Mutual Funds versus ULIPS

Abstract:

This paper has been written with the understanding that the contents of the paper are well known to the Actuaries and other Professionals related to the field of Finance and Investment. However the necessity to submit a paper in this context arose from the bare fact that certain articles keep appearing in News Papers' columns, and discussions are held under investment programme over business channels in media and other platform where an individual states his/ her income and expenditure and seeks expert advice to make an investment choice between Mutual Funds and Unit Linked Insurance policies (ULIPs). The investment expert depending on his/ her field of expertise generally suggests some solution. Some times solutions given suggest that all aspects of both the investment vehicles are not evaluated properly and completely.

We also felt that even persons working in Insurance Companies often compare ULIPs policies unfavorably with Mutual funds on the grounds that charges in UL policies are higher and ULIPs are less flexible than mutual funds.

In this paper, we have tried to present comprehensive information about both the investment vehicles. We tried to emphasize that ULIP policies over long duration are equally , if not more, competitive in terms of charges and flexibility. The paper has been divided into following sections:

1. Introduction,
2. MFs V/S ULIPs,
3. Comparisons between MFs and ULIPs
4. Conclusion
5. Acknowledgement
6. Appendix

1. Introduction:

1.1 There is long history of comparing the Life Insurance products with investment vehicles issued by other financial institutions despite the fact that nature of the Life Insurance products and other financial institutions is different. There is an attempt on our part to help the readers, investing public and sales people to make informed decisions while comparing, purchasing or selling the products. The paper may also help to reply to such perception as investment in Mutual Funds is better than investment in ULIPs, or a combo of pure term insurance and mutual fund is better than ULIP or now because of tax treatment MFs have an edge etc….

1.2 We tried to laid down the facts and the aim is not to prove the superiority of one investment vehicle over another but to compare both in the light of comprehensive information about them and to bring to the fore the insight that both serve divergent investment objectives and hence both can coexist in the Indian Investment space.

2. MFs V/S ULIPs

2.1 The definition of Mutual Funds by SEBI and AMFI are given in Appendix's s*ubsection A under heading* "What is Mutual Fund" along with the IAIS definition of Insurance which is given under heading "What is Life Insurance"? ULIPs stated here are the products issued by the Life Insurance companies.

2.2 Terminology used in MFs is given in subsection B under heading "Some Terminology used in Mutual Funds" in Appendix as recap and for those who would wish to know them.

2.3 IRDA had defined different charges while issuing the new ULIP Guidelines. These are given under Subsection C of Appendix under heading "Terminologies regarding charges used in life Insurance Unit Linked Plans". These are used by most of the readers on day-to-day basis.

2.4 We also understand that MF companies and Life Insurance companies operate under strong regulatory framework. Excerpts are given in Appendix under Subsection D under headings Regulatory aspects In Mutual Funds and Regulatory aspects for Life Insurance Companies.

2.5 The taxation aspects are given in Appendix, Subsection Eunder heading - Taxation aspects in Mutual Funds and Taxation aspects for Life Insurance Companies.

2.6 Subsection F of Appendix states Asset Under Management under a few MFs .

3. Comparisions between MFs and ULIPs

3.1 To begin with the question, which comes to our mind, whether MFs and ULIPs are comparable? Ironically, though a fact that when two term insurance plans offered by the two different Life Insurance companies are compared, then generally simply premium per thousand is compared without taking into account other features such as Options, for example.

3.2 During pre-libralisation of Insurance Industry, LIC's Endowment and Money Back Policies were compared with Recurring Deposits of Banks or Post Offices, National Savings Certificates, Kisan Vikas Patra etc. The comparisons are still made with the returns offered by these financial instruments. It is natural for investing public to make comparison between MFs and ULIPs. Integration of Financial Institutions is on cards and is happening in other advanced countries. Same group may be offering Life Insurance, General Insurance, Mutual Funds and Banking instruments and in such situation comparison become inevitable. But fact is that comparison should be made one like to like basis and as a whole taking into account all features rather then on the basis of conveniently selected features.

3.3 Comparison of features:

3.3.1 In ULIPs, there are three types of charges- asset related charge which is reflected in NAV, premium related charge which is deducted from premium before allocating the same to unit account of policyholders and unit related charge which are deducted from unit account of the policyholder.

3.3.2 In MFs also all three types of charges exist but generally either premium related (contribution to MF) called entry load or unit related called exit load will be applicable in a scheme. There are schemes where only asset related charge is applicable.

3.3.3 As given in Sub Section D of Appendix, Recurring Expenses in MFs is charged to the funds and is recurring in nature. This charge is a fixed percentage chargeable over the entire fund value on an annualised basis. This charges corresponds to Fund Management charge (FMC) in UL policies. This charge for mutual fund generally varies from 1.75% to 2.5% with 2.25% common in most of the MF schemes. This charge(ie FMC is much lower in ULIPs available in the market and is generally varies from 0.75% to 1.75% depending on the type of linked fund and level of equity exposure in the fund. Generally higher the proportion of equity, the higher is the charge.

3.3.4 Typically in ULIPs the premium related charge is very high on first year premium and lower on subsequent premium.

3.3.5 Although charges in ULIP appears to be high due to premium related charges but since asset related charges (ie FMC) is lower in ULIPs, over a longer duration of over 10 years, the total charges deducted from UL actually are either at similar level or even lower than total charges on MF over the same period. This has been illustrated using some examples in the following section.

3.3.6 The customers of ULIPs have the option to switch across funds and first few switches are free of charge in a policy year. This provides very good investment flexibility to the customer enabling him to change his/her risk profile based on changing risk-taking ability over his/her lifetime. In MFs, the switching of investment from one fund is not cost free.

3.3.7 In ULIPs, there is flexibility to make additional investment through single top-ups if policyholder has extra cash sum to invest and regular top-ups wherein the premium allocation charge is much lower. Although, now there are certain condition such as compulsory increase in risk cover if top-up exceeds a certain minimum threshold but after a few years from commencement of policy, this threshold is good enough. In this regards, MF are fully flexible.

3.3.8 The ULIPs also provided liquidity in that customer can withdraw funds from the unit account generally without any exit load up to a certain number of withdrawals although there could be certain minimum restrictions on amount of withdrawal. MFs in this regard are very flexible although there could be exit load.

3.3.9 The customer of ULIPs also have the option to choose more than one funds and choose an allocation ratio for investment of premium in different funds at the time of paying his/her premium, which enables him/her to customise his investment based on his risk appetite at that time. This ratio can also be changed free of charge, if customer so desires.

3.3.10 The fund manager of Life Insurance Companies are not under redemption pressure in a bearish market, leading to higher average annualised returns in the long term in case of Ulips. This works against a retail customer in case of MFs where the charges are dependent on total fund, since redemption pressure forces the fund manager to sell, even though s/he may want to hold back the investments.

3.3.11 It is argued that MFs have an edge that they have multiple fund options including sector specific funds. But the retail investors having limited fund to invest may not use them optimum. Also, as ULIP market grows, the Insurance companies may also offer as many choices. In developed markets, ULIPs offer variety of fund options.

3.3.12 The MFs offer systematic investment plan (SIP) to customer to avoid losses due to timing of investment. The regular premium ULIPs are SIP by design and particularly offer identical feature if premium payment frequency is monthly. Customer need not give post dated cheques or direct debt mandate, if she/he so desires, in ULIPs unlike in MFs. The Insurance companies generally send premium due reminders to policyholders regularly.

3.3.13 Often it is said that mutual fund plus term insurance (MF plus TA) combo is better than ULIPs. However, ULIP design offers a unique feature where risk cover is high initially but reduces gradually as fund value increases and reduced to zero in most of finite term ULIPs. This feature is very good for young married customer when need of risk cover is highest. Also, many ULIPs offer customer to increase or decrease sum assured within ,subject to certain conditions. This is not possible in MF plus TA combo.
ULIPs also offer other risk benefits throgh riders. These are add-on to the base policy, which MFs do not offer.

3.3.14 It is also argued that MFs have better fund management expertise than Life Insurance Companies, which may be true to some extent, but as ULIP market grows the funds under management will also grow rapidly given the long term nature of the products and payment of renewal premiums. This will enable insurance companies to afford equally efficient fund management team.MFS are relatively short-term investment and in closed fund new contribution do not come.

3.3.15 In ULIP, there is a lock in period of 3 years that is not the case with MFs. Over a short-term period, the charges under MFs are lower than that in ULIPs.

3.3.16 MFs suit to those customer better who wants to invest for shorter term and where investment size is very large. ULIPs suit better to those who want to contribute small amounts regularly and over loner term period.

3.3.17 In case of Ulips, customers enjoy the additional advantage of leveraging the power of assignment, which is unique and can be used as collateral secutity.

3.3.18 If the Life Insurance Policies including ULIPs are taken under Married Women Property Act (MWP Act) then in case of insolvency of the proposer, such policies may not be confiscated.

3.3.19 Life Insurance Companies are having specific rural and social sector obligation and thus these companies are engaged in upliftment of such sectors by providing them security. No such regulation appears to be applying to MFs.

3.4 Comparison of Charges in MFs and ULIPs

3.4.1 As level of charges effects fund value that customer receives and thus, the return earned by the customer on his investment (customer's IRR), we tried to compare charges MFs plus TA combo, MFs with five ULIPs products of 10 years, 15years and 20 year term in this section. We compared fund values at the end of each 5years interval. We have also calculated the reduction in yield, which reflect the impact of total charges under two investment vehicles. The reduction in yield can be treated, as equivalent fund management charge over the term of the policy assuming there is only this charge.

Assumptions:

Age at entry	35 years
Initial entry Load MF	2.25%
Recurring Charge of MF	2.25%
Fund growth rate for both MF and ULIPs	10%
Annual Contribution/Premium	Rs.50,000

3.4.2 In Table A, we calculated values at the end of each five years interval for 10,15 and 20 years term policies for 5 ULIP products with sum assured of 5 lacs and 10 lacs. We also calculated the fund value for a MF plus pure Term Assurance combo and MF as well based on the above assumptions.

3.4.3 For comparison in Table A, we assumed that death benefit in all the five ULIPs products is sum assured plus fund value to make it similar to death benefit in MFs plus TA combo.
3.4.4 The information for the charges is taken from publicly available literatures and web sites. The FMC for each product is a weighted average of balance and growth type of funds available for them with weights of 30% and 70%.

3.4.5 In some products mortality charges are not given for all the ages. In such products we estimated rates from rates given using interpolation. These may not be exactly the same that insurance companies are charging but impact of variation is likely to be very small.
3.4.6 In Table B, we calculated the IRR for the customer under each product and Mf plus TA combo and MF. The reduction in yield has also been calculated in each case which is defined as fund growth rate (10%) minus IRR to the customer. Reduction in yield reflect the level of charges in each case. Higher the reduction in yield, higher the level of charges. In other words reduction in yield can be treated as equivalent regular FMC if there were only FMC charge in product.

Table A: Comparison of fund values (death benefit = SA plus fund value)

Term =10 years, Sum Assured = 5lacs, Term Assurance premium for MF plus TA combo= 1600							
Fund at EOY	(A)	(B)	(C)	(D)	(E)	MF+TA	MF alone
5	289867	294457	245531	246902	286791	295,627	305400
10	755698	746562	684477	671030	718431	720,531	744351
Term =15 years, Sum Assured = 5lacs, Term Assurance premium for MF plus TA combo= 1655							
5	286123	294457	245531	246902	286437	295291	305400
10	736327	746554	683090	671030	717218	719713	744351
15	1417010	1422640	1343134	1314611	1353085	1329733	1375254
Term =20 years, Sum Assured = 5lacs, Term Assurance premium for MF plus TA combo= 1865							
5	286013	294457	245531	246311	286052	294,008	305400
10	736160	746554	684477	670134	716591	716,586	744351
15	1416756	1422640	1346810	1313251	1352803	1,323,957	1375254

20	2445987	2438273	2344444	2278206	2291214		2,196,932	2282052
Term =10 years, Sum Assured = 10lacs, Term Assurance premium for MF plus TA combo= 2927								
Fund at EOY	(A)	(B)	(C)	(D)	(E)	(I)	MF+TA	MF alone
5	279292	287765	239586	242887	280558		287,522	305400
10	716253	726825	666466	657902	700240		700,776	744351
Term =15 years, Sum Assured = 10lacs, Term Assurance premium for MF plus TA combo= 3133								
5	279292	287765	238782	242887	279850		286,263	305400
10	716253	726825	663691	657902	697815		697,710	744351
15	1371457	1377941	1297862	1287656	1309273		1,289,081	1375254
Term =20 years, Sum Assured = 10lacs, Term Assurance premium for MF plus TA combo= 3580								
5	279292	287765	239586	242296	279818		283,533	305400
10	716253	726825	666466	657006	698400		691,055	744351
15	1371457	1377941	1305213	1286295	1312186		1,276,786	1375254
20	2358694	2352573	2257306	2219342	2208653		2,118,657	2282052

TableB: Customer IRR and Reduction inYield

(Death benefit = SA plus fund value)

Products	Term=10, SA=5lacs		Term=15, SA=5lacs		Term=20, SA=5lacs		Term=10, SA=10lacs	Term=15, SA=10lacs			Term=20, SA=10lacs	
	Customer IRR	Reduction in Yield	Customer IRR	Reduction in Yield	Customer IRR	Reduction in Yield	Customer IRR	Reduction in Yield	Customer IRR	Reduction in Yield	Customer IRR	Reduction in Yield
(A)	7.39	2.61	7.61	2.39	7.91	2.09	6.44	3.56	7.23	2.77	7.61	2.39
(B)	7.18	2.82	7.65	2.35	7.89	2.11	6.70	3.30	7.28	2.72	7.59	2.41
(C)	5.64	4.36	6.99	3.01	7.56	2.44	5.16	4.84	6.59	3.41	7.24	2.76
(D)	5.29	4.71	6.74	3.26	7.32	2.68	4.93	5.07	6.50	3.50	7.10	2.90
(E)	6.50	3.50	7.07	2.93	7.37	2.63	6.04	3.96	6.69	3.31	7.06	2.94
MF+TA	6.55	3.45	6.89	3.11	7.06	2.94	6.06	3.94	6.51	3.49	6.71	3.29
MF alone	7.12	2.88	7.26	2.74	7.33	2.67	7.12	2.88	7.26	2.74	7.33	2.67

4. Conclusion:

4.1 The main conclusion is that while comparing two investment products and making investment decision, all the features of the products should be considered. The general perception may be misleading. As illustrated above, the ULIP policies look very competitive as compared to MF plus TA combo over longer duration in terms of level of charges and other features contrary to the general perception.

4.2 Over short duration MFs charges are less than that under ULIPs and therefore suitable for those who want to invest large amounts for short term.

4.4 MFs and ULIPs serve divergent investment objectives and hence both can coexist in the Indian Investment space.

4.5 The ULIPs if taken fund value or sum assured whichever is higher then the IRR to customer shall be even higher. We have left this comparision as we allowed the comparision like to like.

4.6 The basic rule of investment is that investment is to made taking into account the nature term and currency of the liabilities. The readers, investing public and sales personnel may now conclude what are the benefits of making investment in MF and ULIPs issued by Life Insurance Companies. They can also conclude which investment is useful in longer term. Further they may have definitive reply to such emerging questions stated under heading **Introduction** e.g. investment in Mutual Funds is better than investment in ULIPs OR – A combo may offer more than ULIP in long run – OR – Now because of tax treatment MFs have an edge- etc….

5. Acknowledgement

5.1 We do not give any credit to our selves for this paper because most of the things are taken from here and there. Moreover we were benefited in the process when we collected the material for this paper. The information was collected from- From different web sites of Life Insurance Companies, Mutual Fund and SEBI, CBDT and from Times Publications.

6. Appendix

6.1 Sub Section A:

What is Mutual Fund?

SEBI definition of Mutual Fund

Mutual fund is a mechanism for pooling the resources by issuing units to the investors and investing funds in securities in accordance with objectives as disclosed in offer document.

Investments in securities are spread across a wide cross-section of industries and sectors and thus the risk is reduced. Diversification reduces the risk because all stocks may not move in the same direction in the same proportion at the same time. Mutual fund issues units to the investors in accordance with quantum of money invested by them. Investors of mutual funds are known as Unit holders.

The investors in proportion to their investments share the profits or losses. The mutual funds normally come out with a number of schemes with different investment objectives, which are launched from time to time. A mutual fund is required to be registered with Securities and Exchange Board of India (SEBI) that regulates securities markets before it can collect funds from the public.

Association of Mutual Funds in India (AMFI) definition of Mutual Fund

A Mutual Fund is a trust that pools the savings of a number of investors who share a common financial goal. The money thus collected is then invested in capital market instruments such as shares, debentures and other securities. The income earned through these investments and the capital appreciation realised are shared by its unit holders in proportion to the number of units owned by them. Thus a Mutual Fund is the most suitable investment for the common man as it offers an opportunity to invest in a diversified, professionally managed basket of securities at a relatively low cost. The flow chart below describes broadly the working of a mutual fund:

What is Life Insurance?

IAIS Definition of Insurance-

“Insurance is an economic device whereby the individual substitutes a small cost (the premium) for a large uncertain financial loss (the contingency insured against) which would exist if it were not for the insurance contract, an economic device for reducing and eliminating risk through the process of combining a sufficient number of homogeneous exposures into a group in order to make the losses predictable for the group as a whole.”

Traditionally Life Insurance companies cover the risk on human lives. The risk may be Mortality Risk, risk of falling sick/ being disabled, or longevity risk in absence of regular and sufficient income. The life insurance coverage may be offered individually or in group form.

6.2 Sub Section B

Some Terminologies used in Mutual Funds are given below:

Loads

Loads are an extra charge that investors pay to the mutual fund. This is an additional expense for the investor. Loads are of two kinds - entry loads and exit loads. A load is usually calculated as a percentage of the NAV.

SCHEME OPTIONS

There are three such options available and these are the dividend payout, dividend reinvestment and the growth option

In the dividend payout option the dividend declared by the scheme is paid out in cash to the investor. Investors have to be careful and select this as the option when they want the actual payment to be received in cash. One has to note that the dividend declaration is always on the face value of the units and not on the current value.

The dividend reinvestment option is one where the dividend declared by the scheme is then poured down back into the scheme at the applicable NAV.

The growth option is one where the gains of the scheme are added on to the NAV of the scheme and no payout is received. This means that the value of the NAV keeps on increasing without any intervention from the fund. If there is a scheme that has grown consistently over the years then it will be witnessed that the NAV has also gone quite high while in the dividend option this will keep reducing as and when the dividend is paid

EXPENSE RATIO

There are various expenses that are incurred by the mutual fund in respect to its operations. The first is the initial issue expense ratio which is the expense incurred at the time of a new fund offering. The other is the expense ratio that is witnessed during the normal operation of the scheme.

There are limits prescribed for various expenses. According to the regulations issued by the Securities and Exchange Board of India (SEBI) the total initial expenses shall not exceed 6% of the initial resources raised under a close-ended scheme and any excess over this figure will have to be borne by the asset management company (AMC). There has been a recent change to the provisions of the charging of the initial issue expenses for an open-ended scheme and there

cannot be any initial issue expenses over and above the entry load on the scheme. The initial issue expenses will include-
Advertising expenses,
Agent commission,
Registrar expenses,
Marketing expenses,
Bankers' fees,
Legal fees,
Printing
Distribution expenses etc.

Recurring expenses include-
Investment management and advisory fees,
Trustee fees,
Custodian fees,
Marketing and selling expenses,
Registrar and transfer agent fees,
Audit fees,
Communication costs,
Cost of providing account statements,
Dividend,
Redemption warrants,
Cost of statutory advertisement
Other expenses.

NEW FUND OFFER (NFO)

A new fund offer is a new scheme launched by a mutual fund. It is called a NFO to differentiate it from the IPO of a stock because there was large confusion among investors who were being sold new units of mutual fund schemes like a new share offering.

SYSTEMATIC INVESTMENT PLAN (SIP)

Systematic Investment Plan is often called SIP and this is a method of investing used by mutual fund investors. In this method there is an investment of a fixed sum on the same day of each month for a period of say 6 months or 1 year by an investor. This ensures that there is a regular investment each month and the idea is to ensure that the highs and lows are averaged out so that the investor is able to get an average price for the units.

6.3 Sub Section C:

Terminologies regarding charges used in life Insurance Unit Linked Plans:

Premium Allocation Charge: This is a percentage of the premium appropriated towards charges from the premium received. The balance known as allocation rate constitutes that part of premium, which is utilized to purchase (investment) units for the policy. The percentage shall be explicitly stated and could vary interalia by the policy year in which the premium is paid, the premium size, premium payment frequency and the premium type (regular, single or top-up premium). This is a charge levied at the time of receipt of premium. If Actuarial Funding is adopted, this charge may also include an initial management charge, which is levied on the units created from the first years' premium, for a specified period.

Fund Management Charge (FMC): This is a charge levied as a percentage of the value of assets and shall be appropriated by adjusting the Net Asset Value.

Policy Administration Charge: This charge shall represent the expenses other than those covered by premium allocation charges and the fund management expenses. This is a charge, which may be expressed as a fixed amount or a percentage of the premium or a percentage of sum assured. This is a charge levied at the beginning of each policy month from the policy fund by canceling units for equivalent amount.

Surrender Charge: This is a charge levied on the unit fund at the time of surrender of the contract. This charge is usually expressed either as a percentage of the fund or as a percentage of the annualized premiums (for regular premium contracts).
Switching Charge: This a charge levied on switching of monies from one fund to another available within the product. The charge will be levied at the time of effecting switch and is usually a flat amount per each switch.

Mortality charge: This is the cost of life insurance cover. It is exclusive of any expense loadings levied either by cancellation of units or by debiting the premium but not both. This charge may be levied at the beginning of each policy month from the fund. The method of computation shall be explicitly specified in the policy document. The mortality charge table shall invariably form part of the policy document. Mortality rates are guaranteed during the contract period, which are filed with the Authority.

Rider premium charge: Rider cover cost: This is the premium exclusive of expense loadings levied separately to cover the cost of rider cover levied either by cancellation of units or by debiting the premium but not both. This charge is levied at the beginning of each policy month from the fund.

Partial withdrawal charge: This is a charge levied on the unit fund at the time of part withdrawal of the fund during the contract period.

Miscellaneous charge: This is a charge levied for any alterations within the contract, such as, increase in sum assured, premium redirection, change in policy term etc. The charge is expressed as a flat amount levied by cancellation of units. This charge is levied only at the time of alteration.

All the charges other than premium allocation charge and cost of life insurance/mortality cost shall have an upper limit.
All the charges stated above, where relevant, may be modified with supporting data within the upper limits with prior clearance from the Authority.

6.4 Sub Section D:

REGULATORY ASPECTS IN MUTUAL FUNDS

Every action of the mutual fund is governed by the various regulations laid down by SEBI and there is a need for mutual funds to follow these guidelines so that investors get the best services along with a fair treatment with respect to their investments.
This include-

One of the main regulations relate to the formation of a mutual fund. The whole idea behind the entire exercise both in terms of business reputation as well as financial parameters is that the sponsor should be sound enough so the mutual fund is backed by the right kind of people.

Mutual Fund has to be in the form of a trust with a trust deed under the provisions of the Indian Registration Act.

Regarding recurring expenses (from investor point of view) of a mutual fund the expense limits are as under-

for the first Rs 100 crore of the average weekly net assets the expense is 2.5%,
for the next Rs 300 crore it is 2.25%,
for the next Rs 300 crore it is 2%,
and for the figure over that amount (Rs 700 crore) it is 1.75%.

In case of a scheme investing in bonds the limit shall be lesser by at least 0.25% of the weekly average net assets. Any expense over and above the prescribed ceiling will be borne by the asset management company.

For change in feature There is also a condition that no change in the fundamental attributes of any scheme or the trust or even fees and expenses or some other change which would modify the scheme and affects the interest of unit holders will be carried out without a written communication being sent to each unit holder. In addition an advertisement has to be given in one English daily newspaper having nationwide circulation and in a newspaper published in the language of the region where the head office of the mutual fund is situated. The unit holders also have to be given an option to exit the scheme at this stage without paying any exit load.

Whenever there is an application by an investor for units in a mutual fund scheme then the asset management company shall issue to the applicant unit certificates or a statement of accounts specifying the number of units allotted to the applicant as soon as possible but this cannot be later than six weeks from the date of closure of the initial subscription list or the date of receipt of the request from an investor in an open ended scheme.

While calculating the prices of the units the mutual fund shall ensure that the repurchase price is not lower than 93% of the net asset value and the sale price is not higher than 107% of the net asset value. However the total difference between the repurchase price and the sale price of the units shall not exceed 7% calculated on the sale price. In case of a close-ended scheme the repurchase price cannot be lower than 95% of the net asset value.

There has to be a dispatch to the unit holders of the dividend warrants within 30 days of the declaration of dividend in the scheme. In case of redemption proceeds this has to be within 10 working days from the date of redemption or repurchase.

Regarding investment - no mutual fund shall invest more than 10% of its NAV in the equity shares or equity related instruments of any company. This limit of 10% will not be applicable for index funds and sector or industry specific schemes. A mutual fund shall also not invest more than 5% of the NAV in the unlisted equity shares of an open-ended scheme and 10% of its NAV in case of a close-ended scheme. No mutual fund shall under all its schemes own more than 10% of any company's paid up capital carrying voting rights. A mutual fund shall not invest more than 15% of its NAV in debt instruments issued by a single issuer, which are rated not below investment grade by a credit rating agency. This can be extended to 20% with the prior approval of the Board of Trustees and the board of the asset management company. These limits are not applicable to government securities and money market instruments. A mutual fund shall not invest more than 10% of its NAV in unrated debt instruments issued by a single issuer and the total investments in such instruments should not exceed 25% of the NAV of the scheme. All such investments have to be made with the prior approval of the Board of Trustees and the board of the asset management company. In case a company has invested more than 5 % of the net asset value of a scheme, the investment made by that scheme or any other scheme of the mutual fund in that company or its subsidiaries shall be brought to the notice of the trustees by the asset management company and disclosed in the half yearly and annual accounts of the scheme with justification for such investments.

Regulatory aspects for Life Insurance Companies

Life Insurance Companies are governed by the provisions of Insurance Act 1938. The amendments under the Act are under the process. The major suggestions are from IRDA under KPN Committee on Provisions of the Insurance Act, 1938. Even in present form the Insurance Act, 1938 is very comprehensive. LIC of India is also governed by the provisions of Life Insurance Corporation, Act, 1956. The Life Insurance Companies are also governed by the Insurance Regulatory and Development Authority Act, 1999 and also the provisions of Rules and regulations framed under Insurance Regulatory and Development Authority Act, 1999. Insurance Act 1938 ranges from formation of the company, investment, loans and Management, Investigation, Appointment of staff, control over Management, Amalgamation and Transfer of Insurance Business, Assignment or Transfer of policies and nominations, commission and rebates and licensing of agents, special provisions of law, management by Administrator, acquisition of the undertakings of Insurers in certain cases, Insurance Association of India, councils of the Association and committees thereof, solvency margins, advance payment of premium, restrictions on the opening of a new place of business, reinsurance, etc. The regulations cover Actuarial Report and Abstract, advertisements, reinsurance, appointed actuary regulations, asset liability and solvency margins, registration of Indian Insurance Committees, Investment, Financial Statements, protection of policyholders, distribution of surplus, obligation of insurers to rural and social sector, brokers and corporate agents etc.

6.5 Sub Section E:

TAXATION ASPECTS IN MUTUAL FUNDS

There are different tax implications for investors when they invest their funds into mutual fund schemes. This depends upon their status, the type of scheme that they have invested in and the nature of the gain that they have earned.

Under EQUITY ORIENTED SCHEME the latest modified definition any scheme that has more than 65% of its assets invested in equities of domestic companies will be considered as equity oriented schemes. This means that even balanced scheme with this percentage of assets in equities would be classified under this head. As far as dividends from equity oriented schemes are concerned there is no tax to be paid by the investor on the amount received hence the entire amount that is received by the investor in their hands will be completely tax free. For capital gains too there is a favourable treatment for equity-oriented funds. There is however the securities transaction tax payable only at the time of the sale of equity oriented funds. The long-term capital gains on such schemes that have paid the STT will be zero while the short-term capital gains on such scheme will be at 10%.

Under DEBT ORIENTED SCHEMES the tax treatment is slightly different and hence one has to pay close attention to the various types of gains or losses that have originated in such schemes. For debt-oriented schemes, the investor does not have to pay any tax on the dividend that is received by them. However there is an indirect expense for the investor in the form of dividend distribution tax that is present on such schemes, Here there are two rates for dividend distribution tax depending upon the category of the investor who is receiving the dividend payout. For investors who are individuals and Hindu undivided families the tax payout is 12.5% plus surcharge plus cess while the figure for categories other than these two the rate is 20% plus surcharge plus cess. Thus individuals will witness an indirect effect because the tax will be charged off to the net asset values of the fund. When a dividend is declared in a debt fund there are two figures that are being talked about. The first is the gross dividend and the second is the net dividend. The net dividend is the important figure for the investor to consider because this is the payout that they will receive from the fund. Then there are capital gains that would arise from the investment in such schemes. Here where there is a short term capital gains the figure of the gain will be added to the income of the individual and then taxed at the applicable rates. This means that the tax rate figure could jump to as high as 30% as several investors will fall into that particular tax bracket. On the other hand where there is long term capital gains there is a choice for the investor to make in terms of the rate of the tax that they will pay. The investor can either pay 10% tax without taking the benefit of indexation or pay 20% after taking the benefit of indexation. The benefit of indexation is the method where by the investor raises the cost of the purchase of the investment depending upon the year in which the purchase is made and the year in which the sale is made. There is a cost inflation index that is announced each year by the tax authorities and this is then used for the purpose of raising the cost so that that investor has a lower burden to pay as tax. There is no securities transaction tax in the case of debt-oriented schemes.

Taxation aspects for Life Insurance Companies

Chapter VI A

Deduction in respect of life insurance premia, deferred annuity, contributions to provident fund, subscription to certain equity shares or debentures, etc.

80C. *(1) In computing the total income of an assessee, being an individual or a Hindu undivided family, there shall be deducted, in accordance with and subject to the provisions of this section, the whole of the amount paid or deposited in the previous year, being the aggregate of the sums referred to in sub-section (2), as does not exceed one lakh rupees.*

(2) The sums referred to in sub-section (1) shall be any sums paid or deposited in the previous year by the assessee

*(*i*) to effect or to keep in force an insurance on the life of persons specified in sub-section (4);*

*(*ii*) to effect or to keep in force a contract for a deferred annuity, not being an annuity plan referred to in clause (*xii*), on the life of persons specified in sub-section (4):*

Provided…..

CHAPTER III

INCOMES WHICH DO NOT FORM PART OF TOTAL INCOME

Incomes not included in total income.

10. In computing the total income of a previous year of any person, any income falling within any of the following clauses shall not be included
[(10D) any sum received under a life insurance policy, including the sum allocated by way of bonus on such policy, other than-
any sum received under sub- section (3) of section 80 DD or sub section (3) of section 80 DDA or,
any sum received under a key man insurance policy; or,
any sum received under an insurance policy issued on or after the 1st day of April, 2003 in respect of which the premium payable for any of the years during the term of the policy exceeds twenty per cent of the actual capital sum assured:
Provided……………..

6.6 Sub Section F:

Mutual Funds in alphabetical order and asset under management on close of June 2006

Name of the Mutual Fund	**Assets Under Management in Crore (Appx.)**
Birla Mutual Fund	14000 (3043 millionUS $ @ 46/-)
DSP ML Mutual Fund	11000 (2391)
Franklin Templeton Mutual Fund	20000 (4348)
HDFC Mutual Fund	
HSBC Mutual Fund	10000 (2174)
Kotak Mutual Fund	10000 (2174)
Prudential ICICI Mutual Fund	30143 (6553)
Reliance Mutual Fund	1000 (217)
SBI Mutual Fund	13000 (2826)
TATA Mutual Fund	11000 (2391)
UTI Mutual Fund	30000 (6522)

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