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A Paradigm Shift from Exemption-Based to Concession-Based Taxation in India: A Critical Analysis of the New Income Tax Regime

SAKSHI SONI* AND RASHMI SINGH**

ABSTRACT

*This paper examines the structural transition in India's personal income taxation from an exemption-based model to a concession-based model effected through the introduction of Section 115BAC by the Finance Act, 2020 and its consolidation by the Finance Act, 2023. It traces the welfare-oriented, deduction-driven philosophy that historically shaped the Income-tax Act, 1961, in which provisions such as Section 80C, Section 80D and housing-loan deductions channelled household savings towards socially desirable instruments. Against that background, the paper analyses the legislative intent behind Section 115BAC, namely simplification, neutrality in taxpayer decision-making and reduction of the compliance burden, and evaluates the consequences of making the new regime the default option. It assesses the likely effects on savings behaviour, middle-class taxpayers, welfare orientation and investment culture, and surveys the practical challenges of administering parallel regimes, including the difficulties posed by Form 10-IE. Drawing on recent decisions of the Income Tax Appellate Tribunal and the Bombay High Court, including *The Chamber of Tax Consultants v. Director General of Income Tax (Systems)*, the paper argues that judicial attention has so far centred on procedural and technological questions rather than the constitutional validity of the regime, and concludes that the long-term success of the shift depends on its sensitivity to the diverse needs of taxpayers.*

Keywords: *New tax regime, Section 115BAC, exemption-based taxation, concession-based taxation, income tax, fiscal policy.*

I. INTRODUCTION

Taxation is one of the most important tools of economic governance. Tax policy serves not only to generate revenue but also to influence social and economic behaviour. India's income tax system has historically developed around the deductions and exemptions of the Income-tax Act, 1961, which encouraged taxpayers to invest, save, insure and contribute to welfare-oriented

* Author is a Guest Faculty at the Department of Law, University of Allahabad, India.

** Author is a Research Scholar at the Department of Law, University of Allahabad, India.

financial schemes. This model embodied a welfare-oriented fiscal philosophy that treated taxation as both a tool for development and a source of state revenue. Under the old regime, the Income-tax Act permitted taxpayers to claim a range of Chapter VI-A deductions, exemptions for allowances and benefits relating to home loans, insurance, pension contributions and medical expenses. As a result, India's personal tax system became heavily reliant on deductions. Although this structure promoted investment and savings, it also produced increasing complexity, administrative difficulties, disputes and compliance burdens.

The Finance Act, 2020, which introduced Section 115BAC, brought about a significant change. Subject to the requirement that taxpayers renounce the majority of exemptions and deductions, the provision established an optional concessional tax regime with reduced slab rates. The Finance Act, 2023 strengthened this system further by making it the default regime and by adding new benefits, including higher rebate caps and standard deduction benefits.

This change reflects a larger shift in India's fiscal strategy, which now encourages tax simplification and greater compliance through concessional rates rather than rewarding particular economic behaviour through exemptions. The change has significant ramifications for taxpayers, as well as for investment culture, saving habits and the function of taxation in socio-economic planning.

II. EVOLUTION OF EXEMPTION-BASED TAXATION IN INDIA

The Indian tax system has consistently used tax incentives to promote socially desirable spending. Post-independence fiscal policy adopted a welfare-oriented approach and used deductions and exemptions to direct household savings towards government-approved instruments and developmental sectors.¹

Several provisions of the Income-tax Act mirrored this approach. Section 80C encouraged investments in provident funds, life insurance, National Savings Certificates and Equity Linked Savings Schemes. Section 80D encouraged health insurance coverage. Housing loan deductions under Sections 24(b) and 80EE encouraged home ownership. In a similar vein, the House Rent Allowance and Leave Travel Allowance exemptions sought to lessen the tax burden on salaried workers.

This exemption-oriented method accomplished several goals simultaneously: promoting insurance coverage, strengthening investments over time, supporting welfare programmes, encouraging household savings and improving the housing and infrastructure sectors.²

¹ Raja J. Chelliah, Tax Reforms Committee: Final Report 12–15 (Ministry of Finance, Gov't of India 1992).

² M. Govinda Rao, *Tax Reforms in India: Achievements and Challenges*, 7 ASIA PAC. DEV. J. 37, 37 (2000).

Over time, however, the tax system's many exclusions led to structural problems. Taxpayers frequently chose investment instruments more for tax savings than for genuine financial planning. The system also produced disparities between taxpayers who could claim deductions and those who lacked sufficient means to invest in tax-saving products.

The exemption-heavy structure further raised administrative complexity and compliance costs. The need for tax authorities to verify claims, supporting evidence and eligibility requirements led to an increase in litigation and disputes over interpretation.

III. LEGISLATIVE INTENT BEHIND SECTION 115BAC

The introduction of Section 115BAC by the Finance Act, 2020 marked a break from India's long-standing, exemption-driven model of personal income taxation. It was expressly framed as an exercise in the simplification and rationalisation of the individual and Hindu Undivided Family (HUF) tax base.³ The Finance Minister's Budget speech characterised the prevailing regime as complicated and difficult to claim correctly. The regime was so heavily populated with exemptions that ordinary taxpayers found it difficult both to understand and to claim them. The Memorandum to the Finance Bill, 2020 similarly described the existing structure as exemption-driven, where each new incentive added a further layer of complexity and paperwork. The mischief identified in legislative terms was not the level of tax but the compliance cost, the additional paperwork, the disputes and the distorted investment decisions caused by too many deductions and allowances under Chapter VI-A and other heads of income.

Three immediate objectives underlay Section 115BAC. First, Parliament sought to simplify individual and HUF taxation by offering a concessional rate schedule with a pruned list of exemptions and deductions.⁴ Second, it aimed to promote greater neutrality in taxpayer decision-making, so that people would not feel compelled to buy particular savings or insurance products for fiscal reasons alone rather than for genuine financial planning. Third, the provision was designed to lower disputes and the administrative burden by reducing the need to maintain extensive documentary proof.⁵

At the same time, Parliament did not scrap the old exemption-based regime overnight. Section 115BAC was introduced as an optional alternative. Taxpayers willing to give up most exemptions and deductions could choose the new lower slab rates, while others could

³ The Finance Act, 2020, No. 12 of 2020, § 115BAC, Acts of Parliament, 2020 (India).

⁴ Nirmala Sitharaman, Minister of Fin., *Budget 2020–21: Speech of the Finance Minister* ¶¶ 118–24 (Feb. 1, 2020) (India).

⁵ Ministry of Fin., Dep't of Revenue, *Memorandum Explaining the Provisions in the Finance Bill, 2020* ¶¶ 115–25 (2020) (India).

continue with the old regime. This dual-regime design was expressly presented as a transitional arrangement: it respected existing savings habits built around tax incentives while slowly pushing taxpayers towards a simpler, lower-rate regime.

The Finance Act, 2023 signified a second phase. It inserted Section 115BAC(1A), changed the slab rates, increased the rebate under Section 87A and, most importantly, made the new regime the default choice for individuals and HUFs from the financial year 2023-24 onwards. The clarification issued by the Press Information Bureau on 31 March 2024 confirms that the legislature now treats the exemption-based regime as a limited fall-back option rather than an equal alternative.⁶ Seen in this light, Section 115BAC is not only about changing slab rates. It is meant to reduce exemptions and deductions gradually, ease compliance and encourage voluntary tax payment while moving towards a simpler, broad-based, low-rate personal tax system.⁷

IV. CRITICAL ANALYSIS OF THE SHIFT TOWARDS CONCESSION-BASED TAXATION

A. Impact on savings behaviour

One of the main criticisms concerns the potential effect of the new concessional tax regime on consumer savings behaviour. Deductions under provisions such as Section 80C in India's long-standing savings-oriented tax system encouraged investments in provident funds, life insurance policies, pension plans and other government-backed financial instruments. These deductions were policy instruments intended to support long-term financial security and capital formation, rather than mere budgetary concessions.

In exchange for lower tax rates, the new tax structure under Section 115BAC significantly restricts the availability of such deductions. As a result, taxpayers who choose the concessional system may no longer feel motivated to invest in conventional savings products. This could eventually erode disciplined saving habits, especially among middle-class salaried taxpayers who previously based their financial planning on tax-saving investments.⁸

India's lack of a reliable social security system on par with other economies makes the issue more significant there. In the past, tax incentives encouraged people to build private financial safeguards through savings and insurance, making up for insufficient pension coverage and a

⁶ Press Info. Bureau, Gov't of India, *Clarification Regarding Applicability of New Tax Regime and Old Tax Regime* (Mar. 31, 2024).

⁷ Centre for Budget & Governance Accountability, *Use and Abuse of Tax Breaks: How Tax Incentives Undermine Equity and Fiscal Transparency in India* 7–18 (2020).

⁸ Girish Ahuja & Ravi Gupta, *Systematic Approach to Income Tax* 1.42–1.47 (Bharat Law House 2024).

weak welfare system. The reduction of these incentives may therefore have a negative effect on retirement readiness and long-term financial resilience.

B. Effects on middle-class taxpayers

For taxpayers seeking easier compliance, the concessional system is frequently promoted as advantageous. The real benefits, however, differ significantly according to one's financial position. Deductions for provident fund contributions, home loans, health insurance, tuition fees and other qualifying expenses have historically been a major source of relief for middle-class salaried individuals. Under the old system, taxpayers could use structured investments and deductions to reduce their taxable income substantially. The concessional regime, by contrast, offers lower rates but removes most exemptions and deductions. The earlier regime may therefore remain more favourable financially for taxpayers who actively invest in tax-saving instruments.

C. Simplification versus welfare orientation

The shift in India's fiscal policy from exemption-based taxation to concession-based taxation reflects a larger conceptual change. India has historically pursued a welfare-oriented taxation policy, using tax incentives as tools to encourage socially acceptable economic behaviour, including property ownership, insurance and saving.⁹

By prioritising neutrality and administrative effectiveness, the concessional regime departs from this strategy. Rather than using incentives to influence taxpayer behaviour, the state aims to establish a more straightforward tax system with reduced rates and few exemptions. This approach lessens the redistributive and welfare-oriented character of taxation, even as it may increase transparency and ease compliance requirements.

D. Increased consumerism and reduced investment culture

The concessional regime has also been criticised for encouraging short-term consumption at the expense of long-term investment behaviour. Under the previous system, taxpayers were prompted to set aside a portion of their income for savings instruments in order to obtain tax benefits. The diminished significance of deductions under Section 115BAC raises disposable income without necessarily channelling it into productive investment avenues. As a result, taxpayers may favour short-term spending over long-term financial planning.¹⁰

⁹ Raja J. Chelliah, *Fiscal Policy in India* 86–91 (1996).

¹⁰ Parthasarathi Shome, *First Report of the Tax Administration Reform Commission* (Ministry of Finance 2014).

Although higher consumption may temporarily boost economic demand, an unsustainable decline in household savings may adversely affect long-term capital formation and economic stability. India's growth model has always relied heavily on domestic savings as a source of funds for investment.¹¹ A persistent decrease in savings-oriented taxation may therefore have macroeconomic ramifications that extend beyond personal tax obligations.

Furthermore, as tax deductions become less significant, industries that have historically relied on tax incentives, such as insurance, pension funds and small savings schemes, may experience a decline in participation.

V. CHALLENGES IN IMPLEMENTATION

While Section 115BAC promises simplification at the level of statutory design, its implementation has produced several practical challenges.

A. Complexity of the dual regime and the annual choice

The most immediate implementation challenge lies in the decision to run two parallel tax regimes simultaneously. Under the current framework, individual and HUF taxpayers must choose, for each assessment year, whether to be taxed under the traditional exemption-based regime or under the concessional regime under Section 115BAC. In the case of persons with business or professional income, once they opt into the new regime their ability to revert to the old regime is significantly constrained.¹²

For the average taxpayer, especially one without professional assistance, it is difficult to compute the tax liability and other factors under both regimes and then make an informed choice. The statutory promise of freedom to choose between regimes is, in practice, limited by capacity and information constraints.

B. TDS administration and employer-side burdens

Section 115BAC has also added complexity at the level of Tax Deducted at Source (TDS), particularly for salaried employees. After the provision came into force, the Central Board of Direct Taxes (CBDT) had to issue circulars and clarifications on how an employer should compute TDS on the basis of the employee's preferred regime.

Many organisations run parallel payroll calculations under both the old and new regimes to determine the most beneficial option for employees. This increases compliance costs through additional software requirements, trained personnel and complex TDS calculations. Differences

¹¹ Reserve Bank of India, *Handbook of Statistics on the Indian Economy, 2024–25* (2025).

¹² Axis Bank, *Difference Between New and Old Tax Regime – Which One Should You Choose?* (June 26, 2025).

between the regime selected for TDS and the regime ultimately chosen at the time of filing returns often result in refunds or additional tax liabilities, thereby creating administrative complications.

C. Product-market distortion and risks of mis-selling

Section 115BAC also affects the financial-product market that was traditionally linked to tax savings. For many years, banks, insurance companies and mutual funds promoted tax-saving products such as fixed deposits, life insurance policies and equity linked saving schemes because they offered deductions under Section 80C. Under the new regime, many of these deductions are no longer available. This creates a risk that investors may buy long-term tax-saving products without actually receiving any tax benefit. In the long run, a decline in tax-driven investments may reduce the flow of stable funds into the financial sector and government-backed savings schemes, thereby affecting broader economic and investment patterns.

D. Frequent amendments and transitional uncertainty

Another important challenge is the frequent modification of the legal framework surrounding Section 115BAC. Since its introduction in 2020, the provision has undergone major changes through the Finance Act, 2023, including revised tax slabs, rebate limits and the introduction of the new regime as the default system. These amendments also required corresponding changes in the Income-tax Rules relating to allowances, perquisites and depreciation. Individuals who made long-term financial commitments, such as home loans, insurance policies or pension investments, based on earlier tax benefits may face uncertainty regarding the continued relevance of such investments. Although changes in tax laws are common, repeated alterations to Section 115BAC undermine its claim to provide a stable and simplified alternative.

VI. JUDICIAL APPROACH TO PROCEDURAL AND TECHNOLOGICAL ISSUES UNDER SECTION 115BAC

Recent decisions of the Income Tax Appellate Tribunal (ITAT) and the High Courts show that courts are mainly dealing with procedural and portal-related issues under Section 115BAC, rather than with the basic validity of the new regime. As of now, there is no reported High Court or Supreme Court judgment that has upheld or struck down Section 115BAC on constitutional grounds. The focus is on how taxpayers exercise their choice between the old and new regimes, how Form 10-IE is handled and how the e-filing system affects rights such as the Section 87A rebate.

In *Akshay Nitin Malu v. Income Tax Officer*,¹³ the assessee first filed Form 10-IE opting for the new regime but then filed his return under the old regime and claimed deductions allowed only under the old regime. The Centralised Processing Centre (CPC) processed the return under the new regime and denied these deductions. The Tribunal held that this was incorrect. It observed that the assessee could not be forced into the new regime merely because Form 10-IE had been filed earlier, when his actual return clearly showed that he wished to be taxed under the old regime.

In *Akshay Devendra Birari v. Deputy Commissioner of Income-tax*,¹⁴ the assessee filed his return under the new regime on time but submitted Form 10-IE only on 10 January 2024, after the due date of 31 July 2023. The CPC and the Commissioner (Appeals) denied the benefit of the new regime solely on the ground that Form 10-IE had been filed late. The Tribunal, however, treated the filing requirement as directory rather than strictly mandatory, since the form was available with the CPC at the time of processing and the assessee's intention to opt for the new regime was clear. The benefit of Section 115BAC could not, therefore, be refused merely because of a procedural delay. In *Rajeev Pandurang Kamat v. Income-tax Officer*,¹⁵ the assessee had filed Form 10-IE for the previous assessment year (AY 2022-23), but the form for AY 2023-24 could not be filed again because of technical restrictions on the portal. Following its own earlier rulings, including *Akshay Devendra Birari*, the Tribunal held that filing Form 10-IE is directory and that, once an assessee has opted for the new regime, there is no reason to deny that benefit in later years simply because of portal constraints.

In a further Pune ITAT case, *Seema Kulkarni v. Income Tax Officer*,¹⁶ the assessee first filed a return under the old regime and later filed a revised return under the new regime. In the revised return, she sought to claim the standard deduction and Chapter VI-A deductions that are not allowed under the new regime. The Tribunal held that, once a valid revised return under the new regime is filed, the original return becomes irrelevant, and the assessee cannot claim the standard deduction or 80C-type deductions. The appeal was dismissed and the CPC's processing under the new regime was upheld. The Bombay High Court's decision in *The Chamber of Tax Consultants v. Director General of Income Tax (Systems) & Ors.*¹⁷ concerns the Section 87A rebate in the context of the new regime. After a software update on 5 July 2024, the income-tax e-filing utility prevented many eligible taxpayers from claiming the Section 87A rebate for AY

¹³ *Akshay Nitin Malu v. Income Tax Officer*, (2025) 233 TTJ 491 (Pune Trib.).

¹⁴ *Akshay Devendra Birari v. Dy. Comm'r of Income Tax, CPC, Bengaluru*, 164 Taxmann.com 58 (Pune Trib. 2024).

¹⁵ *Rajeev Pandurang Kamat v. Income Tax Officer*, 2025 TaxPub (DT) 4101 (Pune Trib.).

¹⁶ *Seema Kulkarni v. Income Tax Officer*, ITA No. 3324/PUN/2025 (Pune Trib. Mar. 26, 2026).

¹⁷ *The Chamber of Tax Consultants v. Director Gen. of Income Tax (Systems) & Ors.*, 170 Taxmann.com 707 (Bom. H.C. 2025).

2024-25 under the new regime. The Chamber of Tax Consultants filed a public interest litigation arguing that this software change wrongly prevented taxpayers from exercising a statutory rebate. The Court held that the rebate under Section 87A is a substantive right and cannot be taken away by a mere change in the utility software.

VII. CONCLUSION

India's taxation policy has undergone a significant shift with the implementation of the new income tax regime, which represents a conscious move away from the country's long-standing exemption-based structure towards a concession-based system with lower tax rates and fewer deductions. This shift is not merely a procedural adjustment; it forms part of a larger policy reorientation that aims to streamline tax administration, improve compliance, increase transparency and reduce the difficulties involved in claiming numerous exemptions and deductions.

The analysis shows that the new regime accords with the government's goal of establishing a more efficient and taxpayer-friendly tax structure. By providing concessional tax rates and removing the majority of exemptions, the regime aims to reduce tax distortions, broaden the tax base and encourage voluntary compliance.

The evidence indicates, however, that not all categories of taxpayer benefit equally from the new regime. Depending on their income profile and financial obligations, people who have historically relied on deductions for investments, house loans, insurance payments and retirement savings may find the previous system more favourable. The coexistence of both regimes has created a transitional period during which taxpayers must carefully consider their financial position before choosing the better option.

From a policy standpoint, the move to concession-based taxation reflects a worldwide preference for more straightforward tax systems with lower rates and fewer exemptions. Concerns nevertheless remain about the possible effects on long-term saving habits, social welfare goals and the investment incentives that tax deductions previously promoted.

In conclusion, the new income tax regime represents a paradigm shift in India's direct tax system by prioritising neutrality, efficiency and simplicity over incentive-driven taxation. Although it offers significant benefits in terms of transparency and ease of compliance, its long-term efficacy will depend on taxpayer acceptance, ongoing policy improvements and the government's ability to ensure that the goals of equity, economic growth and fiscal sustainability are met simultaneously. If its implementation continues to be sensitive to the diverse needs of taxpayers and the shifting economic landscape, the new regime has the potential to become a

cornerstone of a modern and effective taxation framework as India's tax system continues to develop.
