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EY Tax Alert

Key Changes under the Income tax Rules, 2026

EY Alerts cover significant tax news, developments and changes in legislation that affect Indian businesses. They act as technical summaries to keep you on top of the latest tax issues. For more information, please contact your EY advisor.

Executive summary

On 20 March 2026, the Central Board of Direct Taxes (CBDT) notified the Income-tax Rules, 2026 (New Rules) to operationalise the provisions of the Income-tax Act, 2025, effective from tax year 2026-27. This alert summarizes the key changes introduced by the New Rules that impact salaried individuals, such as the replacement of prescribed forms for foreign tax credit and salary-related claims; expansion of the list of cities eligible for higher House Rent Allowance (HRA) exemption; enhancement of exemption limits for specified allowances; and revisions to the valuation of perquisites relating to food benefits, gifts, and motor cars.

These key changes are effective from 1 April 2026 and necessitate immediate action by employers, payroll teams and employees.



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Background

- The Government of India, through the Ministry of Finance, Department of Revenue, Central Board of Direct Taxes (CBDT), issued a press release dated 1 April 2026 announcing that the Income-tax Act, 2025 has come into force with effect from 1 April 2026.
- The Income-tax Act, 2025 replaces the Income-tax Act, 1961 and is described as a reform aimed at simplifying and modernizing India's income-tax law. The Act focuses on greater clarity and ease of compliance through simpler language, a streamlined structure, and a reader-friendly presentation, without altering the underlying tax policy.
- The Bill was passed by Parliament on 12 August 2025 and received the assent of the Hon'ble President of India on 21 August 2025, on which date it became the Income-tax Act, 2025. The Income-tax Rules, 2026 were notified by the CBDT on 20 March 2026 to operationalize the provisions of the new Act.
- The corresponding new Forms under the Act have also been notified. These Forms have been simplified, standardized, and process re-engineered to make compliance simpler.
- With its implementation from 1 April 2026, the Income-tax Act, 2025 marks a new chapter in India's tax administration and an important step towards Viksit Bharat.

Key takeaways

Procedural changes in Claiming Foreign Tax Credit

- The prescribed form for furnishing details to claim foreign tax credit has been changed from Form 67 to Form 44. Where foreign taxes paid or deducted exceed INR 1,00,000, it is mandatory to furnish a certificate from a Chartered Accountant

Furnishing of salary related claims to employer

- For the purposes of deduction of tax at source under the head 'Salaries', Form 12BB has been replaced by Form 124 for furnishing evidence of claims by an employee to the employer.

Form 124 additionally requires an employee claiming exemption in respect of House Rent Allowance (HRA) to disclose whether any relationship exists with the landlord, where such exemption is claimed

House Rent Allowance - expansion of eligible cities

- The list of cities eligible for a higher exemption of 50% of salary for House Rent Allowance, under the provisions applicable to individuals opting for the old tax regime, has been expanded.

In addition to Mumbai, Delhi, Kolkata and Chennai, the higher exemption shall now apply to Bengaluru, Hyderabad, Pune and Ahmedabad

Prescribed allowances - enhanced exemption limits

- The following table summarizes the revised exemption limits, all applicable under the old tax regime:

Allowance	Income Tax Rules, 1962 (Exemption)	Income Tax Rules, 2026 (Exemption)	Condition
Children Education Allowance	INR 100 pm per child	INR 3,000 pm per child	Max 2 children; old regime only
Hostel Expenditure Allowance	INR 300 pm per child	INR 9,000 pm per child	Max 2 children; old regime only
Transport Allowance (specified people with disability)	INR 3,200 pm (all India)	INR 15,000 pm + DA (metro) INR 8,000 pm + DA (other cities)	Expanded to upper extremity disabilities

Valuation of perquisites

- a. Free food and non-alcoholic beverages
 - The exemption threshold in respect of free food and non-alcoholic beverages provided by the employer during working hours at office or business premises, or by way of paid vouchers usable only at eating joints, has been enhanced from INR 50 per meal to INR 200 per meal.
- b. Gifts, vouchers or tokens
 - The exemption threshold for gifts, vouchers, or tokens provided to employees has been increased from INR 5,000 to INR 15,000 in aggregate per tax year.

c. Use of movable assets

- In relation to valuation of benefits arising from use of movable assets belonging to the employer by the employee or any member of the employee's household, the list of assets excluded from perquisite valuation has been expanded. In addition to laptops and computers under the existing rule, mobile phones and tablets are now specifically excluded from perquisite valuation

d. Motor car - revised perquisite valuation/exemption

Scenario A: Motor car owned or hired by the employer – Provided to the employee for official Duties and Personal Use

A1. Employer bears running and maintenance expenses

Particulars	Income Tax Rules, 1962	Income Tax Rules, 2026
Engine cubic capacity Up to 1.6 litres or the motor car is an Electric vehicle	INR 1,800 pm (plus INR 900 for chauffeur, if provided). Perquisite valuation not provided for Electric Vehicle	INR 5,000 pm (plus INR 3,000 for chauffeur, if provided)
Engine cubic capacity Above 1.6 litres	INR 2,400 pm (plus INR 900 for chauffeur, if provided)	INR 7,000 pm (plus INR 3,000 for chauffeur, if provided)

A2. Employee bears running and maintenance expenses

Particulars	Income Tax Rules, 1962	Income Tax Rules, 2026
Engine cubic capacity Up to 1.6 litres or the motor car is an Electric vehicle	INR 600 pm (plus INR 900 for chauffeur, if provided) Perquisite valuation not provided for Electric Vehicle	INR 2,000 pm (plus INR 3,000 for chauffeur, if provided)
Engine cubic capacity Above 1.6 litres	INR 900 pm (plus INR 900 for chauffeur, if provided)	INR 3,000 pm (plus INR 3,000 for chauffeur, if provided)

Scenario B: Motor car owned by the employee – used for Official Duties and Personal Use

B1. Employer bears running and maintenance expenses (motor car)

Particulars	Income Tax Rules, 1962 (Exemption)	Income Tax Rules, 2026 (Exemption)
Engine cubic capacity Up to 1.6 litres or the motor car is an Electric vehicle	Exempt amount INR 1,800 pm (plus INR 900 for chauffeur, if provided) Perquisite valuation not provided for Electric Vehicle	Exempt amount INR 5,000 pm (plus INR 3,000 for chauffeur, if provided)
Engine cubic capacity Above 1.6 litres	Exempt amount INR 2,400 pm (plus INR 900 for chauffeur, if provided)	Exempt amount INR 7,000 pm (plus INR 3,000 for chauffeur, if provided)

B2. Employer bears running and maintenance expenses (other automotive vehicle)

Income Tax Rules, 1962 (Exemption)	Income tax Rules, 2026 (Exemption)
Exempt amount INR 900 pm	Exempt amount INR 3,000 pm

Reconsideration of tax regime choice

- Given the simultaneous enhancement in exemption limits for certain allowances, the upward revision in taxable perquisite values in respect of motor cars, and the expansion of cities eligible for the higher 50% House Rent Allowance exemption, individuals may need to re-evaluate the relative tax efficiency of the old versus the new tax regime, taking into account their salary structure, perquisite profile and available exemptions.

Comments

Introduction of New Income tax Rules reflect the Government's continued focus on simplification of compliance, targeted employee welfare, and alignment of exemption thresholds with current cost structures. Employers will need to revisit payroll systems, declaration formats and perquisite valuation methodologies to align with the New Income tax Rules 2026. Early alignment with the revised changes will be critical to mitigate compliance gaps and ensure smooth tax withholding and reporting from tax year 2026-27 onwards.

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



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