* **IN THE HIGH COURT OF DELHI AT NEW DELHI**

Date of decision: 18th NOVEMBER, 2026

IN THE MATTER OF:

\# **CNR No. DLHC010968542025**

\+ **ITA 720/2025**

COMMISSIONER OF INCOME TAX, INTERNATIONAL TAXATION-1, NEW DELHI .....Appellant

Through: Mr. Puneet Rai, SSC and Mr. Ashvini Kumar, JSC.

versus

EMERGING INDIA FOCUS FUNDS .....Respondent

Through: Mr. Ajay Vohra, Sr. Advocate with Mr. Samarth Chaudhari, Advocates.

CORAM:
HON'BLE MR. JUSTICE SUBRAMONIUM PRASAD
HON'BLE MS. JUSTICE RENU BHATNAGAR

JUDGMENT

1. The presentAppeal under Section 260A of the Income Tax Act, 1961(*hereinafter referred to as* **'IT Act'**)has been filed by the Appellant/Department for the Assessment Year 2022-23 against the Order dated 25.06.2025 passed by the learned Income Tax Appellate Tribunal **['ITAT']** in ITA No.1963/Del/2025.

2. The question which arises for consideration in this Appeal is whether the capital gains arising out of the units of equity-oriented mutual funds would be liable to be taxed in India under Article 13(3A) of theIndia-Mauritius Double Taxation Avoidance Agreement (*hereinafter referred to as* **'India-Mauritius DTAA'**).

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3. Shorn of unnecessary details, the facts of the case leading to the filing of the present Appeal are narrated below:

a) The Assessee is a foreign company and a tax resident of Mauritius. The Assessee is carrying on investment activity in India by way of investments in shares and debentures of Indian companies through recognised stock exchange in India. The Assessee has also obtained registration as a Foreign Institutional Investor from the Securities and Exchange Board of India (*hereinafter referred to as* "**SEBI**"). The Assessee collects money from investors from all over the world and invests the same as per their investment objective as defined in the Private Placement Memorandum (*hereinafter referred to as* '**PPM**'). The investments of the Assessee are only in SEBI-registered mutual funds.

b) The Assessee, *vide* its return of income for the Assessment Year 2022-23 on 13.10.2022, declared total income of Rs.5,460/- and claimed capital gain income of Rs. 5,93,48,24,274/- as exempt under Article 13 of theIndia-Mauritius DTAA on account of sale of units of equity-oriented mutual funds.The case of the Assessee was selected for scrutiny underComputer Assisted Scrutiny Selection(*hereinafter referred to as* '**CASS**'), and a Notice under Section 143(2) of the IT Act dated 31.05.2023 was issued to the Assessee. Thereafter, the Assessing Officer passed a draft Assessment Order dated 28.03.2024 holding that out of the total capital gain of Rs.5,93,48,24,274/-, the capital gains of Rs.3,85,76,35,779/- were held to be covered under Article 13(3A) of the India-Mauritius DTAA and hence, taxable. The Assessing Officer held that when the Assessee sells the equity-

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oriented mutual funds, it becomes the beneficiary of capital gains arising out of the alienation of the underlying asset of investment, i.e.,equity shares. Therefore, since the Assessee has underlying assets of transactions as equity, 65% of the total capital gains, i.e. Rs. 385,76,35,779/-, is covered under Article 13(3A) of the India-Mauritius DTAA as the underlying asset in the transaction is shares and is taxable.

c) The Assessee, thereafter, filed objections before the learnedDispute Resolution Panel (*hereinafter referred to as* '**DRP**'), stating that the capital gains arising out of sale of units of equity-oriented mutual funds are notcovered under Article 13(3A) of the India-Mauritius DTAA, since the said clause isapplicable only on account of alienation of shares and not units of mutual funds. It was the case of the Assessee that it is covered under Article 13(4) of the India-Mauritius DTAA and is, thereby, exempted from tax in India. Thelearned DRP,*vide*the Order dated 03.12.2024, decided the issues against the Assessee. The learned DRP held that the intent of the legislature was always to treat units of equity-oriented mutual funds as equivalent to equity shares since they carry inherent characteristics of equity shares and, therefore, the Assessing Officer was correct in holding that the units of equity-oriented mutual funds are in the nature of equity shares and therefore, the provisions of Article 13(3A) of the India-Mauritius DTAA are applicable to the facts of the Assessee as against the benefit of Article 13(4) of the India-Mauritius DTAA incorrectly claimed by the Assessee. In fact, the learned DRP was of the opinion that the Assessing Officerwas not correct in holding that

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only65%, i.e., the minimum equity investment percentage, is taken to calculate the CapitalGain arising out of shares. The Assessing Officer thus taxed only capital gains of Rs.3,85,76,35,779/- out of the total capital gains of Rs. 5,93,48,24,274/- earned by the Assessee from equity-oriented mutual funds. The learned DRP held that once units of equity-oriented mutual funds were held to be shares, the entire capital gains would be liable to be taxed as per Article 13(3A) of the India-Mauritius DTAA.

d) The said Order dated 03.12.2024 passed by the learned DRP was the subject matter of challenge before the learned ITAT.

e) Before the learned ITAT, the ground taken by the Assessee was that equity-oriented mutual funds will not be covered under Article 13(3A) of the India-Mauritius DTAA as what the Assessee holds are units and not shares. The learned ITAT held that Article 13(3A) of the India-Mauritius DTAA applies only to alienation of shares and, thereafter, went on to the definition of shares given in Section 2(84) of the Companies Act, 2013 (*hereinafter referred to as* 'Companies Act'), which defines "share" as a share in the share capital of a company and includes stock, and it represents the interest of a shareholder in the company, for the purposes of liability and dividend. The learned ITAT thereafter placed reliance upon the definition of "securities" under Section 2(h) of the Securities Contracts (Regulation) Act, 1956 (*hereinafter referred to as* '**SCA**'),which states that "securities" include (i) shares, scrips, stocks, bonds, debentures, debenture stock or other marketable securities of a like nature in or of any incorporated company. The learned ITAT also

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relied upon Section 2(da) of the SCA, which states that "pooled investment vehicle" means a fund established in India in the form of a trust or otherwise, such as a mutual fund, alternative investment fund, collective investment scheme or a business trust as defined in Section 2(13A) of the IT Act and registered with SEBI, or such other fund, which raises or collects monies from investors and invests such funds in accordance with such regulations as may be made by SEBI in this behalf.

f) The learned ITAT was, therefore, of the opinion that mutual funds in India are established in the form of a Trust under the Indian Trusts Act, 1882. The money collected under the mutual fundscheme is invested by professional fund managers in stocks andbonds, etc., in line with a scheme's investment objective.The income/gains generated from this collective investment scheme are distributed proportionately amongst the investors, after deducting applicable expenses and levies, by calculating a scheme's Net Asset Value (*hereinafter referred to as* '**NAV**'). The mutual fund charges a small fee for this purpose. The learned ITAT was of the opinion that under the Indian Laws, the shares and mutual funds are both different forms of securities and investmentshaving significant differences in terms of the rights of investors, regulations, nature of return and taxability under the domestic laws. The learned ITAT, therefore,*vide*the Order dated 25.06.2025, while setting aside the opinions of the learned DRP and Assessing Officer, held that the sale of units of mutual funds will not come under Article 13(3A) of the India-Mauritius DTAA.

4. It is this Order dated 25.06.2025 passed by the learned ITAT which is

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under challenge in the present Appeal.

5. It is the contention of the learned Counsel appearing for the Appellant/Department that equity-oriented mutual funds will fall under Article 13(3A) of the India-Mauritius DTAA as equity-oriented mutual funds primarily consist of equityshares and, therefore, the mutual fund units have tobe treated akin to theequity shares.It is further argued by the Appellant/Department that the Rule of Purposive interpretation has to be applied to read Article 13(3A) of the India-Mauritius DTAA. It is the case of the Appellant/Department that the Assessee derived the capital gains from the sale of equity-oriented mutual funds whose underlying assets are equity shares in Indian companies. Therefore, as a necessary corollary, the gain arising out of the sale of such equity-oriented units essentially arises from the alienation of shares and is covered under Article 13(3A) of the India-Mauritius DTAA.

6. *Per contra*, learned Senior Counsel appearing for the Assessee supports the findings of the learned ITAT and placed reliance upon Article 13(3A) of the India-Mauritius DTAA, Section 2(84) of the Companies Act, Section 2(q) of the Securities and Exchange Board of India (Mutual Funds) Regulations, 1996(*hereinafter referred to as* '**SEBI Regulations**') and Section 2(h) of the SCA to contend that mutual funds are not shares.

7. Heard learned Counsel appearing for the Parties and perused the material on record.

8. Article 13 of the India-Mauritius DTAA reads as under:

"ARTICLE 13
CAPITAL GAINS

1. Gains from the alienation of immovable property, as defined in paragraph (2) of article 6, may be taxed in

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the Contracting State in which such property is situated.

2. Gains from the alienation of movable property forming part of the business property of a permanent establishment which an enterprise of a Contracting State has in the other Contracting State or of movable property pertaining to a fixed base available to a resident of a Contracting State in the other Contracting State for the purpose of performing independent personal services, including such gains from the alienation of such a permanent establishment (alone or together with the whole enterprise) or of such a fixed base, may be taxed in that other State.

3. Notwithstanding the provisions of paragraph (2) of this article, gains from the alienation of ships and aircraft operated in international traffic and movable property pertaining to the operation of such ships and aircraft, shall be taxable only in the Contracting State in which the place of effective management of the enterprise is situated.

[3A. Gains from the alienation of shares acquired on or after 1st April 2017 in a company which is resident of a Contracting State may be taxed in that State.

3B. However, the tax rate on the gains referred to in paragraph 3A of this Article and arising during the period beginning on 1st April, 2017 and ending on 31st March, 2019 shall not exceed 50% of the tax rate applicable on such gains in the State of residence of the company whose shares are being alienated;]

[4. Gains from the alienation of any property other than that referred to in paragraphs 1, 2, 3 and 3A shall be taxable only in the Contracting State of which the alienator is a resident.]

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> *5. For the purposes of this article, the term "alienation" means the sale, exchange, transfer, or relinquishment of the property or the extinguishment of any rights therein or the compulsory acquisition thereof under any law in force in the respective Contracting States."*

9. A perusal of Article 13(3A) of the India-Mauritius DTAA shows that the only gains from the alienation of shares acquired on or after 01.04.2017 in a company which is resident of a Contracting State may be taxed in that State and therefore, such income can be taxed in Mauritius and not in India. Article 13(4) of the India-Mauritius DTAA shows that gains from the alienation of any property other than that referred to in paragraphs 1 to 3 and 3A shall be taxable only in the Contracting State of which the alienator is a resident.

10. The term 'Contracting State' has been defined under Article 3(1)(c) of the India-Mauritius DTAA which reads as under:

> *"3(1)(c) the terms "a Contracting State" and "the other Contracting State" mean India or Mauritius as the context requires."*

11. The term 'Securities' has been defined under Regulation 2(h) of the SCA, which reads as under:

> *"(h) "securities" include—*
>
> *(i) shares, scrips, stocks, bonds, debentures, debenture stock or other marketablesecurities of a like nature in or of any incorporated company or other bodycorporate;*
>
> *(ia) derivative;*
>
> *(ib) units or any other instrument issued by any*

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collective investment scheme tothe investors in such schemes;

(ic)security receipt as defined in clause (zg) of section 2 of the Securitisation andReconstruction of Financial Assets and Enforcement of Security Interest Act,2002;

(id) units or any other such instrument issued to the investors under anymutual fund scheme;

(ii) Government securities;

(iia) such other instruments as may be declared by the Central Government to besecurities; and

(iii) rights or interest in securities;"

12. The term 'mutual fund' has been defined under Regulation 2(q) of the SEBI Regulations, which reads as under:

"2(q) "mutual fund" means a fund established in the form of a trust to raise monies through the sale of units to the public or a section of the public under one or more schemes for investing in securities, money market instruments, gold or gold related instruments, silver or silver related instruments, real estate assets and such other assets and instruments as may be specified by the Board from time to time:

Provided that infrastructure debt fund schemes may raise monies through private placement of units, subject to conditions specified in these regulations:

Provided further that mutual fund schemes investing in exchange traded commodity derivatives may hold the underlying goods in case of physical settlement of such contracts.

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[(qa) "NAV" or "Net Asset Value" shall mean the value computed in the manner provided in sub-regulation (1) of regulation 48 of these regulations;]

[qb]) "networth" means the aggregate of the paid up capital and free reserves after deducting therefrom, miscellaneous expenditure to the extent not written off or adjusted or deferred revenue expenditure, intangible assets and accumulated losses;]"

13. The way equity shares and mutual funds are to be taxed is stated under Section 10(38) of the IT Act, which reads as under:

"(38) any income arising from the transfer of a long-term capital asset, being an equity share in a company or a unit of an equity oriented fund or a unit of a business trust where—

(a) the transaction of sale of such equity share or unit is entered into on or after the date on which Chapter VII of the Finance (No. 2) Act, 2004 comes into force; and

(b)such transaction is chargeable to securities transaction tax under that Chapter :

Provided that the income by way of long-term capital gain of a company shall be taken into account in computing the book profit and income-tax payable under section 115JB :

Provided also that nothing contained in sub-clause (b) shall apply to a transaction undertaken on a recognised stock exchange located in any International Financial Services Centre and where the consideration for such transaction is paid or payable in foreign currency:

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Provided also that nothing contained in this clause shall apply to any income arising from the transfer of a long-term capital asset, being an equity share in a company, if the transaction of acquisition, other than the acquisition notified by the Central Government in this behalf, of such equity share is entered into on or after the 1st day of October, 2004 and such transaction is not chargeable to securities transaction tax under Chapter VII of the Finance (No. 2) Act, 2004 (23 of 2004):

Provided also that nothing contained in this clause shall apply to any income arising from the transfer of long-term capital asset, being an equity share in a company or a unit of an equity oriented fund or a unit of a business trust, made on or after the 1st day of April, 2018.

Explanation.—For the purposes of this clause,—

(a)"equity oriented fund" means a fund—

(i)where the investible funds are invested by way of equity shares in domestic companies to the extent of more than sixty-five per cent of the total proceeds of such fund; and

(ii)which has been set up under a scheme of a Mutual Fund specified under clause (23D):

Provided that the percentage of equity shareholding of the fund shall be computed with reference to the annual average of the monthly averages of the opening and closing figures;

(b)"International Financial Services Centre" shall have the same meaning as assigned to it in clause (q) of section 2 of the Special Economic Zones Act, 2005 (28 of 2005);

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> *(c)"recognised stock exchange" shall have the meaning assigned to it in clause (ii) of the Explanation 1 to sub-section (5) of section 43;"*

14. A perusal of the explanation to the aforesaid Section shows that equityoriented fund means a fund where the investible funds are invested by way of equity shares in domestic companies to the extent of more than sixty-five per cent of the total proceeds of such fund.

15. The question to be considered would, therefore, be whether sale of units of mutual fund of a company which is a resident of Mauritius would be saved from the tax under Section 10(38) of the IT Act in India or not.

16. It is trite that the holder of a mutual fund is not an owner of equity share in a company. Regulation 2(q) of the SEBI Regulationsstates"mutual fund" means a fund established in the form of a trust to raise monies through the sale of units to the public or a section of the public under one or more schemes for investing in securities, money market instruments, gold or gold related instruments, silver or silver related instruments, real estate assets and such other assets and instruments as may be specified by the Board from time to time. The term 'unit' has been defined in Regulation 2(z) of the SEBI Regulations, which reads as under:

> *"(z) "unit" means the interest of the unit holders in a scheme, which consists of each unit representing one undivided share in the assets of a scheme;"*

17. A unit holder of a mutual fund is, therefore, not a shareholder of the company. The unit holder only holds a unit in a fund which invests in shares or in any other securities. The unit holder does not have any rights and liabilities of the shareholder. Since the term 'mutual fund' is specifically

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defined, both countries omitted the use of the word mutual under Article 13(3A) of the India-Mauritius DTAA. It can at best come under Article 13(4) of the India-Mauritius DTAA, thereby being liable for tax only in Mauritius and not in India.

18. Section 10(38) of the IT Act is applicable, which indicates that there is a difference between equity shares and equity-oriented mutual funds and, therefore, both are to be treated separately.

19. The Apex Court in Apollo Tyres Ltd. v. CIT, **(2002) 9 SCC 1**, while dealing with units of UTI, held that units of UTI cannot be construed to be shares under Section 73 of the Contract Act. The Apex Court observed as under:

> ***"13.*** *Relying on the above provision of the UTI Act, the Revenue contends that if UTI is a company and income from its units is dividend then ipso facto the units will have to be shares, therefore, the business of purchase and sale of units conducted by the assessee Company will have to be deemed to be a business in shares which business, according to the Revenue, attracts Explanation to Section 73. On this basis, it is contended that the business of purchase and sale of units by the assessee Company amounts to a business of speculation. Both the Tribunal and the High Court have considered this argument as also the effect of Section 32(3) of the UTI Act and have come to the conclusion that the provision of the said Act is limited for the purpose of assessment of dividend income under the Act, and for deduction of tax at source. They have held that the legal fiction created by Section 32(3) of the UTI Act cannot be carried any further. We have examined the provisions of the UTI Act and we are of the opinion that even though the said section creates a fiction to make UTI a deemed company and distribution of income received by the unit-holder a deemed dividend, by virtue of these deemed provisions,*

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it cannot be said that it also makes the unit of UTI a deemed share. In our opinion, a deeming provision of this nature as found in Section 32(3) should be applied for the purpose for which the said deeming provision is specifically enacted, which in the present case is confined only to deeming UTI as a company and deeming the income from the units as a dividend. If as a matter of fact, the legislature had contemplated making the units as also a deemed share then it would have stated so. In the absence of any such specific deeming in regard to the units as shares, it would be erroneous to extend the provisions of Section 32(3) of the UTI Act to the units of UTI for the purpose of holding that the unit is a share. For these reasons, we are in agreement with the finding of the High Court on this point also."

20. Article 13(3A) of the India-Mauritius DTAA only sought to cover gains arising out of alienation of shares, which are to be taxed in India. Article 13(4) of the India-Mauritius DTAA provides that gains arising out of alienation of any property can be taxed only in Mauritius. The purport of the Double Taxation Avoidance Agreement entered into between the Government of India and the Government of Mauritius is toavoid double taxation and the prevention of fiscal evasion with respect to taxes on income and capital gains and for the encouragement of mutual trade and investment. The provisions, therefore, have to be read very strictly and the argument of the learned Counsel for the Appellant/Department that purposive interpretation has to be applied cannot be accepted. Both the countries were certain as to what should be taxed in India and what should be taxed in Mauritius, and for that purpose Article 13(3A) and Article 13(4)of the India-Mauritius DTAA specifically state which categories of incomeare subject to taxation in India and which are subject to taxation in Mauritius.

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21. It is apparent that the true intention of the contracting nations was to gain taxes arising out of the transaction of shares in Mauritius only and not in India, and for any other property, it was agreed that the same will be taxed only in the Contracting State of which the alienator is a resident and in this case it isMauritius. Each Agreement entered into by the Republic of India with other countries will have different provisions and, therefore, when the Contracting States intended and specifically allocated taxing rights, the finding of the learned ITAT that one will have to look at the underlying sale of shares cannot be accepted. As stated earlier, the Assessee is not a shareholder in any of the companies, and it only holds units of shares.

22. In view of the above, the question of law is answered in favour of the Assessee.

23. Resultantly, the Appeal is dismissed, along with pending application(s), if any.

SUBRAMONIUM PRASAD, J

RENU BHATNAGAR, J

NOVEMBER 18, 2026
S. Zakir

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