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Income Taxation and Its Impact on Salaried Individuals in India: A Critical Analysis with Reference to Assessment Year 2026-27

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Abstract
Income tax is the most valuable source of government revenue. It is a direct tax that still remains an important component of fiscal governance in India. One of the best organized and obedient section of taxpayers is salaried laborers as they have organized payrolls and tax deduction at source (TDS) systems. The Assessment Year (AY) 2026-27 that aligns to Financial Year (FY) 2025-26 illustrates the relevance of the new tax regime that was proposed by section 115BAC of the Income-tax Act, 1961. The current research provides an assessment of the income tax structure of the salaried taxpayers in the AY 2026-27 and strictly examines its impact on disposable income, saving habits, consumption, and distributive justice. The results show that the income tax has a significant role in the economic choice and financial stability of the salaried taxpayers. This paper summarizes that the recent reforms have eased the effective tax burdens on middle income earners and have made compliance easier though the long term shifts in savings behavior need more scrutiny.

Keywords: Income tax, salaried class, Section 115BAC, Section 87A, disposable income, fiscal policy, India, tax burden

Introduction

The income tax is an important element in the fiscal policy and a source of a lot of revenue to the government. In India, the Income Tax Act of 1961 regulates it and has a direct impact on the financial situation of the salaried employees. Salaried workers are more directly affected by changes in tax rates, slabs and deductions than business owners because taxes are deducted most at their source.

Income tax has an impact in the disposal income, ability to save and the spending habit and the well being of the financial aspect. The tax burden on this group has subsequently been changed with reference to equity and economic impacts as new reforms and introduction of alternative tax regimes have further changed the tax burden imposed on this group.

Over the last few years, India has introduced structural reforms in the field of personal income taxation with a view of simplifying and rationalizing the tax system. The default framework has been developed over years, and new tax regime, which is presented by Section 115BAC, is becoming dominant. The policy initiatives to reduce taxes to the middle class without affecting the principles of progressive taxation include the higher standard deduction, higher rebate limits, and revised slab rates of the AY 2026-2027. The paper discusses how such reforms impacted the economy and behavior of the people on salary.

Definitions

Income

Income is any economic or non- monetary profit earned by an individual or an entity within a given time. Section 2(24) of the Income-tax Act, 1961 defines income as profits, gains, dividends, voluntary contributions, perquisites, business profits, capital gains and any other receipts. The notion goes beyond the ordinary earnings to include all kinds of stream of wealth that improves the economic status of the recipient.

Income Tax

Income tax is a direct tax imposed by the government on the taxable income of the individuals, Hindu undivided families, companies, firms and other entities within a given financial year. It functions under the ability-to-pay principle, according to which more funds are paid by taxpayers who have higher incomes. The income-tax Act, 1961 regulates the tax and the central board of direct taxes administers the tax.

Assessment Year

Assessment Year (AY) is a period of twelve months, which begins on April 1 every year, when income made last year is estimated and assessed, taxed and the returns are filed. As an example FY 2025-26 earnings are determined in AY 2026-27. It is the year that the taxpayers calculate their taxation and submit returns according to the previous year revenue.

Previous Year

Previous Year (PY) refers to the last financial year, which has already been followed by the year taken under assessment, and during which the income is actually earned. It spans from April 1 to March 31. Income-tax Act section 3 is used to define it as the year of receiving or accruing income. The income obtained in this time is brought forward to the following assessment year as taxable income.

Income Tax Return

Income Tax Return (ITR) is a prescribed form by which the taxpayers report their total income, deductions availed and tax remitted to the Income Tax Department. It is a formal communication between the taxpayer and tax authorities thus it can be used to assess the tax liability, refunds and verify compliance. There are numerous types of ITRs concerning the types of taxpayers and sources of income.

Person

In the income tax act, 1961 in section 2 (31), person refers to eight categories of tax payers namely individual, Hindu Undivided Family, company, firm, association of persons, body of individuals, local authority and all artificial juridical persons. These include the individuals who make the most significant percentage in terms of taxpayers, such as salaried workers, the business people, and senior citizens among others.

Individual Assessee

A natural person subject to payment of tax under the Act is referred to as an individual assessee. It falls under the men category, women category, senior citizen category (60-80 years old), very senior citizen category (above 80 years old), where each category has specific exemption limits and slab rates. Tax is charged to a person, depending on his residential status, resident, non-resident, or not ordinarily resident, which is used to determine the extent of taxable income.

Objectives of the Study

The main goals of the research are as follows:

1. To examine the income tax system to be utilized by the salaried taxpayers in Assessment year 2025-26.
2. To assess the amount of tax relief offered according to the new tax regime.
3. To test the effect of changes in taxes on the disposable income and the economic behavior.
4. To measure larger fiscal/distributive effects.

Research Methodology

The type of research design used in this study is the doctrinal and the analytical research. It is mainly dependent on official fiscal policy statements and interpretation of provisions in statutory interpretation of the provisions of the Income-tax Act, 1961. Secondary sources of information like government publications, economic analysis and policy discourses were also consulted. The comparison of the old tax regime and the new one is used to determine the relative effect on the salaried taxpayers.

Literature Review

Income taxation is one of the key elements of fiscal governance, whose theoretical roots can be traced to Adam Smith and developed by **Musgrave (1959)**, who theorized about the role of taxation in resource allocation, redistribution, and stabilization.

The Indian system with the **Income-tax Act, 1961** has the progressive slab rates that determine the disposable income trends. Keynes (1936) defended tax relief in the middle income groups as these groups have higher marginal propensity to consume, and this would increase aggregate demand.

Swain (2017) investigated the Indian personal income tax reforms between the FY 2012-13 and 2016-17 and found improvements in tax-free levels in senior citizens and decreased the marginal effective rate by 18.67 to 18.33. The benefits of tax relief were mostly to the lower-income earners, whereas the middle and the high slabs were liable to constant taxes. In the research, it was proposed to have lean structures and increase pension investment to encourage voluntary compliance and economic growth.

Singh (2019) reviewed the taxation trend of India between 1980 and 2017 and remarked that in 2007-08 direct taxes exceeded the indirect levies, and the corporate revenues have now increased by 1.8 times the personal income tax. The administrative expenses decreased to 0.66 percent of the collections (previously 1.83 percent), but compliance expenses were still high at 6-49 percent. India had the lowest tax to GDP ratio of 17.7% among the BRICS countries.

Jouste et al. (2021) examined the 2012 PIT reform in Uganda based on the PAYE data, and results showed that the top percentile taxpayers lost much taxable income after the reform with an elasticity of 0.5-1.2. Reactions were concentrated among the top earners and large companies indicating income redistribution. The reform produced positive net revenue despite the changes in behavior, and this would support higher top rates of domestic resource mobilization.

Bird and Zolt (2005) reviewed redistributive constraints of personal income taxation in developing nations finding that structural and administrative constraints majorly restrain redistributive potentials as opposed to other fiscal tools.

Geetha (2015) surveyed the tax awareness of 600 professionally salaried Kerala-based professionals and discovered that there was a lot of awareness of professional tax and Section 80C deductions but people did not understand the Section 89 relief and capital gains. Inequality arose among the workers in both the public and the private sector and this necessitated systematic training on taxes in order to enhance compliance and wise planning.

Deore (2021) investigated the taxpayer decisions between old and new regimes on AY 2021-22 in among 50 respondents. PFs and insurance investments had a preference with the salaried individuals, who preferred the old regime despite the rate increases, and those with no deductions to the simplified lower-rate structure. Elderly people who had pension backlog also preferred old regime as a means of relief.

Bansal and Sharma (2023) compared the income tax regime of 2012-13 to 2022-23 and noted that the exemption limits remained unchanged in six years as the cost increased, thus imposing disproportionate taxation on the lower and middle-income categories. The new regime had attracted individuals with low investments and those with substantial tax-favored investments enjoyed the old system.

Babu and Raju (2023) summarized the literature on tax rates, revenue and compliance including inverse rate-revenue relationship proposed by Canto (1981), perception of tax burden as suggested by Lall (1982) and suggested reforms that are gradual as postulated by Gupta (2009). The analysis focused on rationally organized structures, reduced compliance expenses, as well as total orientation that favors economic progress.

Ojha and Agarwala (2024) analyzed the policy arguments and reaction of the taxpayers to the new tax regime in India with the old tax regime providing incentives on long-term planning by claiming deductions compared to the new regime providing simplifications by cutting rates without exemptions. Recorded trends indicate that the taxpayer migration towards the new system is witnessed among those who have tax deductions to optimize.

Ramanathan and Pulipati (2025) In their comparison of traditional and revised tax structures, highlighted structural changes in the Budget 2020. Analysis of primary data showed that those taxpayers with limited tax saving preferences are using the revised structure because it is easier, and those having high investments and reliance on the deductions are using the traditional structure. Budgetary changes are still affecting the decisions

The analysis in Das and Verma (2023) takes a long-run view of the development of income tax slab and its economic effects on the salaried population of India. They point out fiscal drag due to non-adjusted slabs during inflation and rise in income and eroding the purchasing power of the middle classes despite regular reforms that provide temporary reprieve.

Gupta and Pandey (2024) evaluate the recent changes in the income tax and their impact on the salaried population, pointing out that although the changes are aimed at the relief of the low- and middle-income population, the benefits and adherence to the new rules are threatened by the complicated nature of the filing and tax saving procedures.

Bharad and Sharma (2024) examine the differences in perceptions and legal between old and new tax regimes using survey data of Ahmedabad taxpayers. Their results show that salaried workers prefer the new system because it is simpler where deductions are small, whereas they prefer the old system because it makes huge investments.

Researcher Rao and Singh (2025) discuss how the new tax regime impacts salaried professionals in Pune by measuring 2025 Budget slab restructurings. This research shows that there is a lower liability among moderate earners up to [?]15 lakhs, which doubles the disposable income at the expense of savings instruments that are deductive.

Patel (2025) studies tax literacy levels of the salaried population, and it has been discovered that there is a huge disparity in the interpretation of the new regime rebates and slabs even when the TDS is greatly compliant. The study emphasises education in order to streamline financial planning and minimise the unplanned tax burden.

Agarwal (1991) measured the responsiveness of personal income tax to income inequality and obtained measures of elasticity of about 1.17. In evaluating information technology use in tax administration, Bagchi (1993) has focused on the need to restructure the organization with the aim of ensuring that technologies are effectively applied.

According to Ministry of Finance reports, AY 2025-26 transition is being done systematically in deduction-based structures to slab rationalization. Analyses covering fiscal reform demands and tax rationalization measures were published by **NITI Aayog (2023).** The literature review has shown that personal income tax reform is a dynamic concept that has implications to fiscal sustainability and economic behavior.

Income Tax structure 2026- 27.

The Dual Regime System

Salaried members of the AY 2026-27 can choose between:

Old Regime: A more expensive, with numerous exemptions and deductions (e.g. Sections 80C to 80U).

New Regime (Section 115BAC): Smaller and more graduated tax slabs with small deductions.

The new regime is the default regime unless the taxpayer has on-boarded by opting out.

Slab Rates with New Regime.

With FY 2026-27 (AY 2026-27), the tax slabs will be in progressive form with the initial rate of nil on income up to ₹4,000,000 and then progressively up to 30 on income above ₹24,00,000. This tax regime will decrease marginal tax pressure on the lower- and middle-income groups.

Table 1: Income Tax Slabs under New Regime for AY 2026-27

Income Slab (₹)	**Tax Rate**
Up to 4,00,000	Nil
4,00,001 - 8,00,000	5%
8,00,001 - 12,00,000	10%
12,00,001 - 16,00,000	15%
16,00,001 - 20,00,000	20%
20,00,001 - 24,00,000	25%
Above 24,00,000	30%

In addition, the following conditions apply:
Standard Deduction: ₹75,000 for salaried individuals.
Health and Education Cess: 4% of tax liability.
Rebate under Section 87A: Available for resident individuals with taxable income up to **₹12,00,000/-**

The enhanced rebate has effectively eliminated tax liability for a significant segment of middle-income salaried taxpayers.

Economic Effect on Salaried people.

Effect on Disposable Income

Take-home salary is directly related to tax liability. In the altered provisions, people with earnings less than ₹12,00,000 (inclusive of deductions that can be made under the new regime) will not or will only have to pay tax of nothing or at the very least a minimal amount. Therefore, net disposable income will rise without necessitating tax-saving investments. Such a change increases financial flexibility. Households do not have to spend money on a particular instrument as a way of cutting down on tax bills. Rather, allocation of funds and saving might become more indicative of true financial concerns.

Consumption Behavior

The theory of the economy implies that middle-class households have a rather high marginal propensity to consume. Increments of disposable income tend to be consumed in goods and services as opposed to being saved out when taxes reduce. Thus, domestic demand in such areas as housing, consumer durables, education, and healthcare might be boosted by tax relief in AY 2026-27. This is a demand-side stimulus that is consistent with the macroeconomic goal of maintaining growth in an internal consumption-based growth revenue as opposed to an export one.

Implication on Savings and Investment Pattern.

Section 80C and others allowed the old regime to promote savings by way of deductions. On the contrary, the new regime lowers the dependence on such specific incentives. Although this will make compliance easy, it can change the long run savings behavior. A possible change is that of tax-oriented to return-oriented investments. This can encourage the allocation of capital in a more efficient way but might also encourage a decline in the involvement in conventional savings schemes unless an independent financial planning.

Compliance and Administrative Efficacy.

Administratively, simplified slab structure makes the computation simpler. The new regime can be easier to understand and follow by the salaried individuals who do not have many deductions. Both the efficiency of tax administration may also be enhanced by reduced paperwork and fewer deduction claims.

Fairness and Distributional Judgments.

The nature of income tax in India has not changed, with higher income groups still being on the receiving end of progressive rates and surcharges wherever the case may be. Rebate benefits mainly benefit lower and middle income earners since they are augmented. Those who oppose this point however, believe that this decreased focus on deduction related savings can undermine social security orientation unless other long term savings inducements are reinforced.

Comparison and Evaluation: Old vs. New Regime

Salaried Tax calculation analysis as of empirical taxation of individuals (AY 2026-27).

8.1 Assumptions which are used to illustrate.

Assessment Year: 2026-27

Financial Year: 2025-26

Taxpayer: Person who is in employment as salaried person (under 60 years)

Standard Deduction: ₹75,000

Health & Education Cess: 4%

No premium to be paid (income less than ₹50,00,000)

Old Regime and New Regime (Section 115BAC) Compared.

8.2 Case Study Analysis

Case 1: Gross Salary :

₹9,00,000

Table 2: Tax Calculation New Regime Case 1: Gross Salary ₹9,00,000

Particulars	**Amount (₹)**
Gross Salary	9,00,000
Less: Standard Deduction	75,000
Taxable Income	**8,25,000**

Tax Calculation:

Income Slab (₹)	**Tax Amount (₹)**
0 – 4,00,000	Nil
4,00,001 – 8,00,000 (5% of 4,00,000)	20,000
8,00,001 – 8,25,000 (10% of 25,000)	2,500
Total Tax	**22,500**

Rebate under section 87 A = 22,500

Net tax = 0

Health & Education cess (4%) = 0

Final Tax Liability = 0

Table 3: Tax Calculation under Old Regime (₹9,00,000 - Assuming No Deductions)

Income Slab (₹)	**Tax Amount (₹)**
0 – 2,50,000	Nil
2,50,001 – 5,00,000 (5%)	12,500
5,00,001 – 9,00,000 (20%)	80,000
Total Tax	**92,500**
Health & Education Cess (4%)	3,700
Final Tax Liability	**96,200**

Rebate under Section 87A: Not applicable (eligible only for income up to ₹5,00,000)

Tax Saving under New Regime = ₹96,200

Case 2: Gross Salary ₹12,00,000

Table 4: Tax Calculation under New Regime (₹12,00,000)

Particulars	**Amount (₹)**
Gross Salary	12,00,000
Less: Standard Deduction	75,000
Taxable Income	**11,25,000**

Tax Calculation:

Income Slab (₹)	**Tax Amount (₹)**
0 – 4,00,000	Nil
4,00,001 – 8,00,000 (5% of 4,00,000)	20,000
8,00,001 – 11,25,000 (10% of 3,25,000)	32,500
Total Tax	**52,500**

Rebate under Section 87A (Income below 12,00,000 limit) = 52,500

Net Tax = 0

Health & education cess = 0

Table 5: Tax Calculation under Old Regime (₹12,00,000 - Assuming ₹1,50,000 deduction under 80C)

Particulars	**Amount (₹)**
Gross Salary	12,00,000
Less: Standard Deduction	50,000
Less: 80C Deduction	1,50,000
Taxable Income	**10,00,000**

Tax Calculation:

Income Slab (₹)	**Tax Amount (₹)**
0 – 2,50,000	Nil
2,50,001 – 5,00,000 (5% of 2,50,000)	12,500
5,00,001 – 10,00,000 (20% of 5,00,000)	1,00,000
Total Tax	**1,12,500**
Health & Education Cess (4%)	4,500
Final Tax Liability	**1,17,000**

Tax Saving under New Regime = ₹1,17,000

Case 3: Gross Salary ₹18,00,000

Table 6: Tax Calculation under New Regime (₹18,00,000)

Particulars	**Amount (₹)**
Gross Salary	18,00,000
Less: Standard Deduction	75,000
Taxable Income	**17,25,000**

Tax Calculation:

Income Slab (₹)	Tax Amount (₹)
0 – 4,00,000	Nil
4,00,001 – 8,00,000 (5% of 4,00,000)	20,000
8,00,001 – 12,00,000 (10% of 4,00,000)	40,000
12,00,001 – 16,00,000 (15% of 4,00,000)	60,000
16,00,001 – 17,25,000 (20% of 1,25,000)	25,000
Total Tax	**1,45,000**
Health & Education Cess (4%)	5,800
Final Tax Liability	**1,50,800**

Table 7: Tax Calculation under Old Regime (₹18,00,000 - Assuming ₹2,00,000 total deductions)

Particulars	Amount (₹)
Gross Salary	18,00,000
Less: Standard Deduction + Other Deductions	2,50,000
Taxable Income	**15,50,000**

Tax Calculation:

Income Slab (₹)	Tax Amount (₹)
0 – 2,50,000	Nil
2,50,001 – 5,00,000 (5% of 2,50,000)	12,500
5,00,001 – 10,00,000 (20% of 5,00,000)	1,00,000
10,00,001 – 15,50,000 (30% of 5,50,000)	1,65,000
Total Tax	**2,77,500**
Health & Education Cess (4%)	11,100
Final Tax Liability	**2,88,600**

Tax Saving under New Regime = ₹1,37,800

Comparative Summary

Table 8: Comparative Tax Liability Under Old and New Regimes

Gross Salary (₹)	Old Regime Tax (₹)	New Regime Tax (₹)	Tax Saving (₹)
9,00,000	96,200	0	**96,200**
12,00,000	1,17,000	0	**1,17,000**
18,00,000	2,88,600	1,50,800	**1,37,800**

Empirical Findings Interpretation.

Zero Tax Zone Expansion: The people with an annual income of up to [₹]12 lakhs will pay no tax in the new regime provided they have rebate conditions.

Middle-Income Advantage: The highest proportional advantage will be attained at the [₹]10-20 lakh income category.

Less Reliance on Deduction: The tax load is also low despite the absence of aggressive tax-saving investments.

Gradual Structure Mixed: Increasing marginal rates are still imposed on the higher income groups.
Significant Reduction in Tax: Effective tax liability will have reduced significantly in middle-income salaried individuals in AY 2026-27.
Higher Disposable Income: Take-home pay has been rising and this might trigger a growth in consumption.
Streamlined Compliance: The new regime is more simplified than the old system.
Potential Change in Savings Patterns: The long-term saving pattern can be structurally changed by lessening the incentives on deductions.

Conclusion

The income tax reforms that apply to AY 2026-27 will be a careful weighted policy option that seeks to consider the revenue aspect and the economic gains of the middle-income earners. The government by reinforcing Section 115BAC under the umbrella of the Income-tax Act, 1961, has placed the focus on simplification and increase of disposable income of the salaried taxpayers.
Although the short-term gains in terms of higher take-home remuneration are clear, the overall effects on the household savings and the overall financial planning should be monitored. Thus, it is generally possible to note that the reforms mark the shift to a smoothing and consumption-friendly tax system of Indian salaried taxpayers.

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