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Can India Tax Mutual Fund Gains of NRIs? Insights from the case of Anushka Sanjay Shah v. ITO and the DTAA Landscape

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The recent decision of the Income Tax Appellate Tribunal (Mumbai) ("**ITAT**") in ***Anushka Sanjay Shah v. ITO***[i] *("**Shah's Case**")* has brought fresh attention to the increasingly litigious issue of capital gains taxation for non-resident investors in Indian mutual fund units.

At the heart of the matter is whether such capital gains, derived by tax residents of countries with which India has a Double Taxation Avoidance Agreement ("**DTAA**") are liable to tax in India.



The Dispute, the Arguments and the Ruling

Anushka Shah ("**Assessee**"), a tax resident of Singapore, earned INR 1.35 crores as short-term capital gains through the redemption of Indian equity and debt mutual fund units. She claimed exemption from Indian capital gains tax under Article 13 (5) of the India–Singapore DTAA which deals with "Capital Gains" and provides as follows:

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

Paragraphs 1 through 3 of Article 13 of the India–Singapore DTAA deal with *inter alia* capital gains arising from alienation of immovable property, business assets linked to a permanent establishment, and ships or aircraft. Paragraphs 4A and 4B, meanwhile, concern gains from the alienation of "*shares*" in a company— with different treatments depending on whether the shares were acquired before or after 1 April 2017. The Assessee argued that mutual fund units do not fall within these carve-outs and that they constitute a separate category of asset and therefore covered by the residuary clause under Article 13(5). By this logic, it was argued that such gains are taxable only in Singapore, the state of residence of the Assessee and not in India.

Additionally, Section 90(2) of the Income-tax Act, 1961 ("**IT Act**") which entitles taxpayers to rely on treaty provisions where they are more beneficial than domestic law further bolstered the Assesses's claim. Section 90(2) is extracted herein below for ready reference:

> *"Where the Central Government has entered into an agreement with the Government of any country outside India or specified territory outside India, as the case may be, under sub-section (1) for granting relief of tax, or as the case may be, avoidance of double taxation, then, in relation to the assessee to whom such agreement applies**, the provisions of this Act shall apply to the extent they are more beneficial to that assessee**."*

The Assessing Officer (AO) rejected these arguments (which view was further endorsed by the Dispute Resolution Panel) asserting that the mutual fund units derived value from assets located in India and hence fell within the source rule of section 9(1)(i) of the IT Act[ii]. Accordingly, the AO argued that such capital gains are taxable in India even if the Assessee was a non-resident.

However, on appeal, the ITAT (Mumbai) agreed with the Assessee and ruled that the capital gains in question were not taxable in India as units of a mutual funds could not be considered as "*shares*", and the residuary clause i.e., Article 13(5) of the Singapore-India DTAA was applicable.

Judicial Precedents: Mutual Fund Units ≠ Shares

The ITAT's reasoning in Shah's case aligns closely with earlier decisions, most notably *Satish Beharilal Raheja v. ITO*[iii], where the Tribunal considered an identically worded residual clause in Article 13(6) of the India–Switzerland DTAA. There, the ITAT Mumbai held that mutual fund units could not be treated as "*shares*" relying on the Supreme Court's ruling in *Apollo Tyres Ltd. v. CIT*[iv], which held that units of Unit Trust of India (UTI) were not shares. In *Apollo Tyres*, the Court held that:

> "*We have examined the provisions of the UTI Act and we are of the opinion that even though the said Section (Section 32(3) of the UTI Act) creates a fiction to make the UTI as a deemed company and distribution of income received by the unit holder as a deemed dividend, by virtue of these deemed provisions, it cannot be said that it also makes the unit of the UTI a deemed share. In our opinion, a deeming provision of this nature as found in Section 32 (3) (of the UTI Act) 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 the 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.*"

Additionally, in Shah's case, the ITAT relied heavily on the reasoning in *DCIT v. K.E. Faizal*[v] of ITAT-Cochin, which dealt with a similar issue under the India–UAE DTAA. The ITAT (Cochin) in that case noted that Article 13(4)[vi] of the India–UAE DTAA applies only if the asset being transferred qualifies as a "*share*" under Indian law. It was observed that the term "*share*" is not defined in the India–UAE DTAA, and Article 3(2) of the treaty directs that undefined terms be construed according to the domestic law of the country imposing the tax. Accordingly, the Tribunal went on to look at, section 2(84) of the Companies Act, 2013 ("**Companies Act**") which defines a share as "*a share in the share capital of a company*" and the term "*company*" refers only to entities incorporated under the Companies Act or similar legislation. By contrast, mutual funds in India are established under the SEBI (Mutual Funds) Regulations, 1996, and structured as trusts, not companies. The ITAT (Cochin) therefore held that, units issued by mutual funds cannot be classified as "*shares*" under the Companies Act. The Tribunal also drew from the Securities Contracts (Regulation) Act, 1956, where both "*shares*" and "*mutual fund units*" are separately listed under the definition of "*securities*," reinforcing that the two are legally distinct instruments.

Notably, most recently in *Saket Kanoi v. DCIT*[vii], the ITAT (Delhi) while dealing with a similar case, while interpreting the India-UAE DTAA, reinforced the principle that treaty relief cannot be denied simply because the country where the assessee is a resident (in this case the UAE) does not impose personal income tax.

The ruling in Shah's case therefore appears to consolidate a growing line of decisions that are unified in some core principles:

(a) Taxation in case of a non-resident is subject to the provisions of relevant DTAAs.

(b) Mutual fund units are not "*shares*" in a company, and therefore fall in the residuary clause of several DTAAs (including Singapore, UAE and Switzerland) where taxation on gains will be done in terms of the law of the contracting state where the assessee is a resident.

(c) Section 90(2) of the IT Act allows a taxpayer to invoke the provisions of DTAA over domestic law especially when they are more beneficial.

Conclusion

Over the last few years, several ITAT benches have distinguished between mutual fund units and shares, thereby creating a more predictable regime. However, much will still turn on the specific terms of the applicable tax treaty and the structure of the investment.

Investors seeking treaty protection must be able to clearly establish their tax residency and the precise nature of their holdings. As more such cases are adjudicated, we can expect finer distinctions to emerge—particularly around what qualifies as a "share," what falls within a treaty's residuary clause, and when treaty relief can meaningfully be invoked.

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[i] Judgment dated 26.03.2025, IT(IT) A No. 174/MUM/2025

[ii] As per section 5(2) read with section 9(1)(i) of the IT Act, transfer of a capital asset situated in India shall be deemed to accrue or arise in India.

[iii] (2013) 145 ITD 29 (Mum)

[iv] AIR 2002 SC 213

[v] Judgement dated 08.07.2019, ITA No. 423/Coch/2018

[vi] Article 13(4) of the India-UAE DTAA provides that income arising to a resident of the UAE from the transfer of shares in an Indian company other than those specifically covered within the ambit of other paragraphs of Article 13, may be taxed in India.

[vii] Judgement dated 23.10.2024, ITA No. 3243/Del/2023

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