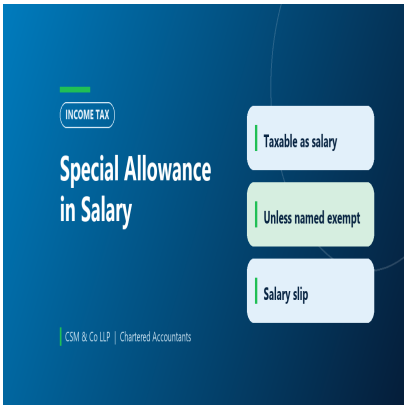

Special Allowance in Salary: How It Is Taxed and Which Allowances Are Exempt

Description

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Quick summary

- A “special allowance” shown in a salary slip is taxable as salary unless it is one of the allowances the law names as exempt.
- Exempt allowances include travel on tour or transfer, daily charges, conveyance in duties, helper, research and uniform allowances, up to actual expenditure, and fixed-limit allowances such as children’s education (?3,000 a month per child from 01/04/2026).
- In the new tax regime only the travel, daily charge and conveyance allowances (and the disabled employee transport allowance) stay exempt; the rest need the old regime.
- The list is in Schedule III of the Income-tax Act, 2025 and Rule 280 of the Income-tax Rules, 2026.

Many salary slips show a line called “special allowance”. It is usually a balancing amount that the employer adds to reach the agreed total pay. For tax, the name does not matter. The allowance is taxable as salary unless the law specifically names it as exempt.

Which allowances are exempt?

Until FY 2025-26 the exemptions were under section 10(14) of the Income-tax Act, 1961 and Rule 2BB. From Tax Year 2026-27 they are in Schedule III (Table Sl. Nos. 12 and 13) of the Income-tax Act, 2025, and Rule 280 of the Income-tax Rules, 2026.

Exempt up to the actual expenditure (Schedule III, Sl. No. 12)

Allowance	Exempt up to
Travel on tour or transfer, and transfer, packing and transportation of personal effects	Actual expense

Allowance	Exempt up to
Daily charges while away from the normal place of duty on tour or transfer	Actual expense
Conveyance in the performance of duties (no free conveyance from the employer)	Actual expense
Helper engaged for the performance of duties	Actual expense
Academic, research and training pursuits in educational and research institutions	Actual expense
Purchase or maintenance of uniform	Actual expense

Exempt up to a fixed limit (Schedule III, Sl. No. 13), from 01/04/2026

Allowance	Exempt amount
Children education allowance	?3,000 a month per child, up to two children
Hostel expenditure allowance	?9,000 a month per child, up to two children
Transport allowance for a blind, deaf and dumb or orthopaedically disabled employee	?15,000 a month plus dearness allowance (metro cities) or ?8,000 plus dearness allowance (other cities)
Transport business employee (no daily allowance)	70% of the allowance, up to ?25,000 a month
Underground mine allowance	15% of basic pay
Special compensatory (remote locality), tough location allowances	?1,500, ?4,500 or ?7,000 a month, depending on the place
Compensatory field area allowance	?13,500 a month in notified areas
Compensatory modified field area allowance	?8,000 a month in notified areas
Island duty allowance (Andaman and Nicobar, Lakshadweep)	10%, 16% or 20% of basic pay, depending on the area
Armed forces allowances: counter-insurgency, highly active field area, high altitude, Siachen	?22,000, ?22,000, ?4,500 to ?30,000 and ?42,500 a month

Up to FY 2025-26 the old limits applied, for example ?100 a month per child for education, ?300 for hostel, ?3,200 for the disabled employee's transport allowance and 70% up to ?10,000 for transport business employees.

What stays exempt in the new tax regime?

Under section 202 of the Income-tax Act, 2025 the new regime does not give most exemptions under Schedule III Sl. Nos. 12 and 13, except those prescribed. Rule 280(3) prescribes the allowances for travel on tour or transfer, packing and transport of effects, daily charges, conveyance in duties, and the disabled employee's transport allowance. Helper, research, uniform, children education, hostel and the other fixed-limit allowances need the old regime.

When is a special allowance taxable?

- A plain "special allowance", a fixed allowance, a city compensatory allowance, dearness allowance and an allowance that you can spend as you wish are all taxable.
- An exempt allowance becomes taxable if it does not meet the conditions of the rule, for example conveyance allowance when the employer gives a free car.
- HRA has its own rules under the HRA exemption.

Does restructuring your salary help?

Under the old regime, if your employer pays genuine exempt allowances (for example uniform or children education), the exempt part reduces taxable salary. Moving amounts from taxable special allowance to exempt allowances you do not actually qualify for gives no benefit and can create a tax demand. Work out your tax under both regimes before you decide.

Examples

1. Ms V has a "special allowance" of ?10,000 a month in her slip. It is not named in the rule, so it is fully taxable.
2. Mr C is a public sector doctor posted at a tribal area medical camp and gets a notified special compensatory allowance. It is exempt up to the limit for that place, in the old regime.
3. Ms S gets children education allowance for two children. From 01/04/2026, up to ?3,000 a month per child (?72,000 a year for two) is exempt in the old regime, and ?9,000 a month per child (?2,16,000 a year for two) for hostel allowance.

Frequently asked questions

Is special allowance taxable?

Yes, a general special allowance shown in the salary slip is taxable as salary. It is exempt only if it matches one of the allowances listed in the rules and you meet the conditions.

Can I save tax by increasing allowances in my salary?

Only if the allowances are genuinely exempt and you spend them (or fall within a fixed limit) and you are in the old regime. A plain special allowance does not save tax.

Which allowances stay exempt in the new regime?

Allowances for travel on tour or transfer, daily charges while travelling, conveyance in the performance of duties, and the transport allowance of a disabled employee.

Where is the list of exempt allowances?

In Schedule III (Sl. Nos. 12 and 13) of the Income-tax Act, 2025 and Rule 280 of the Income-tax Rules, 2026.

Official sources

- Income-tax Rules, 2026 (Rule 280)
- Income Tax Department: Income-tax Act, 2025 (as amended by Finance Act 2026), Schedule III and section 202
- Income Tax Department: e-Filing portal

Related reading

- What is House Rent Allowance (HRA): Exemption, Calculation and New Rules 2026
- Conveyance Allowance: Exemption Limit, Calculation and Eligibility
- Transport Allowance: Tax Exemption, Limits for Tax Year 2026-27 and Rules

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