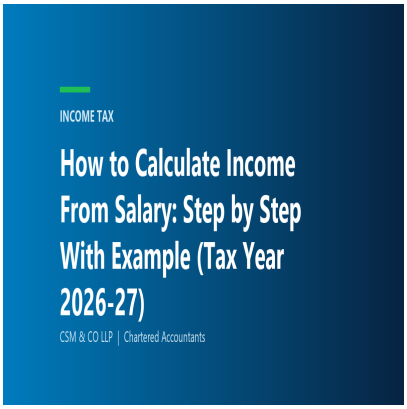

How to Calculate Income From Salary: Step by Step With Example (Tax Year 2026-27)

Description

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Quick summary

- Income from salary is worked out in four steps: add everything that counts as salary (section 16), subtract the exempt allowances, add taxable perquisites, then subtract the section 19 deductions.
- Section 19 allows the standard deduction (?75,000 new regime, ?50,000 old), professional tax (old regime) and retirement items such as gratuity and leave encashment within their limits.
- Chapter VIII deductions (section 123 and others) are subtracted afterwards, in the old regime only.
- Employers deduct TDS on salary under section 392 and issue Form 130 by 15 June; check it against your AIS before filing.

Income from salary is the first and usually the largest head of income for an employee. This post shows how it is worked out under the Income-tax Act, 2025 and then how tax is calculated on it, with a full example under both regimes.

Step 1: add up what counts as salary

Section 16 of the Act says salary includes:

- wages (basic pay, dearness allowance, allowances, bonus),
- any annuity or pension,
- any gratuity,
- any fees or commission,
- perquisites (rent-free accommodation, a car for personal use, free shares and others in section 17),
- profits in lieu of salary (section 18), such as compensation on termination,
- any advance of salary,
- any payment for leave not availed of (leave encashment),
- the taxable annual accretion to a recognised provident fund, and
- the employer’s contribution to the notified pension scheme (NPS).

Under section 15, salary due to you in the tax year is chargeable whether paid or not, salary paid in advance is chargeable in the year it is paid, and arrears paid in the year are chargeable if not taxed earlier. So salary that is due but unpaid at year end is still income of that year.

Step 2: take out exempt allowances

Some allowances are exempt in part or full, within limits, under Schedule III and Rule 279. The best known is **house rent allowance** (old regime only). It is exempt to the extent of the least of the HRA received, the rent paid less 10% of salary, and 50% of salary in Mumbai, Kolkata, Delhi, Chennai, Hyderabad, Pune, Ahmedabad and Bengaluru (40% elsewhere), where salary is basic pay plus dearness allowance if the terms provide. Leave travel concession and some others are also old regime items. See our posts on allowances for each.

Step 3: add the taxable perquisites

Free or concessional accommodation, a car, free meals above the limit, loans at a low rate, gifts above the limit, and shares allotted under an ESOP or RSU are valued under Rule 15 and added. See our posts on perquisites and ESOP taxation.

Step 4: subtract the deductions from salary (section 19)

Deduction	Amount	Regime
Professional tax	The whole amount	Old only
Standard deduction	?75,000, or the salary if less	New
Standard deduction	?50,000, or the salary if less	Old
Death-cum-retirement gratuity of government employees	The whole amount	Both
Gratuity of other employees	Within the limits in our gratuity post	Both
Leave encashment on retirement	Government employees: the whole amount. Others: the least of the cash equivalent of leave at credit (up to 30 days for each year of service), ten times the average monthly salary of the last ten months, the notified limit and the amount received	Both
Voluntary retirement payment	The least of the amount received and ?5,00,000, subject to the conditions in section 19(2)(e)	Both

Deduction	Amount	Regime
Retrenchment compensation to a workman	The least of three amounts in the Table	Both

The result is **income from salary**. If you received arrears or advance salary that pushes you into a higher slab, claim **relief under section 157** with Form 39.

Step 5: from income from salary to taxable income

Add income from other heads (house property, other sources and so on), set off losses and then, **in the old regime only,** subtract the Chapter VIII deductions: section 123 (up to ?1,50,000), your own NPS contribution up to ?50,000, health insurance, education loan interest, donations and others. The new regime allows only a few of these, mainly the employer's NPS contribution. The balance is **total income**.

Step 6: apply the rates

New regime (section 202), tax year 2026-27: up to ?4,00,000 nil; 5% to ?8,00,000; 10% to ?12,00,000; 15% to ?16,00,000; 20% to ?20,00,000; 25% to ?24,00,000; 30% above. Rebate under section 156(2) of up to ?60,000 if total income is up to ?12,00,000.

Old regime: up to ?2,50,000 nil; 5% to ?5,00,000; 20% to ?10,00,000; 30% above. Rebate of up to ?12,500 if total income is up to ?5,00,000. Higher basic exemption limits apply for resident senior citizens.

Then add surcharge if income is above ?50 lakh, and **4% health and education cess**.

Worked example

Basic ?6,00,000, HRA ?3,00,000, special allowance ?4,50,000, bonus ?1,50,000. Employee's PF ?72,000. Rent paid ?3,30,000 a year in Pune. Professional tax ?2,400. Other qualifying investments ?78,000.

Item	Old regime (?)	New regime (?)
Gross salary	15,00,000	15,00,000
Less: HRA exemption (least of 3,00,000; 3,30,000 - 60,000 = 2,70,000; 50% of 6,00,000 = 3,00,000)	2,70,000	Not available
Less: professional tax	2,400	Not available
Less: standard deduction	50,000	75,000
Income from salary	**11,77,600**	**14,25,000**
Less: section 123 (PF 72,000 + others 78,000)	1,50,000	Not available

Item	Old regime (?)	New regime (?)
Total income	**10,27,600**	**14,25,000**
Tax on slabs	1,20,780	93,750
Add: cess at 4%	4,831	3,750
Tax payable	**1,25,611**	**97,500**

The new regime costs ?28,111 less for this employee because the deductions (?4,72,400 in all: HRA, professional tax, standard deduction and section 123) are below the break-even for a ?15 lakh salary. See our post on saving tax by salary level.

TDS on salary

The employer deducts tax on salary under **section 392(1)** at the average rate on your estimated income for the year, after taking into account the evidence you give in **Form 124** (Rule 205) and details of other income and previous employment (Form 122). It can adjust later months for any excess or shortfall (section 392(5)(c)). The employer pays the tax to the government and issues **Form 130** by **15 June** after the end of the year (Rule 215).

Documents you need to file the return

1. **Form 130**, the TDS certificate for salary.
2. **AIS** and the TDS statement on the e-filing portal, to reconcile TDS and any interest or other income.
3. **Rent receipts, landlord's PAN, investment and loan statements** for the old regime claims.
4. **Form 123**, if the employer gives perquisite details separately.

If Form 130 and your AIS differ, ask your employer to correct the TDS return before you file, or report the figures you are able to support.

Frequently asked questions

What is included in salary for income tax?

Wages, any annuity or pension, gratuity, fees or commission, perquisites, profits in lieu of salary, advance salary, payment for leave not availed of, and certain provident fund and pension scheme items (section 16 of the Income-tax Act, 2025).

What deductions are allowed from salary?

Under section 19(1): professional tax (old regime only), the standard deduction (?75,000 new regime,

?50,000 old regime), and retirement items such as gratuity, leave encashment and commutation of pension within their limits.

Is the standard deduction available in both regimes?

Yes. It is ?75,000 or the salary, whichever is less, in the new regime, and ?50,000 or the salary, whichever is less, in the old regime.

Which form shows my salary and TDS?

Form 130, the TDS certificate for salary under section 395. The employer must furnish it by 15 June after the end of the tax year (Rule 215).

Do I need Form 124?

Give your employer Form 124 with evidence of HRA, LTA, home loan interest and Chapter VIII claims so that TDS is deducted on the right income (section 392(5)(b), Rule 205).

Where do I report salary in the return?

In the salary schedule of the return, using Form 130 and the figures in your AIS. Reconcile any difference before filing.

Official sources

- Income Tax Department: Income-tax Act, 2025 (sections 16, 17, 19, 123, 156, 202, 392)
- Income Tax Department: Income-tax Rules, 2026 (Rules 205, 215, 279)
- Finance Act, 2026 (rates for tax year 2026-27)

Related reading

- What is House Rent Allowance (HRA): Exemption, Calculation and New Rules 2026
- Special Allowance in Salary: How It Is Taxed and Which Allowances Are Exempt
- Conveyance Allowance: Exemption Limit, Calculation and Eligibility

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