Capital gains on alienation of equity-oriented mutual funds not taxable under the India-Mauritius DTAA

In the case of ***Emerging India Focus Funds, Apex Financial Services (Mauritius) Ltd[1]***, the Delhi bench of the ITAT has ruled that under the India-Mauritius Double Taxation Avoidance Agreement ("**DTAA**"), taxation of capital gains arising on sale of units of 'equity-oriented mutual funds' cannot be equated with sale of 'shares'; gains from transfer of the former are not taxable under the DTAA in terms of the unambiguous language of Article 13(3A).

Factual background & assessment proceedings

The assessee, a Mauritius based company registered as Foreign Institutional Investor with SEBI, was carrying on investment activity in India. In assessment year 2022-23, the assessee earned capital gains of Rs.593,48,24,274 from sale of equity-oriented mutual funds in India, which was claimed as exempt from tax in

[1] ITA No.1963/Del/2025

India under Article 13(4) of the DTAA. The assessing officer, however, denied said exemption on the premise that when the assessee sells units of equity oriented mutual funds, it becomes the beneficiary of capital gains arising from the alienation of the underlying asset of investment, i.e., shares and therefore, gains from their sale should be treated as gains arising from the alienation of 'shares' under Article 13(3A) of the DTAA, making them taxable in India.

The Dispute Resolution Panel **("DRP")** upheld the view taken by the assessing officer, holding that entire capital gains arising from sale of equity oriented mutual funds are liable to be taxed, applying the doctrine of 'purposive construction'. The DRP allowed benefit of grandfathering clause in respect of sale of units acquired prior to 01.04.2017.

ITAT Ruling

The ITAT referring to the judgment of the Supreme Court in *Azadi Bachao Andolan[2]*, observed that where words used in the DTAA are clear and unambiguous, there is no need to resort to different rules

[2] 263 ITR 706 (SC)

for treaty interpretation; tax treaties are entered into at a political level and rules for interpretation of DTAA are different from rules for interpretation of domestic laws.

In that background, the ITAT observed that the amendment brought into Article 13 of the DTAA sought to grant the right to tax capital gains arising only from alienation of shares acquired after 01.04.2017 to the source state. The Tribunal also made reference to the Protocol which was signed between India and Mauritius, observing that the said Protocol confines itself to 'shares' and does not disturb the allocation of taxing rights in respect of other fiscal instruments like debentures, hybrid instruments, etc.

The ITAT further observed that since the term 'shares' is not defined in the DTAA, the same would derive its meaning from the Indian domestic laws. The ITAT analyzed the definition of 'shares' and 'securities' given under the Companies Act, 2013 and the Securities Contracts (Regulation) Act, 1956 respectively and observed that under Indian domestic laws, shares and mutual funds are distinct form of securities, basis following points of distinction:

- The Companies Act, 2013 governs all aspects with respect to 'shares', i.e., their issuance, types, shareholder rights, dividends, transferability, etc. In contrast, mutual funds in India are established in the form of a Trust under Indian Trust Act, 1882 in accordance with SEBI Regulations, 1996;
- Shares and mutual funds are different forms of securities; investments in both have significant differences in terms of the rights of investors, regulation, nature of return and taxability under the domestic laws.

Relying on various judgments[3], including of the Supreme Court in Apollo Tyres Ltd[4], wherein it was held that there was no specific provision providing that units in mutual funds and/ or bonds would be covered within the meaning of 'shares', the ITAT concluded that for the purposes of DTAA, the gain on sale of 'equity-oriented mutual funds' cannot be equated with alienation of 'shares'.

The ITAT, accordingly, reversed the view of the assessing officer and DRP, holding that capital gains arising from sale of units of equity-oriented mutual funds would not be taxable in India under Article 13(3A) of India-Mauritius DTAA.

[3] CIT vs Hertz Chemicals Ltd [2016] 386 ITR 39 (Bom); Vanguard Emerging Markets Stock Index Funds vs ACIT [2025] 172 taxmann.com 515 (Mum Trib.); ITO vs Satish Beharilal Raheja [2013] 37 taxmann.com 296 (Mum Trib.); DCIT (International Taxation) vs K.E. Faizal [2019] 108 taxmann.com 545 (Cochin Trib.))

[4] 255 ITR 273 (SC)