provides funds in times of urgent need.

In this light, let's understand, what is Health Insurance.

Health insurance is a type of insurance coverage that allows an insured to receive reimbursement for medical and surgical expenses. Health insurance is an agreement in which an insurance company agrees to guarantee compensation for medical expenses if the insured becomes ill or is injured in an accident that requires hospitalisation. In general, insurance companies have agreements with leading hospitals to provide cashless treatment to their customers. If the insurance company has no affiliation with the hospital, they reimburse the insured's expenses. The government also encourages health insurance by providing a tax break.

With the rising cost of health care and medical bills that the average person cannot afford, this type of insurance has a growing market. It is estimated that a family spends 10% of their monthly income on health care. In India, where there is no public social insurance, individuals must care for themselves as well as their families. A prolonged illness or disability can devastate the family budget. Despite the fact that health insurance is an important social security financial product, it is unfortunate that in India, health insurance policies are predominantly purchased by families and individuals who can afford to pay their medical bills.

However, the Indian government is making every effort to get individuals to purchase health insurance, and specialized insurance companies are promoted which are exclusively dealing in health insurance. Life insurance companies are also permitted to issue health insurance policies. A health insurance policy covers medical expenses incurred as a result of an accident, illness, or injury. Individuals can obtain such a policy in exchange for monthly or annual premium payments for a set period of time. During this time, if an insured is in an accident or is diagnosed with a serious

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illness, the insurance provider will cover the costs of treatment. Insured can also enjoy several add-on benefits, extended with health insurance policies, which are discussed in detail in the following sections.

3.3.2 *Need for Health Insurance*

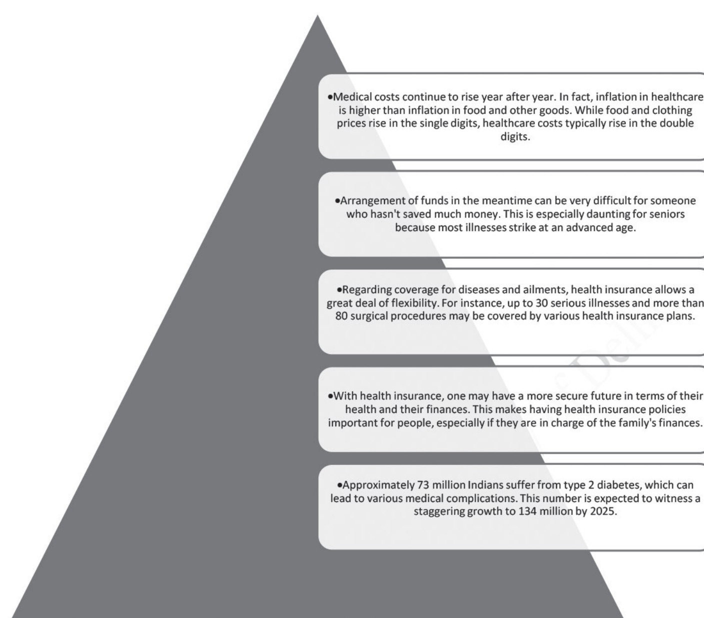

Figure 3.1: Need for Health Insurance

3.3.3 *Benefits of Health Insurance Plans*

- **Hospitalisation Expenses:** Any illness that necessitates immediate hospitalisation is covered by most health insurance plans. However, claims are only accepted if the illness hasn't already been identified when the insurance plan wasn't used.
- **Pre- and Post-Hospitalisation Charges:** A health insurance plan may pay for pre-hospitalization costs such as diagnostic costs, physician fees, etc. The majority of insurance carriers also pay for post-release expenses including prescription drugs, regular check-ups, injections, etc. It is possible to recover compensation cash in the form of a lump sum or by generating the requisite bills.

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- **Lifetime Renewability:** The insurance providers of health insurance policies are required by the Insurance Regulatory and Development Authority of India (IRDA) to provide lifetime renewability benefits to the policyholders. It enables you to renew your health insurance plan without any upper age limit restrictions. Parents and senior adults will benefit the most from this feature because they can renew their insurance without getting stressed to seek additional health insurance coverage as they get older.
- **Cashless Treatment:** Every health insurance provider develops a network of hospitals where the insured can make cashless claims. This simplifies the entire process of receiving emergency medical care. Individuals are not required to pay for any of the covered treatments at a network hospital.
- **No Claim Bonus:** Insured people receive discounts, or a bigger amount insured (at no additional cost) in the following years for each year without a claim, which can help lower their yearly premium payments or extend their sum insured coverage.
- **No Room Rent Capping:** Room rent of hospital rooms is covered under such health insurance policy, allowing insured individuals to recover with comfort. Total amount disbursed in such cases are specified by an insurance company beforehand.
- **Medical Check-up:** Options for health examinations are also provided by insurance policies. Some insurers may also provide free health assessments depending on insured's prior No Claim Bonuses.
- **Tax Benefit:** Section 80D of the Income-tax Act, 1961 allows for the tax deduction of health insurance premium payments. You can deduct up to INR 25,000 per year from your taxable income for an insurance policy covering you, your spouse, your children, and your parents under the age of 60 years. You could claim an additional INR 50,000 deduction if you also acquired a policy for a parent over the age of 60 years.
- **Transportation Charges:** Any ambulance expenses incurred during a medical emergency are covered by a standard health insurance policy. This is a significant benefit because premium hospitals frequently charge exorbitant transportation fees.

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3.3.4 *Comparison of Policies Offered by Various Health Insurance Companies*

In India, there are seven different types of health insurance plans to meet the various needs of people. These are explained further below:

- **Individual Health Insurance:** Individual health insurance plans have a single policyholder who receives all of the coverage benefits available. Individual health insurance plans typically cover insureds' medical expenses based on the sum insured chosen and the premium paid. Some of the benefits provided by these plans include in-patient hospitalisation expenses, pre-hospitalization and post-hospitalization expenses, day-care expenses, and domestic hospitalisation expenses. It typically comes with no upper age limit for policy renewal, implying that the plan provides the insured with lifetime renewability benefits. There are no limits to the number of claims that can be made during the term of an individual health insurance policy.
- **Family Floater Health Insurance:** A family floater health insurance plan covers the entire family for a floater sum insured. Family floaters are advantageous because they make it easier for an individual to manage his or her health insurance by covering himself or herself as well as family members. This insurance plan offers an affordable option when one has to include his/her parents in the policy as compared to a separate senior citizen health insurance policy for their parents.
- **Senior Citizen Health Insurance:** Senior citizen health insurance plans are designed to meet the insurance needs of people aged 60 to 75. It is advisable to obtain a senior citizen health insurance policy because most individual or family floater health insurance plans do not cover people over the age of 65 and only allow renewals. Some of the coverage benefits of senior citizen health insurance plans include day-care expenses, cashless hospitalisation, domiciliary hospitalisation expenses, coverage for pre-existing diseases, and coverage for specific diseases.
- **Women-Specific Health Insurance Plans:** Women-specific health insurance plans are specifically designed to meet the insurance

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needs of women of various ages. These plans protect women from healthcare costs during pregnancy, retirement, coverage for new-born babies, coverage for child education, and so on. Furthermore, after a certain age, they cover women for specific diseases to which they are predisposed. These plans have low premiums and generally provide the insured with lifetime renewability benefits.

- **Critical Illness Insurance Plans:** Plans for critical illness insurance cover a variety of life-threatening conditions, including heart attack, stroke, paralysis, cancer, renal failure, etc. When a critical disease is initially diagnosed, these plans offer a lump payment that the insured person may use both inside and outside of India. The insured may even use this money to pay off any outstanding bills, such as those for a child's education, or in any other manner permitted by the requirements. Given the high cost of critical illness treatments, it is advised to be protected by such insurance.
- **Disease-Specific Health Plans:** People looking for comprehensive coverage for a specific disease, such as cancer, diabetes, or heart disease, may be interested in disease-specific health insurance plans. This plan is also available to those who have a corporate health insurance plan or any other regular health insurance plan, as these plans may not always provide adequate coverage for specific diseases. Disease-specific health insurance plans waive the waiting period, which is otherwise required if you are covered under a standard health insurance plan. The plan, however, is best suited for people who have a family history of a specific disease, such as hypertension or diabetes.
- **Top-Up Health Insurance:** A top-up health insurance plan enables the insured to enhance the sum insured under their base policy to make up the difference in case hospital costs are higher than the plan's limits. When a single hospitalisation occurs during the term of the base health insurance policy and the amount of the claim exceeds the deductible and the total insured, the top-up health insurance policy kicks in. These plans handle each claim independently.

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Table 3.1: Comparison of Policies Offered by Various Health Insurance Companies

Health Policy	Description
Family Floater Health Plan	Cover all family member (you, your spouse, children and parents) in a single policy.
Critical Illness Health Plan	Provide financial coverage to insured in case he/she diagnosed with listed critical illness.
Top up Health Plan	Provide Extra Coverage in case your existing plan is not sufficient to cover the medical bills.
Senior Citizen Health plan	Provide quality healthcare treatment such as domiciliary hospitalization and psychiatric care to the people above the age of 60 years.
Individuals' health Plan	Provide coverage only to an individual. It covers expenses like hospitalization for injuries, illness, Surgery Cost, room rent, day-care etc.
Personal Accident Assurance	Cover the medical expenses that occur due to an accident while providing coverage for partial disability, permanent disability and accidental death.

IN-TEXT QUESTIONS

1. Which of the following terms matches closest with 'Family Floater'?

(a) Health insurance

(c) Property insurance

(b) Accidental injury

(d) Consequential loss

2. Health Insurance coming under____________Insurance.

3. A health insurance should be

(a) Affordable

(b) Continuous

(c) Universal

(d) All of those

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4. ____________ is a form of health insurance against loss by accidental bodily injury
   (a) Property insurance
   (b) Marine insurance
   (c) Personal insurance
   (d) Accident insurance
5. ____________ is a plan that is tailor made for families.
   (a) Floater Health Insurance Policy
   (b) Group health insurance
   (c) Unit-linked
   (d) Health insurance

3.4 Property Insurance

3.4.1 *Meaning*

The Property insurance policy protects the physical goods and equipment of a business or home against losses caused by theft, fire, and other perils. It could be an all-risk policy that protects against all of the risks specified in the policy document. Property insurance is a package policy that provides a variety of coverages under a single policy. They may also cover personal liabilities in some cases. Further, property insurance coverage also covers the risk of all damage caused by fire, theft, wind, smoke, lightning, etc., but it excludes damage caused by water owing to flooding, water seepage, tsunamis, cyclones, etc. Some property insurance policies also don't cover losses caused by terrorism, earthquakes, and other war-related events.

3.4.2 *Cost Covered under the Property Insurance*

There are three types of property insurance coverage which are explained below:

- **Replacement Cost:** The expense of repairing or replacing property that is of equal or greater value is covered by replacement cost.

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Instead of using the cash value of the assets, the coverage is based on replacement cost values.

- **Actual Cash Value:** It signifies the payment of replacement cost *minus* depreciation to the insured. For instance, if a property that is five years old is destroyed, the insured will receive the value of the five-year-old property rather than the new one.

3.4.3 *Types of Property Insurance*

- Property insurance compensates the property owner financially in the event that his or her property and its contents are damaged. Depending on the type of property and risks covered, property insurance policies can be classified into various categories. Here are some common types of property insurance available in India:
- **Homeowner's Insurance:** In India, this is the most common and widely purchased type of property insurance. As the name implies, homeowner's insurance protects the owner's property from financial losses caused due to expected perils. In fact, many lenders have made homeowner's insurance mandatory for those seeking to finance their house.
- **Renter's Insurance:** Similar coverage is offered by renter's or tenant's insurance and homeowner's insurance. However, this specific sort of property insurance is only intended to protect the tenant's personal items kept inside the rented home. It could consist of things like clothing, jewellery, furniture, electronic devices, etc. Some policies also cover additional liabilities a tenant may incur towards his/her landlord.
- **Fire Insurance:** One of the most frequent accidents that can seriously harm a property's contents and surroundings is an accidental fire. A unique kind of property insurance called fire insurance offers protection against such inevitable fires and related risks including explosion, implosion, lightning, impact damage, etc. Both residential and commercial properties can get a fire insurance policy.
- **Commercial Property Insurance:** This kind of fire insurance is also highly popular in India. Commercial properties like offices, warehouses, retail stores, eateries, and factories are covered by this sort of property insurance. It is prudent for business owners to obtain commercial property insurance to protect their operating capital in the event that their commercial property and its contents are compromised.

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- **Natural Disaster Insurance:** A standard property insurance policy may or may not cover natural disasters. However, perils such as earthquakes, hurricanes, storms, floods, cyclones, etc. have the potential to completely destroy a property, resulting in huge financial losses for the owner. A special type of property insurance, known as natural disaster insurance, secures a property against such perils.

IN-TEXT QUESTIONS

6. Property Insurance may not include ___________

(a) Burglary

(b) Fidelity

(c) Insolvency

(d) Sickness

7. Risk is the chance of ___________

(a) Peril

(b) accident

(c) loss

(d) event.

8. The person who seeks protection against a risk and to whom the insurance policy is issued is known as ___________

(a) insurer

(b) customer

(c) insured

(d) creditor

9. When a particular property is insured with two insurers it is called ________

(a) Property insurance

(b) Double insurance

(c) Single insurance

(d) Particular insurance

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3.5 Postal Life Insurance

3.5.1 *Meaning*

The Postal Life Insurance Scheme provides high returns on premium with life insurance coverage. This scheme offers a maximum sum assured of Rs. 50 lakhs. The Government of India offers this policy to employees of Central and State Public Sector Enterprises, Central and State Governments, Government Aided Educational Institutions, Universities, Government Aided Educational Institutions, Autonomous Bodies, Local Bodies, Cooperative Societies, Joint Ventures with at least a 10% Government/ PSU stake, etc.

Postal Life Insurance (PLI), the oldest insurer in the country, was established on February 1, 1884. The program was originally intended as a welfare program for Postal service employees, and later extended to the employee of Telegraph department employees in 1884. Initially, the maximum insurance limit was Rs. 4,000, whereas it is currently Rs. 50 lakhs. Postal Life Insurance is among the earliest insurance schemes to be launched in India. The most remarkable aspect of a PLI scheme is that it yields high returns (with bonus) for policyholders while charging extremely low premiums.

3.5.2 *Characteristics of Postal Life Insurance*

A policyholder is entitled for the following advantages:

- **Nomination Facility:** The policyholder is able to choose a beneficiary and can alter his/her beneficiary.
- **Loan Facility:** This policy comes with a loan facility. The policyholder may pledge his or her policy as collateral to the Heads of the Region/ Circle on behalf of the President of India once the policy has reached maturity for three years in the case of an Endowment Assurance policy and for four years in the case of a Whole Life Insurance policy. In addition, this programme provides assignment options.
- **Policy Renewal:** A lapsed policy can be renewed by the policyholder. The policy can be revived if the following conditions are met:
    1. The Policy has lapsed after six consecutive non-payments of premium with the policy being in effect for less than three years.

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2. The policy has lapsed after 12 consecutive premium non-payments, if it has been in effect for more than three years.

- **Duplicate Policy Document:** If the policyholder loses the original policy document, a duplicate policy document will be issued. This applies in case where original policy document has been mutilated, burned, or torn and the insured desires a duplicate.
- **Conversion of Policy:** This Whole Life Assurance policy can be converted to an Endowment Assurance policy. An Endowment Assurance Policy may be converted to another Endowment Assurance plan in accordance with the insurer's regulations and guidelines.

3.5.3 *Benefits of Investing in Postal Life Insurance*

The Postal Life Insurance program includes the following Benefits and savings:

- The insured can avail income tax exemption as provided under section 88 of the Income-tax Act, 1961.
- This policy offers assignment, loan, conversion, surrender, and paid-up value options.
- The Process of Transferring the policy to any Circle within India is free.
- Passbook facility for keeping a track of premium payments, loan transactions, etc. is available.
- Annual, half-yearly, and monthly premiums payment options are available. Policyholders can make a payment on any working day when its due.
- PLI also includes incentives for advance payments. If policyholder decided to pay six months of premiums in advance, he/she can avail a discount of 1% on total amount of premium paid (total value of premium worth). Similarly, if he decided to pay a premium of 12 months in advance, in that case he/ she can avail a discount of 2% on total value of premium worth.
- This scheme has a centralised accounting which makes claims process simple, easy and rapid.

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3.6 Rural Postal Life Insurance

3.6.1 *Introduction*

In 1993, a special committee known as the Malhotra Committee observe that insurance represented a negligible proportion of India's gross household savings. The numbers of people from the rural area who holds insurance policy were notably low. As per the committee Suggestion, in rural places, postmasters have very trusting and pleasant relationships with consumers, therefore this position might be leveraged to promote insurance.

With a robust network of urban and rural post offices, Rural postal life insurance was set to succeed. It was believed that through utilising the existing network of post offices, the anticipated operational costs can pull down significantly. Presently, RPLI is the only insurer in the country that offers highest returns for the lowest premiums. RPLI provides insurance to all government sector personnel, including the military, government school staff, nationalised banks, and local civic groups. Private sector employees can also get rural postal insurance.

3.6.2 *Benefits of Rural Postal Life Insurance in India*

Several benefits are associated with rural postal insurance schemes. Some of the most outstanding advantages of these schemes are listed as under.

- Nominations can be changed.
- The policy can be assigned to a lender to avail a loan.
- A Duplicate Policy Bond will be issued in case the original policy is lost.
- In case the policy has lapsed, it can be revived.
- You can convert the policy to an Endowment Assurance from a Whole Life Assurance.

3.6.3 *Insurance Schemes under Rural Postal Life Insurance*

There are a variety of insurance programs available to customers under the rural postal insurance initiative. These plans consist of pure insurance plans and endowment plans. Customers may enroll in one or more of

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these insurance plans and may also switch plans if they are dissatisfied. Important characteristics and advantages of these programs are described in detail below.

Table 3.2: Various Policies under Rural Postal Life Insurance (Based on Whole Life Assurance)

Name of the Policy (Based on Whole Life Assurance)		
Bases	◆ **Whole Life Assurance (GRAMA SURAKSHA)**	◆ **Convertible Whole Life Assurance (GRAMA SUVIDHA)**
Objective	◆ To pay the nominee a sum equal to the assured sum plus accrued bonus in the event of the policyholder's demise.	◆ To pay the nominee a sum equal to the assured sum plus accrued bonus in the event of the policyholder's demise.
Eligibility criteria	◆ Minimum age to enter is 19 and maximum age to enter is 55.	◆ Minimum age to enter is 19 and maximum age to enter is 50.
Conversion of Policy	◆ Whole Life assurance policy may be converted to an endowment policy after one year of coverage has passed and before the policyholder reaches age 59.	◆ Whole Life Assurance can be converted to Endowment after Completing 5 years. However, the same can't be converted After 6 years.
Minimum Sum Assured	◆ Rs 10000	◆ Rs 10,000
Maximum Amount Guaranteed	◆ Rs 100000	◆ Rs 1,00,000
Loan Option	◆ Yes, After Completion of four years of policy.	◆ Yes, After Completion of four years of policy.
Surrender of policy	◆ After completion of 3 policy years.	◆ After completion of 3 policy years; bonus in case of surrender is nullified.
Premium Payable	◆ Premiums vary by sum assured, applicant's age etc.	◆ Premiums vary by sum assured, applicant's age etc.

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Table 3.3: Various Policies under Rural Postal Life Insurance (Based on Endowment Policy)

Name of the Policy (Based on Endowment Policy)			
Bases	◆ **Endowment Assurance (GRAMA SANTOSH)**	**Anticipated Endowment Assurance (GRAMA SUMANGAL):**	**GRAM PRIYA (10 Year RPLI)**
Objective	To provide the nominee/assignee/ heir with the sum assured and bonuses until they reach the age of maturity on the demise of upon the policyholder.	◆ To provide periodic benefits to policyholders. Only the sum insured, and bonuses will be paid upon the policyholder's death, and staggered payments will Cease.	◆ To provide benefits to the policyholder or his/her nominee upon expiration of the policy term. The assurance covers the sum assured plus accrued bonuses.
Eligibility criteria	◆ Minimum age to enter is 19 and maximum age to enter is 55.	◆ Minimum age to enter is 19 years and maximum age to enter is 45 years.	◆ Minimum age to enter is 19 years and maximum age to enter is 45 years.
Description	◆ This scheme is an endowment plan aimed to fulfil the insurance needs of policy holders. Loan can be availed against this policy but only after Completion of four years. Similarly, the policy can be surrender after completion of 3 years; bonus in case of surrender before 5 years is nullified.	◆ This is a money-back insurance policy, suitable for consumers who need short-term cash. This scheme offers for 2 tenures. One for 15 year and another for 20 years. For the former, benefits are paid at an interval of 6, 9, and 12 years; for the later, benefits are paid at interval of 8, 12, and 16 years.	◆ This is an endowment plan with a 10-year term. Coverage commences on the date the policy is purchased.
Minimum Sum Assured	◆ Rs 10,000	◆ --------	◆ 10,000
Maximum Amount Guaranteed	◆ Rs 1,00,000	◆ Rs 50,00,000	◆ 10,00,000

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3.7 Pension Plan

3.7.1 *Meaning*

Pension schemes offer both investment and insurance cover. By investing regularly in your pension plan, you'll accumulate a large sum over time. This will ensure steady retirement income. The PPF is a popular retirement plan in India. Early retirement contributions produce a funds to have financially stable golden future. Compounding can help a retirement plan beat inflation.

Example: Priyanka is 32 years and has an expected life of 80 years. She earns Rs. 50,000 and wants to retire at age of 60. She wants Rs. 30,000/month in retirement. How much should she invest to reach her goals by age 60? Priyanka needs Rs. 4.05 crores to earn Rs. 30,000. Assume 12% return till age 60 and 5% thereafter, with 6% inflation. She must invest Rs. 14,820 each month for 28 years to have a secure retirement.

3.7.2 *Types of Pension Plan*

- **National Pension Scheme (NPS):** The Indian government created NPS to help retired people. Some of its features are as follows: Suppose, an Individual invests in this scheme till the age of 60 years. Minimum amount of investment required is Rs 1,000 per month. Your money will be placed in debt and equity funds based on your preference. Your returns depend on your selected funds. When you retire, you can withdraw 60% of your funds. You must use the remaining 40% to buy an annuity — a retirement plan offering periodic income.
- **Public Provident Fund (PPF):** The PPF is a 15-year long-term investment scheme. Therefore, the effect of compounding is tremendous, particularly toward the conclusion of the term. You can invest up to 1.5 lakh annually in your PPF account. You can either pay in full or in twelve instalments spread out over the course of the financial year. Your PPF investments are eligible for tax deductions* under Section 80C of the Income-tax Act, 1961 (ITA). The government determines the quarterly PPF interest rate based on the income from government securities. The funds are not market-linked.

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- **Employee Provident Fund (EPF):** EPF is a government-sponsored savings vehicle for salaried workers. Both you and your employer must make equal contributions to your EPF account. Each month, your share is deducted from your salary. The Employees' Provident Fund Organization (EPFO) determines the rate of interest on investments. At retirement, you receive the total amount of your and your employer's contributions plus accumulated interest.
- **Annuity Plans with Insurance Coverage:** These plans give lifelong protection and a steady income. If a tragedy event occurs while the plan is active, your family member receives a lump sum payment; however, there are other plans that do not provide financial protection. Two types of Annuity Plans exist:
    1. **Deferred Annuity:** It is a contract with an insurance company that helps you develop a fund for retirement. You have the option of making a single premium payment or paying payments on a recurring basis during the policy's term. This scheme allows you to invest in accordance with your financial resources. Your pension begins at the conclusion of the policy period. If your retirement date is many years away, this plan is appropriate for you.
    2. **Immediate Annuity:** It is a contract between a person and an insurance company in which the person pays a lump sum and receives a lifelong income that is guaranteed and begins almost immediately.

3.7.3 *Benefits of Pension Plan*

- **Guaranteed Pension/Income:** Depending on how you invest, you can get a fixed and consistent income after retirement (delayed plan) or immediately after investing (immediate plan). This ensures financial stability at retirement.
- **Tax-Efficiency:** Certain pension plans are exempt from income tax under Section 80C. If you intend to invest in a pension plan, Chapter VI-A of the Income-tax Act of 1961 provides significant tax relief. For instance, Section 80CCD permits tax deductions for the Atal Pension Yojana (APY) and the National Pension Scheme (NPS).

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- **Liquidity:** Retirement plans lead to limited liquidity. However, some plans allow withdrawals even during the accumulation phase. This will eliminate the need to rely on bank loans or other sources to meet financial needs during times of emergency.

3.8 Unit Linked Insurance Plan

3.8.1 *Meaning*

A unit linked insurance plan (ULIP) is a multifaceted product that offers both insurance coverage and equity or bond investing exposure. This product requires regular premium payments from policyholders. The portion of the premiums is pooled with the assets of other policyholders and invested in stocks, bonds, or a combination of the two. A unit-linked insurance plan can be used for a variety of purposes, including as providing life insurance, creating wealth, producing retirement income, and funding the education of children and grandkids. Usually, an investor opens a ULIP to provide for their descendants. Beneficiaries would receive payments from a life insurance ULIP upon the death of the policyholder. The investment options of a unit-linked insurance plan are structured similarly to mutual funds where they combine investments with those of other investors. As a result, the assets of a ULIP are managed with the goal of achieving a specific investment objective. Investors have the option of purchasing shares in a single market linked ULIP fund or diversifying their holdings across many funds.

3.8.2 *Types of ULIPs*

Depending on the category of investment units, there are four types of ULIP:

- **Equity Funds:** These ULIPs generally invest in high-risk equities and company stocks. They are risky ULIP investments, but also the most rewarding. If you have a moderate to high risk tolerance and believe that fortune favors the brave, you should select one of these schemes. Here, if you win, you win big. High payoff for high risk.

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- **Income, Fixed-interest, and Bond Funds:** Under this scheme, your money will be placed in government securities, fixed-income securities, corporate bonds, and other medium-risk investments. This scheme provides low to medium reward.
- **Cash Funds:** These ULIPs invest in money market funds, cash, bank deposits, and other low-risk money market instruments. It has low-risk as well as low-reward.
- Balanced funds are the most steady and smart investment since they diversify their investments. They It invests proportionally in high-risk equities and low-risk fixed-interest products. It has High-risk with medium reward.

Based on the Investment Objectives

- To fund your child's education: This is one of a popular reason for choosing a ULIP because it protects your children and dependents from financial difficulties in the event of death of a policy holder
- To develop a corpus of funds: Idle assets can be put to work through investment plans, and a plan that also offers life insurance cover essentially kills two birds with one stone. Instead of navigating through the depths of hell to discover the right investment at the optimal interest rate and the optimal duration, investor typically allow insurance companies to manage their funds. Building a large corpus is a time-consuming endeavor when pursued using the conventional method of hard labor. ULIPs minimize your involvement in the management of money and allow you to take a slice of the profit pie.

ULIPs Based Available for Creating Wealth:

- **Life stage based vs. non-life stage based:** These plans consider themselves to be your financial aid, varying your investments between different levels of risk as you age. The strategy recognizes that an individual's goals shift throughout time and that their risk tolerance is at its maximum during their youth. Equity and debt instruments will be invested in varying proportions and at varying intervals.
- **Guarantee/non-guarantee:** Modern ULIPs provide guaranteed additions and benefits, though these are usually very long-term.

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Guaranteed ULIPs shield the investor from all types of risk, however the returns are lower. Non-guaranteed ULIPs provide a variety of investment options with varied levels of risk. While they give no guarantees, they allow you to determine where and when your money is invested.

- **Single Premium/Regular Premium:** Each individual's ability to pay a premium is unique. Single premium plans demand a single premium payment at the plan's commencement, whereas regular premium plans divide and stagger the premium payments over time.
- **To Plan for Retirement:** When your normal source of income ceases and you are no longer able to work, retirement corpus building ULIPs can come to your rescue. There are ULIP plans designed to provide for your future. They provide monthly payments once the plan expires.
- **To Meet Medical or Personal Emergencies:** Sometimes, there is unavoidable expenses. Medical emergencies, accidents, legal bills, settlement amounts, debt, etc., can cause havoc on your finances without warning. There are options that enable you to establish a nest egg and use it as a health insurance coverage. The plan permits you to access a portion of your greater maturity corpus in order to cover emergency medical expenses.

3.8.3 *Unit Linked Insurance Plan vs Mutual Fund*

Mutual Fund is a financial trust that pools funds from the investors and then invest them into bonds, stocks, money market instruments, etc. Mutual fund performance depends on underlying securities. The main purpose of the plan is to enhance investors' returns. Whereas ULIP is a product that combines both investment and insurance. It combines investment and life insurance in one plan. Mutual funds and ULIPs (Unit-Linked Insurance Plans) are two excellent investment vehicles for creating long-term wealth. However, both has its own pros and cons.

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Table 3.4

Parameter	ULIP	Mutual Fund
Investment	◆ It Combines both investment and saving. You can decide what portion will be invested in market and what portion will go to life insurance.	◆ It's a Pure Investment product. The funds generally invested either into debt or equity. The switch between insurance product and pure investment product is not possible.
Aim	◆ Long-term Investment for future wealth creation plus it provide life insurance.	◆ Short-term investment to achieve near future goals.
Tax Benefit	◆ The Premium paid on ULIP are eligible for deduction under section 80C of IT act. The Return on ULIP is Tax free.	◆ Depending on the holding period the capital gains on mutual funds are taxable. The short-term gain of equity funds is taxable at the rate of 15% whereas the long-term gains are taxable at the rate of 10%. Similarly, the long-term gain of debt is taxable at the rate of 20% after indexation. Whereas short-term capital gain is taxable according to the individual tax rate slab.
Lock In Period	◆ Minimum five Years.	◆ No Lock in Period for Regular Mutual Funds.
Risk Cover	◆ The beneficiary is provided with the sum assured in the case of demise of policyholder.	◆ The investment is transferred to the nominee in case of the demise of the policyholder.

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IN-TEXT QUESTIONS

10. _______________ are those where a part of the premium is charged for the risk cover and the rest is invested in selected mutual funds as per the choice of the investor.

(a) Mutual fund insurance

(b) Unit-linked insurance

(c) Double insurance

(d) Partial insurance

11. A policy where the policyholder makes a one-time payment of premium, is known as a _______________:

(a) Money-back policy

(b) Single premium policy

(c) Salary Savings Scheme policy

(d) Half-yearly policy

12. What is the proof of the insurance contract?

(a) Certificate

(b) Policy

(c) Receipts

(d) None of the above

13. The things or property insured is called _______________ of the insurance

(a) Subject matter

(b) Insurable interest

(c) Policy

(d) None

14. The cause of a possible loss, such as fire windstorm theft etc. is known as _______________

(a) Peril

(b) Barratry

(c) Both

(d) None

15. The term of ULIP should not be less than _______________ years.

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3.9 Summary

This lesson discusses the salient features of a broad canvas of topics related to insurance. Health insurance is a type of insurance coverage in which an insurance company agrees to guarantee compensation for medical expenses if the insured becomes ill or is injured in an accident that requires hospitalization. Property insurance protects physical goods and equipment of a business or home against losses caused by theft, fire, and other perils. Postal Life Insurance is a bouquet of life insurance policies offered by the Department of Posts for specific segments of the population namely professionals and public sector employees. Rural Postal Life Insurance is another bouquet of life insurance policies offered by the Department of Posts for rural residents. Pension plans offer a mix of insurance and investment for pension after retirement. A unit linked insurance plan (ULIP) is a product that offers both insurance coverage and equity or bond investing exposure.

3.10 Answers to In-Text Questions

1. *(a)* Health insurance
2. Personal
3. *(d)* All of those
4. *(d)* Accident insurance
5. *(a)* Floater Health Insurance Policy
6. *(a)* Burglary
7. *(c)* Loss
8. *(c)* Insured
9. *(b)* Double insurance
10. *(b)* Unit-linked insurance
11. *(b)* Single premium policy
12. *(b)* Policy
13. *(a)* Subject matter
14. *(a)* Peril
15. Five

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3.11 Self-Assessment Questions

1. Compare the Various types of health insurance plan available in India.
2. Define Postal Life Insurance and its Importance.
3. "ULIP is a combination of investment and insurance products". Explain.
4. Discuss the various types of Rural postal life insurance.
5. Explain the benefit of buying Pension Plan. Further describe how EPF are different from PPF.
6. Mention the cost covered under the Property Insurance.
7. Describe how Unit linked insurance plans are different from Mutual fund investment.

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UNIT - IV

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L E S S O N

1

Personal Tax

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STRUCTURE

1.1 *Learning Objectives*
1.2 *Introduction to Basic Tax Structure in India for Personal Tax*
1.3 *Aspects of Personal Tax Planning*
1.4 *Exemption*
1.5 *Deductions*
1.6 *e-Filing*
1.7 *Summary*
1.8 *Answers to In-Text Questions*
1.9 *Self-Assessment Questions*
1.10 *References*
1.11 *Suggested Readings*

1.1 Learning Objectives

- Understanding the concept of direct and indirect tax.
- Knowing the concept of personal tax planning.
- Understanding the concepts of deduction and exemptions under income tax.
- Understanding the concept of e-filing.

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1.2 Introduction to Basic Tax Structure in India for Personal Tax

India's tax system has its roots in prehistoric periods, when gold, silver, and agricultural produce were used as forms of payment by farmers and craftspeople. The British colonial government created the current tax structure that exists today in the year 1860.

India has a very well-organized tax system since it is the main source of funding for government agencies. The nation's overall growth and development have been aided by the tax revenue received. Every tax that is collected is supported by an ancillary law, as per Article 256 of our constitution.

1.2.1 *Role of Centre and State Government*

The Central Government and the State Governments have distinct functions under India's tax system. Taxes imposed by the Central Government include income tax, central excise duty, service tax, and customs duty. State excise duty, VAT, professional tax, land revenue, stamp duty, and tax on agricultural income are only a few of the taxes imposed by the state government. The municipality and local governments, among other local agencies, also impose some small levies.

1.2.2 *Direct Tax*

Both individuals and corporate entities are subject to direct taxes. These taxes cannot be paid by or transferred to a different person, business, or entity than the one against which they are assessed. Income tax, capital gains tax, and wealth tax are a few of these levies. Of all these taxes, income tax is the most well-known.

If an assessee's total income above the maximum amount that can be excused, they must pay income tax. The tax structure and rates are set forth in the Union Budget each year. The computation of income takes into account a number of variables, including real estate, earnings, capital gains, businesses, occupations, and other sources. Different slabs are used to categorize the income levels. Individuals, Hindu Undivided Families, Businesses, Firms, Trusts, and Cooperative Societies are all included in this.

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1.2.3 *Indirect Tax*

There is no direct payment to government officials in the case of indirect taxes. Intermediate bodies that sell the items or provide the services collect these taxes, which are imposed on commodities and services. Following is a list of a few of these:

Customs Duty: This is a charge imposed on goods imported into India from other nations.

Service Tax: Service providers are subject to this tax.

Octroi Tax: This tax, which varies from state to state based on the state government, is imposed on goods that are transported between states.

1.2.4 *GST (Goods and Services Tax)*

The Goods and Services Tax, or GST, was incorporated into India's tax system on July 1st, 2017. Both the Indian federal government and the state governments are responsible for collecting the numerous direct and indirect taxes that make up this tax. Let's examine the taxes that the Goods and Services Tax has replaced:

Central Excise Duty on Sales

Purchase Tax, Service Tax, and Entertainment Tax are the three parts of the GST:

Central Goods and Services Tax is referred to as CGST. The central government gathers this data on the supply of goods and services inside the state.

The acronym for State Goods and Services Tax is SGST. The state government gathers this data on the supply of products and services inside the state.

IGST: This represents tax imposed on supply which are made inter state.

1.3 Aspects of Personal Tax Planning

1.3.1 *Tax Planning: What is It?*

The process of analyzing a financial scenario or plan to make sure everything is in place to enable you to pay the fewest taxes possible is known as tax planning. A tax-efficient approach is one that reduces your

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overall tax liability. A financial strategy for an individual investor should include tax planning as a critical component. Success mostly depends on minimizing tax obligations and optimizing retirement plan contributions.

Tax planning takes a number of factors into account. The timing of income, the amount and timing of purchases, and the preparation for additional expenses are all taken into account. To get the best results, the types of retirement plans and investment choices must also work in tandem with the tax filing status and deductions.

1.3.2 *Why Tax Planning?*

The main goals of tax planning are as follows. Tax planning reduces tax burden by allowing the assessee to save as much tax as possible by setting up their financial operations in accordance with tax rulings. Additionally, it complies with tax law rules, reducing the likelihood of litigation. The ability to use returns for investments is one of the main advantages of tax planning. Because of the tax benefits, it is the most efficient approach to make wise investments while making the most of the resources at hand. Investing tax revenue allows white money to enter the economy and support the growth of the nation's economy. Therefore, tax planning supports both national and individual economic stability.

In India, there are numerous ways for taxpayers to save taxes. Numerous exclusions and deductions are available with these alternatives, which contribute to lowering the overall tax burden. Sections 80C through 80U offer deductions that qualified taxpayers may claim. The overall tax due is increased by these deductions. When tax planning is carried out within the parameters established by the relevant authorities, it is perfectly lawful and, in reality, a prudent move. But it's against the law to use dishonest means to evade paying taxes, and you risk fines. Tax savings can be achieved through preparation, evasion, and avoidance of taxes.

What are the Types of Tax Planning?

Now that you know as to what tax planning is, let us look at three types of tax planning.

1. Proximity and Duration Tax Planning

Annual tax planning aimed at achieving particular goals is referred to as short-term tax planning. On the other hand, long-term tax planning

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describes actions made by the assessee that do not result in an immediate payment. To put it simply, long-range planning happens early in the fiscal year, but short-range planning typically takes place at the end.

2. Authorized Tax Preparation

Tax planning is deemed permissive when carried out under the provision of a country's taxation laws.

3. Purposive Tax Planning

It is a strategy for tax preparation with a specific goal in mind. It might entail changing assets as needed and diversifying company and revenue assets dependent on residential status.

1.3.3 *The Purpose of Tax Planning*

A significant component of your total financial planning is tax planning. Less burdens from paying less in taxes will enable you to design your financial objective in accordance with your needs and aspirations. The following are some goals of tax planning:

1. A lower tax obligation
2. Investment that yields results
3. Economic expansion
4. Reduction of litigation
5. Stability of the economy

1.3.4 *How to Get Started with Tax Planning?*

1. To begin with, consider your entire revenue. This is where the procedure begins, and it calls for you to determine your monthly and annual income with accuracy.
2. Consider the parts of your income that are taxable. In addition to base pay, housing and rent allowances included in the compensation are not taxed. On the other hand, investment gains may increase taxable income. Thus, in order to be able to plan taxes, one must be aware of their taxable income.
3. Utilize deductions to lower the overall amount of taxable income. Pay structures and careful investment planning can help achieve this. For instance, the tax rate on interest earned from a fixed deposit is equal to that of income.

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IN-TEXT QUESTIONS

1. Which of the following s not a purpose of tax planning?

(a) lower tax obligation

(b) Investment that yields results

(c) Economic expansion 4. Reduction of litigation

(d) Tax Evasion.

2. Which of the following is not indirect tax?

(a) GST

(b) Custom duty

(c) Excise duty

(d) Corporate tax

3. The purpose of tax planning is to

(a) Reduce the tax burden

(b) Reduce the tax incidence

(c) Avoid tax

(d) Tax evasion

4. Reducing tax liability, utilizing the deductions, exemptions or reliefs allowed in the Act and Rules is called:

(a) Tax evasion

(b) Tax planning

(c) Tax avoidance

(d) Tax management

5. Using the loopholes of law to reduce tax is known as

(a) Tax evasion

(b) Tax planning

(c) Tax avoidance

(d) Tax management

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1.4 Exemption

An assessee's total income is not comprised of the numerous types of revenue mentioned in the various clauses of section 10. We refer to these incomes as exempted incomes. As a result, the calculation of taxable income will not include such income.

Additionally, some revenues are included in gross total income but can be fully or partially deducted under Chapter VI-A when calculating total income. Pupils should be aware of this crucial distinction between the deduction under Chapter VI-A and the exemption under Section 10.

Exemption of Allowances For Salaried Employees

1.4.1 *House Rent Allowance (HRA)*

Individuals who live in a rented house/apartment can claim HRA to lower tax outgo. HRA can be wholly or partially exempted from tax. House Rent Allowance (HRA) is a tax benefit provided to employees occupying government or statutory offices whose income does not exceed the prescribed limit.

You can claim the following as HRA exemption-

- Rent paid less than 10% of the Basic salary + DA.
- Total HRA as received from the employer.
- 40% of the salary for non-metros and 50% of wages for metro cities.
- Actual rent should be less than 10% of a person's basic salary + DA.
- Leave Travel Allowance

Salaried individuals can get their travel within India exempted from tax. This allowance is applicable for only short distances and can be availed once every year.

Salaried individuals can take only their spouse, children, and parents on this trip. The exemption is allowed on producing original bills of expense.

1.4.2 *Leave Travel Exemption*

- LTA covers domestic travel only.
- The mode of travel should be railways, airways, or public transport.

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- An actual journey is a must to claim the exemption.
- The exemption for travel is allowed for the employee alone or with his immediate family only.

1.4.3 *Standard Deduction*

Re-introduced in the 2018 budget, this deduction has replaced the previously used conveyance allowance and medical allowance. As a result, an employee can claim a flat Rs. 40,000 deduction from the total income instead of stating the bifurcation between travel and health as done previously.

Later, the limit of Rs. 40,000 was increased to Rs. 50,000 in the Interim Budget 2019.

Exemption Under Section 89(1) and 10 (10C)

If you have received a portion of your salary in advance, you are allowed some tax relief under Section 89(1).

The same is exempted from tax if you receive compensation for voluntary retirement or separation. This provision is detailed in Section 10(10C). However, the exemption is subjected to the pre-requisite that the receipts comply with rule 2BA and the maximum compensation received does not exceed Rs. 5,00,000.

Many government savings schemes are also included under the deduction of income tax for salaried individuals. These tax savings options are covered under sections 80C, 80CCC, 80CCD, and 80D.

- **Other Exemptions**
- **Exemption from the Receipt Upon Opting for Voluntary Retirement**
- The same is exempted from tax if you receive any compensation on voluntary retirement or separation. This provision is detailed in Section 10(10C). However, the exemption is subjected to the pre-requisite that the receipts comply with rule 2BA and the maximum compensation received does not exceed Rs. 5,00,000.
- **Pension:** Pension received is considered as salary and thus is taxable.
- **Gratuity:** Gratuity is a retirement benefit that an employer provides. An employee is entitled to gratuity upon completing five years of

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service in that company. However, the amount is paid upon retirement or resignation. Tax treatment of gratuity is complex and depends on the employer's coverage under the Payment of Gratuity Act. Thus, you should coordinate with your HR for further information on this.

1.4.4 *Leave Encashment*

According to labour laws, all salaried individuals are entitled to a minimum amount of paid leave each year. It is not required, though, for a single employee to take all of the leave to which he is entitled in a given year. Actually, the majority of firms provide their workers the choice to roll over any unused paid time off.

When the person retired or resigned from the company, whichever came first, they would inevitably have accrued unused leave balance. This forces the business to reimburse the workers for any unused paid time off. Leave encashment is a more popular term for this idea.

Particulars	Amount (Rs)
Leave encashment received (A)	**XXXX**
Less: Exemption under Section 10(10AA) – (B) Least of the following:	**XXXX**
i) Amount notified by the Government** Rs 25,00,000 (C) ii) Actual leave encashment amount (D) iii) Average salary* of last 10 months (E) iv) Salary per day *unutilised leave (considering maximum 30 days leave per year) for every year of completed service (F)	25,00,000 XXXX XXXX XXXX
Leave encashment taxable – (A) – (B)	**XXXX**

Figure 1.1

Amounts that a Member Receives from HUF Revenue [Section 10(2)]

(i) A HUF is a "person," as defined in Chapter 1, and as such, is an assessment unit for the purposes of the Act. The HUF is responsible for assessing its own income.

(ii) Section 10(2) states that members of a HUF are exempt from paying tax on any amounts they receive from their family, preventing the

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double taxation of the same income—once in the hands of the HUF that generates it and once in the hands of a member when it is paid out to him.

(iii) The exemption only pertains to payments made to members of the HUF by the organization.

Interest on Funds to an Individual's Credit in his NRE Account [Section 10(4)(ii)]

According to section 10(4)(ii), an individual is exempt from paying taxes on any interest earned on funds held in a Non-resident (External) Account (NRE A/c) at any Indian bank in accordance with the Foreign Exchange Management Act, 1999 (FEMA, 1999) and its implementing regulations, provided that the individual: o is a person resident outside India, as defined by FEMA, 1999; or is an individual who has been granted permission to keep such an account by the Reserve Bank of India.

1.4.5 *Remuneration Received by Individuals, who are not Citizens of India [Section 10(6)]*

(i) Compensation received by representatives of foreign state embassies, etc. [Section 10(6)(ii)]

A person is exempt from paying taxes for services rendered as an official of a foreign state in the capacity of an embassy, high commission, legation, commission, consulate, or trade representation, or as a staff member of any of these entities.

Conditions:

(a) Our equivalent government officials' or employees' salaries that they get while living in these foreign nations should be exempt.

(b) The staff members listed above should be citizens of the nations that are represented, and they should not be involved in any other businesses, professions, or jobs in India.

(ii) Payment received for services performed in India while working for a foreign company [Section 10(6)(vi)]

Tax exemption also applies to compensation that a foreign national receives when working for a foreign company for services performed while he is in India.

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Conditions:

(a) The foreign company is not involved in any trade or activity;

(b) The employee spent no more than 90 days in India in the preceding year;

(c) The compensation is not subject to withholding from the employer's income that is subject to Act-related taxes.

1.4.6 *Compensation Received on Account of Disaster [Section 10(10BC)]*

(i) This provision excludes any money that a person or his legal heir may receive as compensation for a tragedy.

(ii) The federal government, a state government, or a local government ought to provide such compensation.

(iii) The Act has already permitted a deduction for compensation for mitigating any damage or loss, thus this exception would not apply to that amount.

(iv) "Disaster" refers to any catastrophe, tragedy, calamity, or serious incident that occurs anywhere and can be caused by accident, carelessness, or natural or artificial causes. It should result in one of three things: (1) a significant loss of life or significant suffering for humans; (2) property damage and destruction; or (3)

Section 10(11A)] Payment from Sukanya Samriddhi Account

According to Section 10(11A), any payment made under the Government Savings Bank Act, 1873, from an account formed in compliance with the Sukanya Samriddhi Account Rules, 2014, is not to be included in the assessee's total income.

As a result, interest earned on deposits made into and withdrawals made from any account under the aforementioned plan would not be charged.

Section 10(16) Provides Subsidies for Education.

Regardless of the amount or source of the scholarship, the value awarded to the recipient to cover educational expenses is free from taxes in their hands.

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Members of Parliament and State Legislatures shall not be Paid the following Incomes:

(i) Daily stipend: Any member of Parliament, state legislature, or committee thereof may receive a daily stipend.

The Constituency Allowance of MPs refers to any allowance received by a Member of Parliament under the Members of Parliament (Constituency Allowance) Rules, 1986. Similarly, the Constituency Allowance of MLAs is any amount received by an individual as a result of their membership in a State Legislature under any Act or rules established by that State Legislature.

Government Rewards for Works of Literature, Science, and Art as well as other Accolades [Section 10(17A)]

This clause exempts from application any award made in the public interest by the Central or State Government, or by any other body authorized by the Central Government, as well as any prize made by the Central or State Government for whatever purposes the Central Government may deem appropriate in the public interest.

A Sikkimese Individual's Specified Income [Section 10(26AAA)]

(i) The following income would not be subject to income tax if it were earned or arises for a Sikkimese individual:

(a) Income in the State of Sikkim from any source; or (b) Income from dividends or interest on securities.

(ii) A Sikkimese lady who marries a non-Sikkimese person on or after April 1, 2008, will not be eligible for this exemption, nevertheless.

IN-TEXT QUESTIONS

6. Incomes which are not included in total income of the assessee are called.

(a) Exempt Incomes

(b) Taxable Incomes

(c) Incomes deductible/c VI-A

(d) None of the above

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7. Any sum received by an Individual as a member of HUF from the income of HUF shall be .
   (a) Fully taxable
   (b) Fully exempt u/s 10(2)
   (c) Fully taxable u/h "Salary"
   (d) Taxable @ 15%
8. Paid by Government of India to a Citizen of India for rendering services outside India is Exempt u/s 10(7).
   (a) Salary
   (b) Allowance& perquisites
   (c) Both *(a)* & *(b)*
   (d) None of the
9. ____________is one of the component considered for HRA in case of employee is residing in Delhi.
   (a) 50%
   (b) 60%
   (c) 40%
   (d) 30%

1.5 Deductions

As we've already seen, some incomes are excluded under clause 10. These types of revenue are not included in the calculating process and are not included in the total income. Conversely, gross total income deductions are found in Chapter VI-A. It's crucial to remember that no deductions will be allowed in the absence of gross total income. There are deductions for specific payments, deductions for certain incomes, deductions for other income, and other deductions in this chapter.

Section 80C

Section 80C provides for a deduction from the Gross Total Income of savings in specified modes of investments. The deduction under section

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80C is available only to an individual or HUF. The maximum permissible deduction under section 80C is Rs. 1,50,000. The following are the investments/contributions eligible for deduction:

- Contribution in Unit-linked Insurance Plan 1971
- Contribution in Unit-linked Insurance Plan of LIC Mutual Fund
- Premium paid in respect of Life Insurance policy
- Contribution to SPF/PPF/RPF
- Contribution to approved superannuation Fund
- Any sum paid or deposited in Sukanya Samridhi Account..
- Subscription to National Savings Certificates VIII
- Contribution to approved annuity plan of LIC
- Subscription towards notified units of mutual fund or UTI
- Contribution to notified pension fund set up by mutual fund or UTI
- Contribution to National Housing Bank (Tax Saving) Term Deposit Scheme, 2008
- Repayment of housing loan including stamp duty, registration fee and other expenses
- Subscription to certain equity shares or debentures

Deduction in Respect of Contribution to Certain Pension Funds [Section 80CCC]

Eligible assessee: An individual assessee who paid or deposited any amount from his income that was subject to tax in the prior year to establish or maintain a contract for an annuity plan of LIC of India or another insurer in order to receive pension payments from the fund established by LIC or such other insurer is eligible to deduct that amount from his total income.

Maximum Deduction: The maximum permissible deduction is Rs. 1,50,000 (Further, the overall limit of Rs. 1,50,000 prescribed in section 80CCE will continue to be applicable i.e. the maximum permissible deduction under sections 80C, 80CCC and 80CCD(1) put together is Rs. 1,50,000).

Deemed Income: Where any amount standing to the credit of the assessee in the fund in respect of which a deduction has been allowed, together

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with interest or bonus accrued or credited to the assessee's account is received by the assessee or his nominee on account of the surrender of the annuity plan in any previous year or as pension received from the annuity plan, such amount will be deemed to be the income of the assessee or the nominee in that previous year in which such withdrawal is made or pension is received. It will be chargeable to tax as income of that previous year.

Section 80CCD

Section 80CCD aims to encourage the habit of savings among individuals, providing them an incentive for investing in pension schemes which are notified by the Central Government. Contributions made by an individual and his/her employer, both are eligible for tax deduction, subject to the deduction being less than 10% of the salary of the person. Only individual taxpayers are eligible for this deduction.

Section 80CCD(1): All individuals who have subscribed to the National Pension Scheme (NPS) will be eligible to claim tax benefits under Section 80 CCD (1) up to the limit of Rs. 1.5 lakh. In addition to that, an exclusive tax deduction for investments of up to Rs. 50,000 in NPS (Tier I account) can be availed by the subscribers under Section 80 CCD (1B).

Section 80D

Section 80D of the Income-tax Act, 1961 offers deduction for money spent on health insurance and maintaining your health, and is significant for your tax planning and personal finance.

Insured	Deduction Amt. (₹)	
	Age Below 60 yrs.	Age Above 60 yrs.
Self, Spouse and Children	25,000	50,000
Parents	25,000	50,000
Max Deduction	**50,000**	**1,00,000**
Opt: Preventive Healthcare*	5,000	5,000

Table 1: Medical Deduction u/s 80D

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Individuals beyond 80 years of age typically do not qualify for health insurance. Therefore, even if funds are used for their treatment rather than for health insurance premiums, a deduction of up to <50,000 is permitted.

Consequently, the highest deduction allowed by this section is ~55,000.

Deduction in Respect of Maintenance Including Medical treatment of a Dependant Disabled [Section 80DD]

Section 80 DD provides for tax deduction for families taking care of a disabled family member so that they can take proper care of the dependent without any burden. It is to be noted that such deductions under section 80 DD can only be claimed by the family of the disabled person and not the person himself. In case the disabled person has already claimed deduction, section 80 DD will not be applicable to the family members. The deduction limit permitted u/s 80 DD is up to Rs. 75,000 in cases of disability up to 40%. The annual limit for availing deductions u/s 80 DD is Rs. 1.25 Lakhs per annum for taking care of a disabled person with disability up to 80% or more.

Dependents comprise of parents, spouse, siblings, children or any other family member who is under a HUF.

Section 80DDB

- Deductions under Section 80DDB can be claimed only by individuals and HUFs.
- No deduction under this section can be claimed by corporates or any other entity.
- The deduction under section 80DDB can be claimed only by the assessee who is a resident of India during the relevant previous year that is the section does not apply to non-resident Indians.
- The deduction can be claimed only by the person who has actually incurred the expenses.

Thus, if an assessee incurs expense on medical treatment of a specified disease or ailment of Rs. 60,000/-, then he can claim a deduction of Rs. 40,000/- under section 80DDB. However, if the assessee has received an amount of Rs. 30,000/- from an insurance company against such expenses, then the amount of deduction that he can claim under section 80DDB stands reduced by such amount. Thus, the assessee can then claim only

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an amount of Rs. 10,000 /- (Rs. 40,000 less the amount received from the insurance company Rs. 30,000) under Section 80DDB.

Section 80E

Section 80E education loan deduction is a tax incentive given to people who avail education loan for higher studies. This deduction is available only on the interest amount paid on the loan and not on the principal amount. Education Loan deduction can be claimed for a maximum of eight years, starting from the year in which interest repayment begins.

Section 80TTB

(i) A senior citizen (a resident who was 60 years of age or older at any point in the relevant prior year) is an eligible assessee if their gross total income includes interest from savings and fixed deposit accounts.

   (a) A financial institution covered by the 1949 Banking Regulation Act

   (b) A co-operative society that conducts banking operations (such as a cooperative bank for land development or mortgage).

   (c) A Post Office.

(ii) Deduction amount: Actual interest earned on deposits or $50,000, whichever is less.

When interest income is obtained from any deposit held by, or on behalf of, a firm, an AOP, or a BOI, (iii) No deduction is available to the partner or member.

Section 80G

The Income-tax Act's Section 80G deduction allows taxpayers to deduct amounts paid as donations to any fund, institution, or charitable trust. The Income-tax Act does not treat all donations similarly. Contributions made to certain funds and organizations are 100% or 50% deductible, with no upper limit. However, some donations are eligible for a 100% or 50% deduction, depending on the qualifying limit.

Donations Eligible for Income Tax Deduction under Section 80G

Any donation of over Rs. 2000 made by way of cash will not be eligible for deduction under Section 80G from 1st April, 2017. Hence, make all

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donations over Rs. 2000 by way of cheque, demand draft, bank transfer, credit card or debit card.

Qualifying Limit for Section 80G Deduction

100% Deductible without Qualifying Limit

- National Defence Fund set up by the Central Government
- Prime Minister's National Relief Fund
- National Foundation for Communal Harmony
- An approved university/educational institution of National eminence
- Zila Saksharta Samiti constituted in any district under the chairmanship of the Collector of that district
- Fund set up by a state government for medical relief to the poor
- National Illness Assistance Fund
- National Blood Transfusion Council or any State Blood Transfusion Council
- National Trust for Welfare of Persons with Autism, Cerebral Palsy, Mental Retardation, and Multiple Disabilities
- National Sports Fund
- National Cultural Fund
- Fund for Technology Development and Application
- National Children's Fund
- Chief Minister's Relief Fund or Lieutenant Governor's Relief Fund with respect to any State or Union Territory
- The Army Central Welfare Fund or the Indian Naval Benevolent Fund or the Air Force Central Welfare Fund, Andhra Pradesh Chief Minister's Cyclone Relief Fund, 1996
- The Maharashtra Chief Minister's Relief Fund during October 1, 1993, and October 6, 1993
- Chief Minister's Earthquake Relief Fund, Maharashtra
- Any fund set up by the State Government of Gujarat exclusively for providing relief to the victims of the earthquake in Gujarat

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- Any trust, institution or fund to which Section 80G(5C) applies for providing relief to the victims of the earthquake in Gujarat (contribution made between January 26, 2001, and September 30, 2001)
- Prime Minister's Armenia Earthquake Relief Fund
- Africa (Public Contributions – India) Fund
- Swachh Bharat Kosh (applicable from FY 2014-15)
- Clean Ganga Fund (applicable from FY 2014-15)

National Fund for Control of Drug Abuse (applicable from FY 2015-16)

List of Donations Eligible for 50% Deduction without Qualifying Limit.

- Prime Minister's Drought Relief Fund
- Jawaharlal Nehru Memorial Fund
- Indira Gandhi Memorial Trust
- Rajiv Gandhi Foundation

List of donations eligible for 100% deduction subject to 10% of adjusted gross total income.

- Donations to the government or any approved local authority, institution or association to be utilised to promote family planning
- Donation by a company to the Indian Olympic Association or any other notified association or institution established in India to develop infrastructure for sports and games in India or sponsor sports and games in India.

Section 80GGA

Section 80GGA allows deductions for donations made towards scientific research or rural development. This deduction is allowed to all assessees except those who have an income (or loss) from a business and/or a profession.

Section 80GG

Section 80GG allows you to claim a deduction for rent paid even if your salary does not include the HRA component or by self-employed individuals having income other than salary. The condition is that you should not own any residential accommodation in the place of residence to claim deduction under Section 80GG.

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Section 80GG deduction will be allowed as lowest of below mentioned:

- Rs 5,000 per month
- 25% of the adjusted total income
- Actual rent minus 10% of adjusted total income

What is adjusted total income?

Adjusted gross total income is the gross total income (sum of income under all heads) reduced by the aggregate of the following:

- Amount deductible under Sections 80C to 80U (but not Section 80G)
- Exempt income
- Long-term capital gains
- Short-term capital gains u/s 111A
- Income referred to in Sections 115A, 115AB, 115AC, 115AD and 115D

IN-TEXT QUESTIONS

10. Donation is deductible under section

(a) 80C

(b) 80D

(c) 80E

(d) 80G

11. Which of the following donations is eligible for 100 % deduction?

(a) Help to poor

(b) National Defense

(c) Rajiv Gandhi Foundation

(d) Any notified temple

12. Deduction on interest on loan taken for studies fall under _____.

(a) 80CC

(b) 80C

(c) 80E

(d) 80D

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Notes

13. Contribution to RPF is deducted u/s____________

(a) 80C

(b) 80D

(c) 80E

(d) 80G

14. Which among the following deduction is available only to disabled persons

(a) 80C

(b) 80G

(c) 80Q

(d) 80U

1.6 e-Filing

e-Filing refers to the process of submitting your tax returns electronically. Short for electronic filing, e-Filing can be completed through income tax website. e-Filing can be used by all taxpayers.

e-Filing offers speed, security, and convenience to taxpayers. It also reduces the income tax department's burden and provides a sophisticated alternative to traditional paper filing.

Under the new tax regime, you must file the return if your total income in a financial year exceeds the prescribed income tax exemption level of Rs. 3 lakh. Under the previous tax system, an individual taxpayer's income tax exemption was Rs. 2.5 lakh, resident senior citizen taxpayers between the ages of 60 and 80 were eligible for Rs. 3 lakh, and resident super senior citizen taxpayers who were 80 years of age or beyond were eligible for Rs. 5 lakh.

ITRs must be filed by businesses, regardless of whether they are profitable or not.

If you invest in or receive income from foreign assets, you must file an ITR.

Why to File ITR?

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All taxpayers are responsible for filing an Income Tax Return (ITR) every year if the total income is above specified threshold or said person fall in category of person who are mandatorily required to file their Income tax returns.

All taxpayers are mandated to submit an Income Tax Return (ITR) every year by respective due dates as per the law to report their income and claim a tax refund, if applicable. Taxpayers who fail to file their return will have to pay fees of Rs. 5,000 (Rs. 1,000 if the total income is less than Rs. 5 lakh) under Section 234F.

Steps to File ITR

- Step 1 - Go to the Income Tax e-filing website
- Step 2 - Register or Log in to the website
- Step 3 - Enter the required details
- Step 4 - Select the mode of Filing
- Step 5 - Select the status
- Step 6 - Select the appropriate ITR form
- Step 7 - If you select ITR 1
- Step 8 - If you select ITR 4
- Step 9 - Summary of tax computation
- Step 10 - Proceed to validation
- Step 11 - Submit the ITR

1.7 Summary

In this chapter we came across various aspects of personal taxation involving what is it and why there is need of personal taxation in which we discussed about the basic structure of personal taxation and how it is designed after having clear understanding of the same we move towards various exemptions and deductions which are available for individuals in which we discussed thoroughly about prominent deductions under chapter VI-A available to individuals from section 80c to 80u and we also discussed about various exemptions which do not form part of total income right from very inception. At last, we discussed E -Filling and its importance involving the steps to file ITR.

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Notes

1.8 Answers to In-Text Questions

1. *(d)* Tax Evasion.
2. *(d)* Corporate tax
3. *(a)* Reduce the tax burden
4. *(b)* Tax planning
5. *(b)* Tax planning
6. *(a* Exempt Incomes
7. *(b)* Fully exempt u/s 10(2)
8. *(b)*Allowance& perquisites
9. *(b)*60%
10. *(c)* 80E
11. *(b)* National Defense
12. *(c)* 80E
13. *(b)* 80D
14. *(d)* 80U

1.9 Self-Assessment Questions

1. What is tax planning?
2. Discuss the exemptions available to individual.
3. What are the deductions, which an individual can avail?

1.10 References

- Introduction to Financial Planning (4th Edition 2017) – Indian Institute of Banking & Finance.
- Sinha, Madhu. *Financial Planning: A Ready Reckoner July 2017*, McGraw Hill.

1.11 Suggested Readings

- Halan, Monika. *Lets Talk Money: You've Worked Hard for It, Now Make It Work for You, July 2018,* Harper Business.
- Pandit, Amar. *The Only Financial Planning Book that You Will Ever Need,* Network 18 Publication Ltd.

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Glossary

Actuary: Actuaries are the experts and work with an insurance company. They analyze data to assess risk and help insurance firms to a set price of the Insurance Product**.**

Bill Discounting: The bank takes the bill from the borrower on his customer and after deducting some amount as discount or commission, pays the balance immediately.

Burglary: Coverage against loss as a result of forced entry into premises.

Collateral: Any asset given as security to the bank to ensure repayment of loan and it can be seized by the bank in case of non-payment.

Consumer Durable Products: All products expected to have a long useful life after purchase e.g., furniture, appliances etc.

Cooperative Banks: A small sized financial institution whose members are the owners and also the customers of the bank. It operates for the benefit of its members.

Death Benefit: The 'Death Benefit' is paid to the nominee if the person whose life is assured dies during the policy term. Sum assured and death benefit are not the same. Death benefit can be sum guaranteed or even greater, including rider and/or other advantages. Term insurance has no bonus or guaranteed additions.

Insured: This refers to the person(s) that an insurance policy provides coverage for.

Insurer: The insurer is the insurance firm that sells the insurance product.

Life Assured: It is the person who is covered under the insurance policy.

Life Cover: It is the amount that the Insurer will pay to the nominee in the case of cessation of life of the individual (insured).

Loss: "Loss" refers to damage caused to an insured piece of property.

Maturity Benefit: For Protection + Savings policies, the Insurer (insurance company) pays a certain lump sum of money on completion of the policy term. This amount is known as the Maturity Amount.

Nominee or Beneficiary: It is the person you appoint at the time of buying the policy to receive the benefits of your insurance policy, in your absence.

Peril: Perils are the causes of damage to your insured property that your policy protects against. Lightning, windstorms, fire are examples of Peril.

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Policy Term: The number of years for which the Life Cover continues.

Premium: A premium is an amount that is paid to the insurer for receiving the benefits of the insurance policy. These payments can be made on a regular basis throughout the policy duration, for a limited number of years, or just once, as per the options available under the policy you choose.

Proposer: It is the person who pays the premiums of the policy. For example: If you have bought the policy for yourself, then you are both the Life Assured as well as the Proposer. Similarly, if you purchase an insurance policy for a family member, then you are the proposer, and the family member is the Life Assured.

Reinstatement: The restoring of a lapsed policy to full force and effect.

Riders: Riders are additional benefits that can be added to an insurance policy for a slightly higher price. Different insurers provide a number of riders for endowment policies.

Risk: Risk is the possibility that a loss will occur.

Sum Assured: It is the amount the insurer agrees to pay in the case of an occurrence of event, such as death.

Surrender Value: If the policyholder terminates the plan before maturity, the insurance company pays the amount to the person is called Surrender Value.

Tax Benefit: All payments paid towards a life insurance plan are tax deductible under Section 80 (C) of the Income Tax Act, 1961. Maximum deduction is Rs. 1.5 lakh.

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